

Edgar Filing: Artisan Partners Asset Management Inc. - Form 10-Q

Artisan Partners Asset Management Inc.
Form 10-Q
May 02, 2018
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-Q

(Mark
One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE
ACT OF 1934
FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2018

OR
 TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE
ACT OF 1934
FOR THE TRANSITION PERIOD FROM TO

Commission file number: 001-35826

Artisan Partners Asset Management Inc.
(Exact name of registrant as specified in its charter)

Delaware 45-0969585
(State or other jurisdiction of (I.R.S. Employer
incorporation or organization) Identification No.)

875 E. Wisconsin Avenue, Suite 800 53202
Milwaukee, WI
(Address of principal executive offices) (Zip Code)

(414) 390-6100
(Registrant's telephone number, including area code)

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 (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and “emerging growth company” in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer
(Do not
check if a
Non-accelerated filer smaller reporting company
Smaller reporting
company)
Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

The number of outstanding shares of the registrant’s Class A common stock, par value \$0.01 per share, Class B common stock, par value \$0.01 per share, and Class C common stock, par value \$0.01 per share, as of April 27, 2018 were 53,936,262, 8,802,249 and 14,249,130, respectively.

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Except where the context requires otherwise, in this report, references to the "Company", "Artisan", "we", "us" or "our" refer to Artisan Partners Asset Management Inc. ("APAM") and its direct and indirect subsidiaries, including Artisan Partners Holdings LP ("Artisan Partners Holdings" or "Holdings"). On March 12, 2013, APAM closed its initial public offering and related corporate reorganization. Prior to that date, APAM was a subsidiary of Artisan Partners Holdings.

Forward-Looking Statements

This report contains, and from time to time our management may make, forward-looking statements within the meaning of the safe harbor provisions of the U.S. Private Securities Litigation Reform Act of 1995. Statements regarding future events and our future performance, as well as management's current expectations, beliefs, plans, estimates, or projections relating to the future, are forward-looking statements within the meaning of these laws. In some cases, you can identify these statements by forward-looking words such as "may", "might", "will", "should", "expects", "intends", "plans", "anticipates", "believes", "estimates", "predicts", "potential" or "continue", the negative of these terms and comparable terminology. These forward-looking statements are only predictions based on current expectations and projections about future events. Forward-looking statements are subject to a number of risks and uncertainties, and there are important factors that could cause actual results, level of activity, performance, actions or achievements to differ materially from the results, level of activity, performance, actions or achievements expressed or implied by the forward-looking statements. These factors include: the loss of key investment professionals or senior management, adverse market or economic conditions, poor performance of our investment strategies, change in the legislative and regulatory environment in which we operate, operational or technical errors or other damage to our reputation and other factors disclosed in the Company's filings with the Securities and Exchange Commission, including those factors listed under the caption entitled "Risk Factors" in Item 1A of the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2017, filed with the SEC on February 21, 2018, which is accessible on the SEC's website at www.sec.gov. We undertake no obligation to publicly update any forward-looking statements in order to reflect events or circumstances that may arise after the date of this report, except as required by law.

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Forward-looking statements include, but are not limited to, statements about:

- our anticipated future results of operations;
 - our potential operating performance and efficiency;
 - our expectations with respect to future levels of assets under management, including the capacity of our strategies and client cash inflows and outflows;
 - our expectations with respect to industry trends and how those trends may impact our business;
 - our financing plans, cash needs and liquidity position;
 - our intention to pay dividends and our expectations about the amount of those dividends;
 - our expected levels of compensation of our employees, including equity compensation;
 - our expectations with respect to future expenses and the level of future expenses;
 - our expected tax rate, and our expectations with respect to deferred tax assets; and
 - our estimates of future amounts payable pursuant to our tax receivable agreements.
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Part I — Financial Information

Item 1. Unaudited Consolidated Financial Statements

ARTISAN PARTNERS ASSET MANAGEMENT INC.

Unaudited Condensed Consolidated Statements of Financial Condition

(U.S. dollars in thousands, except per share amount)

| | March 31, 2018 | December 31, 2017 |
|--|-------------------|----------------------|
| ASSETS | | |
| Cash and cash equivalents | \$ 200,831 | \$ 137,286 |
| Accounts receivable | 74,758 | 76,693 |
| Investment securities | 5,298 | 4,978 |
| Property and equipment, net | 20,262 | 21,025 |
| Deferred tax assets | 440,383 | 429,212 |
| Restricted cash | 629 | 629 |
| Prepaid expenses and other assets | 12,295 | 13,364 |
| Assets of consolidated investment products | | |
| Cash and cash equivalents | 44,783 | 21,881 |
| Accounts receivable and other | 35,367 | 16,768 |
| Investment assets, at fair value | 119,577 | 115,319 |
| Total assets | \$ 954,183 | \$ 837,155 |
| LIABILITIES, REDEEMABLE NONCONTROLLING INTERESTS, AND STOCKHOLDERS' EQUITY | | |
| Accounts payable, accrued expenses, and other | \$ 24,515 | \$ 23,019 |
| Accrued incentive compensation | 68,490 | 2,911 |
| Borrowings | 199,171 | 199,129 |
| Amounts payable under tax receivable agreements | 400,467 | 385,413 |
| Liabilities of consolidated investment products | | |
| Accounts payable, accrued expenses, and other | 27,213 | 8,180 |
| Investment liabilities, at fair value | 53,755 | 47,857 |
| Total liabilities | 773,611 | 666,509 |
| Commitments and contingencies | | |
| Redeemable noncontrolling interests | 81,652 | 62,581 |
| Common stock | | |
| Class A common stock (\$0.01 par value per share, 500,000,000 shares authorized, 53,483,634 and 50,463,126 shares outstanding at March 31, 2018 and December 31, 2017, respectively) | 535 | 505 |
| Class B common stock (\$0.01 par value per share, 200,000,000 shares authorized, 9,707,506 and 11,922,192 shares outstanding at March 31, 2018 and December 31, 2017, respectively) | 97 | 119 |
| Class C common stock (\$0.01 par value per share, 400,000,000 shares authorized, 13,796,501 and 13,184,527 shares outstanding at March 31, 2018 and December 31, 2017, respectively) | 138 | 132 |
| Additional paid-in capital | 89,001 | 147,910 |
| Retained earnings (deficit) | 4,040 | (37,870) |
| Accumulated other comprehensive income (loss) | (739) | (873) |
| Total Artisan Partners Asset Management Inc. stockholders' equity | 93,072 | 109,923 |
| Noncontrolling interest - Artisan Partners Holdings | 5,848 | (1,858) |
| Total stockholders' equity | 98,920 | 108,065 |
| Total liabilities, redeemable noncontrolling interests, and stockholders' equity | \$ 954,183 | \$ 837,155 |
| The accompanying notes are an integral part of the consolidated financial statements. | | |

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ARTISAN PARTNERS ASSET MANAGEMENT INC.

Unaudited Consolidated Statements of Operations

(U.S. dollars in thousands, except per share amounts)

| | For the Three Months Ended March 31, | |
|--|---|------------|
| | 2018 | 2017 |
| Revenues | | |
| Management fees | \$211,966 | \$184,074 |
| Performance fees | 42 | — |
| Total revenues | \$212,008 | \$184,074 |
| Operating Expenses | | |
| Compensation and benefits | | |
| Salaries, incentive compensation and benefits | 105,224 | 93,249 |
| Pre-offering related compensation - share-based awards | — | 6,339 |
| Total compensation and benefits | 105,224 | 99,588 |
| Distribution, servicing and marketing | 7,009 | 7,374 |
| Occupancy | 3,925 | 3,506 |
| Communication and technology | 8,660 | 8,423 |
| General and administrative | 7,204 | 7,151 |
| Total operating expenses | 132,022 | 126,042 |
| Total operating income | 79,986 | 58,032 |
| Non-operating income (loss) | | |
| Interest expense | (2,776) | (2,881) |
| Net investment gain (loss) of consolidated investment products | 6,285 | — |
| Net investment income | 321 | 93 |
| Other non-operating income (expense) | 133 | 60 |
| Total non-operating income (loss) | 3,963 | (2,728) |
| Income before income taxes | 83,949 | 55,304 |
| Provision for income taxes | 12,285 | 12,749 |
| Net income before noncontrolling interests | 71,664 | 42,555 |
| Less: Net income attributable to noncontrolling interests - Artisan Partners Holdings | 26,052 | 22,760 |
| Less: Net income attributable to noncontrolling interests - consolidated investment products | 4,338 | — |
| Net income attributable to Artisan Partners Asset Management Inc. | \$41,274 | \$19,795 |
| Basic and diluted earnings per share | \$0.75 | \$0.37 |
| Basic and diluted weighted average number of common shares outstanding | 47,360,438 | 41,019,598 |
| Dividends declared per Class A common share | \$1.39 | \$0.96 |

The accompanying notes are an integral part of the consolidated financial statements.

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ARTISAN PARTNERS ASSET MANAGEMENT INC.

Unaudited Consolidated Statements of Comprehensive Income

(U.S. dollars in thousands)

| | For the Three Months Ended March 31, | |
|--|--|----------|
| | 2018 | 2017 |
| Net income before noncontrolling interests | \$71,664 | \$42,555 |
| Other comprehensive income (loss), net of tax | | |
| Unrealized gain (loss) on investment securities: | | |
| Unrealized gain (loss) on investment securities, net of tax of \$0 and (\$8), respectively | — | 56 |
| Less: reclassification adjustment for gain (loss) included in net income | — | 93 |
| Net unrealized gain (loss) on investment securities | — | (37) |
| Foreign currency translation gain (loss) | 632 | 206 |
| Total other comprehensive income (loss) | 632 | 169 |
| Comprehensive income | 72,296 | 42,724 |
| Comprehensive income attributable to noncontrolling interests - Artisan Partners Holdings | 26,291 | 23,058 |
| Comprehensive income attributable to noncontrolling interests - consolidated investment products | 4,338 | — |
| Comprehensive income attributable to Artisan Partners Asset Management Inc. | \$41,667 | \$19,666 |

The accompanying notes are an integral part of the consolidated financial statements.

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ARTISAN PARTNERS ASSET MANAGEMENT INC.

Unaudited Consolidated Statements of Changes in Stockholders' Equity

(U.S. dollars in thousands)

| | Class A Common stock | Class B Common stock | Class C Common stock | Additional paid-in capital | Retained earnings | Accumulated other comprehensive income (loss) | Non-controlling interest - Artisan Partners Holdings | Total stockholders' equity | Redeemable non-controlling interest |
|--|-------------------------------|----------------------------|----------------------------|----------------------------------|----------------------|---|--|----------------------------------|---|
| Balance at January 1, 2018 | \$505 | \$ 119 | \$ 132 | \$ 147,910 | \$(37,870) | \$ (873) | \$ (1,858) | \$ 108,065 | \$ 62,581 |
| Net income | — | — | — | — | 41,274 | — | 26,052 | 67,326 | 4,338 |
| Other comprehensive income - foreign currency translation | — | — | — | — | — | 429 | 203 | 632 | — |
| Other comprehensive income - available for sale investments, net of tax | — | — | — | — | 358 | (260) | — | 98 | — |
| Cumulative impact of changes in ownership of Artisan Partners Holdings LP, net of tax | — | — | — | (383) | — | (35) | 418 | — | — |
| Amortization of equity-based compensation | — | — | — | 10,043 | — | — | 4,357 | 14,400 | — |
| Deferred tax assets, net of amounts payable under tax receivable agreements | — | — | — | 3,271 | — | — | — | 3,271 | — |
| Issuance of Class A common stock, net of issuance costs | 6 | — | — | 21,293 | — | — | — | 21,299 | — |
| Forfeitures and employee/partner terminations | — | (11) | 11 | — | — | — | — | — | — |
| Issuance of restricted stock awards | 15 | — | — | (15) | — | — | — | — | — |
| Employee net share settlement | (1) | — | — | (1,210) | — | — | (594) | (1,805) | — |
| Exchange of subsidiary equity | 10 | (5) | (5) | — | — | — | — | — | — |
| Purchase of equity and subsidiary equity | — | (6) | — | (21,472) | — | — | — | (21,478) | — |
| Capital contributions | — | — | — | — | — | — | — | — | 14,733 |
| Distributions | — | — | — | — | — | — | (22,683) | (22,683) | — |
| Dividends | — | — | — | (70,436) | 278 | — | (47) | (70,205) | — |
| Balance at March 31, 2018 | \$535 | \$ 97 | \$ 138 | \$ 89,001 | \$ 4,040 | \$ (739) | \$ 5,848 | \$ 98,920 | \$ 81,652 |

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| | | | | | | | | |
|---|--------|--------|--------|------------|-----------|-----------|--------------|--------------|
| Balance at January 1, 2017 | \$ 421 | \$ 151 | \$ 171 | \$ 119,221 | \$ 13,395 | \$ (1,648 |) \$ (13,997 |) \$ 117,714 |
| Net income | — | — | — | — | 19,795 | — | 22,760 | 42,555 |
| Other comprehensive income - foreign currency translation | — | — | — | — | — | 126 | 80 | 206 |
| Other comprehensive income - available for sale investments, net of tax | — | — | — | — | — | (17 |) (19 |) (36 |
| Cumulative impact of changes in ownership of Artisan Partners Holdings LP, net of tax | — | — | — | (1,274 |)— | (237 |) 1,510 | (1 |
| Amortization of equity-based compensation | — | — | — | 11,024 | — | — | 7,806 | 18,830 |
| Deferred tax assets, net of amounts payable under tax receivable agreements | — | — | — | 19,987 | — | — | — | 19,987 |
| Issuance of Class A common stock, net of issuance costs | 56 | — | — | 162,024 | — | — | — | 162,080 |
| Issuance of restricted stock awards | 13 | — | — | (13 |)— | — | — | — |
| Employee net share settlement | — | — | — | (530 |)— | — | (400 |) (930 |
| Exchange of subsidiary equity | 2 | (2 |)— | — | — | — | — | — |
| Purchase of equity and subsidiary equity | — | (21 |) (35 |) (162,438 |)— | — | — | (162,494 |
| Distributions | — | — | — | — | — | — | (16,530 |) (16,530 |
| Dividends | — | — | — | (21,036 |) (19,594 |)— | (42 |) (40,672 |
| Balance at March 31, 2017 | \$ 492 | \$ 128 | \$ 136 | \$ 126,965 | \$ 13,596 | \$ (1,776 |) \$ 1,168 | \$ 140,709 |

The accompanying notes are an integral part of the consolidated financial statements.

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ARTISAN PARTNERS ASSET MANAGEMENT INC.

Unaudited Consolidated Statements of Cash Flows

(U.S. dollars in thousands)

| | For the Three Months Ended March 31, | |
|--|---|------------|
| | 2018 | 2017 |
| Cash flows from operating activities | | |
| Net income before noncontrolling interests | \$71,664 | \$42,555 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 1,265 | 1,257 |
| Deferred income taxes | 7,252 | 9,657 |
| Net investment income | (321) | (93) |
| Loss on disposal of property and equipment | 5 | 14 |
| Amortization of debt issuance costs | 114 | 112 |
| Share-based compensation | 14,400 | 18,830 |
| Net investment (gain) loss of consolidated investment products | (6,285) | — |
| Purchase of investments by consolidated investment products | (332,365) | — |
| Proceeds from sale of investments by consolidated investment products | 339,686 | — |
| Change in assets and liabilities resulting in an increase (decrease) in cash: | | |
| Accounts receivable | 1,935 | (3,661) |
| Prepaid expenses and other assets | 1,643 | 1,589 |
| Accounts payable and accrued expenses | 67,318 | 47,763 |
| Class B liability awards | — | (506) |
| Deferred lease obligations | (25) | 1,479 |
| Net change in operating assets and liabilities of consolidated investment products | 1,038 | — |
| Net cash provided by operating activities | 167,324 | 118,996 |
| Cash flows from investing activities | | |
| Acquisition of property and equipment | (301) | (353) |
| Leasehold improvements | (528) | (1,138) |
| Proceeds from sale of investment securities | — | 6,382 |
| Purchase of investment securities | — | (250) |
| Net cash provided by (used in) investing activities | (829) | 4,641 |
| Cash flows from financing activities | | |
| Partnership distributions | (22,683) | (16,530) |
| Dividends paid | (70,205) | (40,672) |
| Net proceeds from issuance of common stock | 21,478 | 162,494 |
| Payment of costs directly associated with the issuance of Class A common stock | (88) | (100) |
| Purchase of equity and subsidiary equity | (21,478) | (162,494) |
| Taxes paid related to employee net share settlement | (1,805) | (930) |
| Capital contributions to consolidated investment products | 14,733 | — |
| Net cash used in financing activities | (80,048) | (58,232) |
| Net increase (decrease) in cash and cash equivalents | 86,447 | 65,405 |
| Cash, cash equivalents and restricted cash | | |
| Beginning of period | 159,796 | 157,406 |
| End of period | \$246,243 | \$222,811 |
| Cash, cash equivalents and restricted cash as of the end of the period | | |
| Cash and cash equivalents | \$200,831 | \$222,182 |
| Restricted cash | 629 | 629 |

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| | | |
|---|-----------|-----------|
| Cash and cash equivalents of consolidated investment products | 44,783 | — |
| Cash, cash equivalents and restricted cash | \$246,243 | \$222,811 |

Supplementary information

Noncash activity:

| | | |
|--|----------|-----------|
| Establishment of deferred tax assets | \$18,325 | \$119,175 |
| Establishment of amounts payable under tax receivable agreements | 15,054 | 99,189 |

The accompanying notes are an integral part of the consolidated financial statements.

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ARTISAN PARTNERS ASSET MANAGEMENT INC.

Notes to Unaudited Consolidated Financial Statements

(U.S. currencies in thousands, except per share or per unit amounts and as otherwise indicated)

Note 1. Nature of Business and Organization

Nature of Business

Artisan Partners Asset Management Inc. (“APAM”), through its subsidiaries, is an investment management firm focused on providing high-value added, active investment strategies to sophisticated clients globally. APAM and its subsidiaries are hereafter referred to collectively as “Artisan” or the “Company”.

Artisan’s autonomous investment teams manage a broad range of U.S., non-U.S. and global investment strategies that are diversified by asset class, market cap and investment style. Strategies are offered through multiple investment vehicles to accommodate a broad range of client mandates. Artisan offers its investment management services primarily to institutions and through intermediaries that operate with institutional-like decision-making processes and have long-term investment horizons.

Organization

On March 12, 2013, APAM completed its initial public offering (the “IPO”). APAM was formed for the purpose of becoming the general partner of Artisan Partners Holdings LP (“Artisan Partners Holdings” or “Holdings”) in connection with the IPO. Holdings is a holding company for the investment management business conducted under the name “Artisan Partners”. The reorganization (“IPO Reorganization”) established the necessary corporate structure to complete the IPO while at the same time preserving the ability of the firm to conduct operations through Holdings and its subsidiaries.

As the sole general partner, APAM controls the business and affairs of Holdings. As a result, APAM consolidates Holdings’ financial statements and records a noncontrolling interest for the equity interests in Holdings held by the limited partners of Holdings. At March 31, 2018, APAM held approximately 69% of the equity ownership interest in Holdings.

Holdings, together with its wholly owned subsidiary, Artisan Investments GP LLC (“AIGP”), controls a 100% interest in Artisan Partners Limited Partnership (“APLP”), a multi-product investment management firm that is the principal operating subsidiary of Artisan Partners Holdings. APLP is registered as an investment adviser with the U.S. Securities and Exchange Commission under the Investment Advisers Act of 1940. APLP provides investment advisory services to separate accounts and pooled investment vehicles, including Artisan Partners Funds, Inc. (“Artisan Funds” or the “Funds”) and Artisan Partners Global Funds plc (“Artisan Global Funds”). Artisan Funds are a series of open-end, diversified mutual funds registered under the Investment Company Act of 1940, as amended. Artisan Global Funds is a family of Ireland-domiciled UCITS.

2018 Follow-On Offering

On February 27, 2018, APAM completed a registered offering of 644,424 shares of Class A common stock (the “2018 Follow-On Offering”) and utilized all of the proceeds to purchase an aggregate of 644,424 common units of Artisan Partners Holdings at a price per unit of \$33.33. The offering and subsequent purchase of units had the following impact on the consolidated financial statements:

• APAM received 644,424 GP units of Holdings, which increased APAM’s ownership interest in Holdings. See Note 7, “Noncontrolling interest - Holdings” for the financial statement impact of changes in ownership.

• APAM’s purchase of common units of Holdings with the proceeds resulted in an increase to deferred tax assets and amounts payable under the tax receivable agreements. See Note 11, “Income Taxes and Related Payments”.

Holdings Unit Exchanges

Limited partners of Artisan Partners Holdings are entitled to exchange partnership units (along with a corresponding number of shares of Class B or C common stock of APAM) for shares of Class A common stock from time to time (the “Holdings Common Unit Exchanges”). The following partnership units were exchanged for APAM Class A common stock during the three months ended March 31, 2018:

| Total | Class A | Class B | Class E |
|--------|---------|---------|---------|
| Common | Common | Common | Common |
| Units | Units | Units | Units |

Exchanged

Common units exchanged on March 1, 2018 958,288 499,222 449,066 10,000

The corresponding shares of APAM Class B and Class C common stock were immediately canceled upon exchange. The Holdings Common Unit Exchanges increased APAM's equity ownership interest in Holdings and resulted in an increase to deferred tax assets and amounts payable under the tax receivable agreements. See Note 11, "Income Taxes and Related Payments".

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Note 2. Summary of Significant Accounting Policies

Basis of presentation

The accompanying financial statements are unaudited. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, necessary for a fair statement of such consolidated financial statements have been included. Such interim results are not necessarily indicative of full year results.

The consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles (“U.S. GAAP”) for interim financial reporting and accordingly they do not include all of the information and footnotes required in the annual consolidated financial statements and accompanying footnotes.

The year-end condensed balance sheet data was derived from audited financial statements, but does not include all disclosures required by U.S. GAAP. As a result, the interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements included in APAM’s latest annual report on Form 10-K.

The accompanying financial statements were prepared in accordance with U.S. GAAP and related rules and regulations of the SEC. The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates or assumptions that affect the reported amounts and disclosures in the financial statements. Actual results could differ from these estimates or assumptions.

Principles of consolidation

Artisan’s policy is to consolidate all subsidiaries or other entities in which it has a controlling financial interest. The consolidation guidance requires an analysis to determine if an entity should be evaluated for consolidation using the voting interest entity (“VOE”) model or the variable interest entity (“VIE”) model. Under the VOE model, controlling financial interest is generally defined as a majority ownership of voting interests. Under the VIE model, controlling financial interest is defined as (i) the power to direct activities that most significantly impact the economic performance of the entity and (ii) the right to receive potentially significant benefits or the obligation to absorb potentially significant losses. Artisan generally consolidates VIEs in which it meets the power criteria and holds an equity ownership interest of greater than 10%. The consolidated financial statements include the accounts of APAM and all subsidiaries or other entities in which APAM has a direct or indirect controlling financial interest. All material intercompany balances have been eliminated in consolidation.

Artisan serves as the investment adviser to Artisan Funds, Artisan Global Funds and other investment products, including Artisan sponsored private funds. Artisan Funds and Artisan Global Funds are corporate entities the business and affairs of which are managed by their respective boards of directors. The shareholders of the funds retain voting rights, including rights to elect and reelect members of their respective boards of directors. Each series of Artisan Funds is a VOE and is separately evaluated for consolidation under the VOE model. The shareholders of Artisan Global Funds lack simple majority liquidation rights, and as a result, each sub-fund of Artisan Global Funds is evaluated for consolidation under the VIE model. Artisan sponsored privately offered funds are also evaluated for consolidation under the VIE model because third-party equity holders of the funds generally lack the ability to divest Artisan of its control of the funds.

From time to time, the Company makes investments in Artisan Funds, Artisan Global Funds, and Artisan sponsored private funds. If the investment results in a controlling financial interest, APAM consolidates the fund, and the underlying activity of the entire fund is included in Artisan’s Consolidated Financial Statements. As of March 31, 2018, Artisan has a controlling financial interest in two sub-funds of Artisan Global Funds and certain privately offered funds and, as a result, these funds are included in Artisan’s Consolidated Financial Statements. Because these consolidated investment products meet the definition of investment companies under U.S. GAAP, Artisan has retained the specialized industry accounting principles for investment companies in its Consolidated Financial Statements. See Note 6, “Variable Interest Entities and Consolidated Investment Products” for additional details.

Recent accounting pronouncements

Accounting standards adopted as of January 1, 2018

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers, which supersedes existing accounting standards for revenue recognition and creates a single framework. The guidance also changes the accounting for certain costs to obtain or fulfill a contract. The Company adopted ASU 2014-09 as of January 1, 2018, utilizing the modified retrospective method. There was no cumulative effect adjustment of applying the new revenue

standard and the comparative information has not been restated. There are no significant differences between the reported results under the revenue standard and what would have been reported under the previous revenue guidance, other than the disclosures included in Note 9, "Revenue From Contracts with Customers". The Company expects the impact of adopting the new revenue standard to be immaterial to its results on an ongoing basis.

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The application of ASU 2014-09 had no impact on the Consolidated Statement of Financial Condition as of March 31, 2018, as compared to the previous revenue recognition standard. The application of the new principal versus agent guidance resulted in presentation changes whereby certain costs are now reported on a gross basis, when the Company is acting as principal, and reported on a net basis, when the Company is acting as an agent. The new standard requires the entire amount of fee waivers and expense reimbursements to be presented net against revenue, which resulted in an \$11 thousand decrease in management fee revenue and a corresponding \$11 thousand decrease in general and administrative expenses within the Consolidated Statements of Operations for the three months ended March 31, 2018. Applying ASU 2014-09 had no impact to operating income or net income, as compared to applying the previous revenue recognition standard. Artisan did not apply any of the practical expedients in ASU 2014-09.

In January 2016, the FASB issued ASU 2016-01, Recognition and Measurement of Financial Assets and Financial Liabilities, which requires all equity investments to be measured at fair value with changes in the fair value recognized through net income. The Company adopted ASU 2016-01 as of January 1, 2018, utilizing the modified retrospective method. Upon adoption, the Company made a cumulative-effect adjustment to the Company's Consolidated Statements of Financial Condition, which resulted in a \$0.4 million decrease to accumulated other comprehensive income (loss) and a corresponding \$0.4 million increase to retained earnings (deficit). The application of ASU 2016-01 results in the recognition of the Company's unrealized gains (losses) on investment securities through net income. The Company recognized \$0.3 million of unrealized gains in net income for the three months ended March 31, 2018.

In November 2016, the FASB issued ASU 2016-18, Restricted Cash, to clarify guidance on the classification and presentation of restricted cash in the statement of cash flows. Restricted cash and restricted cash equivalents, including cash of consolidated investment products, is required to be included in cash and cash-equivalent balances in the statement of cash flows. The guidance is effective as of January 1, 2018, and requires retrospective application to all periods presented. The Consolidated Statements of Cash Flows includes a reconciliation to the line items on the Consolidated Statements of Financial Condition.

Accounting standards not yet adopted

In February 2016, the FASB issued ASU 2016-02, Leases, which introduces a lessee model that brings most leases on the balance sheet. The new guidance will be effective on January 1, 2019 and will require a modified retrospective approach to adoption. Early adoption is permitted. The Company is currently evaluating the impact of adoption on its Consolidated Financial Statements. The standard is expected to result in a significant increase in total assets and total liabilities, but will not have a significant impact on the Consolidated Statements of Operations.

Note 3. Investment Securities

The disclosures below include details of Artisan's investments, excluding money market funds and consolidated investment products. Investments held by consolidated investment products are described in Note 6, "Variable Interest Entities and Consolidated Investment Products". Artisan's investment securities as of December 31, 2017 consisted of the following:

| | Cost | Unrealized Gains | Unrealized Losses | Fair Value |
|-------------------|---------|---------------------|----------------------|------------|
| December 31, 2017 | | | | |
| Mutual funds | \$4,361 | \$ 617 | \$ | —\$ 4,978 |

Artisan's investments in mutual funds consist of investments in shares of Artisan Funds and Artisan Global Funds. As of January 1, 2018, the Company adopted ASU 2016-01, which requires all equity investments to be measured at fair value with changes in the fair value recognized through net income. As a result, the Company made a cumulative-effect adjustment to reclassify \$0.4 million of unrealized gains attributable to APAM from accumulated other comprehensive income (loss) to retained earnings (deficit). The remaining \$0.2 million of unrealized gains as of January 1, 2018 were attributable to noncontrolling interests. Effective January 1, 2018, unrealized gains and losses are recorded to net investment income in the statement of operations.

The table below presents the Company's unrealized gains and losses for the specified period that relate to investment securities held as of March 31, 2018.

| | For the three months ended March 31, 2018 |
|--|---|
| Net gains (losses) recognized on investment securities | \$ 321 |
| Less: Net realized gains (losses) recognized on investment securities sold during the period | \$ — |
| Unrealized gains (losses) recognized on investment securities held as of the end of the period | \$ 321 |

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Note 4. Fair Value Measurements

The table below presents information about Artisan’s assets and liabilities that are measured at fair value and the valuation techniques Artisan utilized to determine such fair value. The financial instruments held by consolidated investment products are excluded from the table below and are presented in Note 6, “Variable Interest Entities and Consolidated Investment Products”.

In accordance with ASC 820, fair value is defined as the price that Artisan would receive upon selling an investment in an orderly transaction to an independent buyer in the principal or most advantageous market for the investment. The following three-tier fair value hierarchy prioritizes the inputs used in measuring fair value:

• Level 1 – Observable inputs such as quoted (unadjusted) market prices in active markets for identical securities.

• Level 2 – Other significant observable inputs (including but not limited to quoted prices for similar instruments, interest rates, prepayment speeds, credit risk, etc.).

• Level 3—Significant unobservable inputs (including Artisan’s own assumptions in determining fair value).

The following provides the hierarchy of inputs used to derive fair value of Artisan’s assets and liabilities that are financial instruments as of March 31, 2018 and December 31, 2017:

| Assets and Liabilities at Fair Value | | | | |
|--------------------------------------|---------|---------|---------|--|
| Total | Level 1 | Level 2 | Level 3 | |

March 31, 2018

Assets

| | | | | |
|--------------------|----------|----------|------|---|
| Money market funds | \$68,823 | \$68,823 | \$ — | — |
| Mutual funds | 5,298 | 5,298 | — | — |

December 31, 2017

Assets

| | | | | |
|--------------------|----------|----------|------|---|
| Money market funds | \$26,727 | \$26,727 | \$ — | — |
| Mutual funds | 4,978 | 4,978 | — | — |

Fair values determined based on Level 1 inputs utilize quoted market prices for identical assets. Level 1 assets generally consist of money market funds, open-end mutual funds and UCITS funds. Cash maintained in demand deposit accounts is excluded from the table above.

Artisan’s policy is to recognize transfers in and transfers out of the valuation levels as of the beginning of the reporting period. There were no transfers between Level 1, Level 2 or Level 3 securities during the three months ended March 31, 2018 and 2017.

Note 5. Borrowings

Artisan’s borrowings consist of the following as of March 31, 2018 and December 31, 2017:

| | Maturity | Outstanding Balance | Interest Rate Per Annum |
|----------------------------|-------------|---------------------|-------------------------|
| Revolving credit agreement | August 2022 | \$ — | NA |
| Senior notes | | | |
| Series B | August 2019 | 50,000 | 5.32 % |
| Series C | August 2022 | 90,000 | 5.82 % |
| Series D | August 2025 | 60,000 | 4.29 % |
| Total borrowings | | \$ 200,000 | |

The fair value of borrowings was approximately \$204.9 million as of March 31, 2018. Fair value was determined based on future cash flows, discounted to present value using current market interest rates. The inputs are categorized as Level 2 in the fair value hierarchy, as defined in Note 4, “Fair Value Measurements”.

Interest expense incurred on the unsecured notes and revolving credit agreement was \$2.7 million and \$2.8 million for the three months ended March 31, 2018 and 2017, respectively.

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As of March 31, 2018, the aggregate maturities of debt obligations, based on their contractual terms, are as follows:

| | |
|------------|-----------|
| 2018 | \$— |
| 2019 | 50,000 |
| 2020 | — |
| 2021 | — |
| 2022 | 90,000 |
| Thereafter | 60,000 |
| Total | \$200,000 |

Note 6. Variable Interest Entities and Consolidated Investment Products

Artisan serves as the investment adviser for various types of investment products, consisting of both VIEs and VOEs. Artisan consolidates an investment product if it has a controlling financial interest in the entity. Any such entities are collectively referred to herein as consolidated investment products or CIPs.

As of March 31, 2018, Artisan is considered to be the primary beneficiary of two sub-funds of Artisan Global Funds and certain Artisan sponsored private funds related to two investment strategies for which it serves as investment manager. As of March 31, 2018, Artisan's direct equity investment in the consolidated investment products was \$37.1 million.

Artisan's maximum exposure to loss in connection with the assets and liabilities of CIPs is limited to its direct equity investment, while the potential benefit is limited to the management fee and incentive allocation received and the return on its equity investment. With the exception of Artisan's direct equity investment, the assets of CIPs are not available to Artisan's creditors, nor are they available to Artisan for general corporate purposes. In addition, third-party investors in the CIPs have no recourse to the general credit of the Company.

Artisan earned management fees of \$45 thousand from CIPs during the three months ended March 31, 2018. No management fees were earned from CIPs during the three months ended March 31, 2017. No incentive allocation revenue was recognized during the three months ended March 31, 2018 and 2017. Management fees and incentive allocations earned from CIPs are eliminated from revenue upon consolidation.

Third-party investors' ownership interest in CIPs is presented as redeemable noncontrolling interest in the Unaudited Consolidated Statements of Financial Condition as third-party investors have the right to withdraw their capital, subject to certain conditions. Net income attributable to third-party investors is reported as net income attributable to noncontrolling interests - consolidated investment products in the Unaudited Consolidated Statement of Operations.

Fair Value Measurements - Consolidated Investment Products

The carrying value of CIPs' investments is also their fair value. Short and long positions on equity securities are valued based upon closing prices of the security on the exchange or market designated by the accounting agent or pricing vendor as the principal exchange. The closing price may represent last sale price, official closing price, a closing auction or other information depending on market convention. Short and long positions on fixed income instruments are valued at market value. Market values are generally evaluations based on the judgment of pricing vendors, which may consider, among other factors, the prices at which securities actually trade, broker-dealer quotations, pricing formulas, estimates of market values obtained from yield data relating to investments or securities with similar characteristics and/or discounted cash flow models that might be applicable.

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The following tables present the fair value hierarchy levels of assets and liabilities held by CIPs measured at fair value as of March 31, 2018 and December 31, 2017.

| | Assets and Liabilities at Fair Value | | | |
|--|--------------------------------------|----------|---------|---------|
| | Total | Level 1 | Level 2 | Level 3 |
| March 31, 2018 | | | | |
| Assets | | | | |
| Money market funds | \$39,750 | \$39,750 | \$ — | — |
| Equity securities - long position | 75,743 | 74,394 | 1,349 | — |
| Fixed income instruments - long position | 41,808 | — | 41,808 | — |
| Derivative assets | 1,961 | 721 | 1,240 | — |

| | | | | |
|---|----------|----------|--------|---|
| Liabilities | | | | |
| Equity securities - short position | \$35,444 | \$35,444 | \$ — | — |
| Fixed income instruments - short position | 17,909 | — | 17,909 | — |
| Derivative liabilities | 402 | 94 | 308 | — |

| | Assets and Liabilities at Fair Value | | | |
|--|--------------------------------------|----------|---------|---------|
| | Total | Level 1 | Level 2 | Level 3 |
| December 31, 2017 | | | | |
| Assets | | | | |
| Money market funds | \$21,881 | \$21,881 | \$ — | — |
| Equity securities - long position | 69,044 | 69,044 | — | — |
| Fixed income instruments - long position | 45,758 | — | 45,758 | — |
| Derivative assets | 343 | 303 | 40 | — |

| | | | | |
|---|----------|----------|--------|---|
| Liabilities | | | | |
| Equity securities - short position | \$29,199 | \$29,199 | \$ — | — |
| Fixed income instruments - short position | 18,513 | — | 18,513 | — |
| Derivative liabilities | 145 | 45 | 100 | — |

CIP balances included in the Company's Consolidated Statements of Financial Condition were as follows:

| | March 31, December 31, | |
|--|------------------------|-----------|
| | 2018 | 2017 |
| Net CIP assets included in the table above | \$ 105,507 | \$ 89,169 |
| Net CIP assets not included in the table above | 13,252 | 8,762 |
| Net CIP assets | 118,759 | 97,931 |
| Less: redeemable noncontrolling interest | 81,652 | 62,581 |
| Artisan's direct equity investment in CIPs | \$37,107 | \$ 35,350 |

Transfers between investment levels may occur as the markets fluctuate and/or the availability of data used in an investment's valuation changes. Artisan's policy is to recognize transfers in and transfers out of the valuation levels as of the beginning of the reporting period. During the three months ended March 31, 2018, the Company had transfers from Level 1 to Level 2 of \$0.6 million. There were no transfers into Level 1 from Level 2, or into or out of Level 3 during the three months ended March 31, 2018.

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Note 7. Noncontrolling interest - Holdings

Net income attributable to noncontrolling interests - Artisan Partners Holdings in the Unaudited Consolidated Statements of Operations represents the portion of earnings or loss attributable to the equity ownership interests in Holdings held by the limited partners of Holdings. As of March 31, 2018, APAM held approximately 69% of the equity ownership interests in Holdings.

In order to maintain the one-to-one correspondence of the number of Holdings partnership units and APAM common shares, Holdings will issue one general partner ("GP") unit to APAM for each share of Class A common stock issued by APAM. For the three months ended March 31, 2018, APAM's equity ownership interest in Holdings has increased as a result of the following transactions:

| | Holdings GP Units | Limited Partnership Units | Total | APAM Ownership % | |
|--|----------------------|---------------------------------|------------|------------------------|---|
| Balance at December 31, 2017 | 50,463,126 | 25,106,719 | 75,569,845 | 67 | % |
| 2018 Follow-On Offering | 644,424 | (644,424) | — | 1 | % |
| Holdings Common Unit Exchanges | 958,288 | (958,288) | — | 1 | % |
| Issuance of APAM Restricted Shares | 1,510,570 | — | 1,510,570 | 1 | % |
| Restricted Share Award Net Share Settlement | (53,986) | — | (53,986) | (1) | % |
| Forfeitures of Holdings GP Units from Employee Terminations ⁽¹⁾ | (38,788) | — | (38,788) | — | % |
| Balance at March 31, 2018 | 53,483,634 | 23,504,007 | 76,987,641 | 69 | % |

⁽¹⁾ The impact of the transaction on APAM's ownership percentage was less than 1%.

Since APAM continues to have a controlling interest in Holdings, changes in ownership of Holdings are accounted for as equity transactions. Additional paid-in capital and noncontrolling interest - Artisan Partners Holdings in the Unaudited Condensed Consolidated Statements of Financial Condition are adjusted to reallocate Holdings' historical equity to reflect the change in APAM's ownership of Holdings.

The reallocation of equity had the following impact on the Unaudited Condensed Consolidated Statements of Financial Condition:

| Statement of Financial Condition | For the Three Months Ended March 31, | |
|---|--|-----------|
| | 2018 | 2017 |
| Additional paid-in capital | \$(383) | \$(1,274) |
| Noncontrolling interest - Artisan Partners Holdings | 418 | 1,510 |
| Accumulated other comprehensive income (loss) | (35) | (236) |
| Net impact to financial condition | — | — |

In addition to the reallocation of historical equity, the change in ownership resulted in an increase to deferred tax assets and additional paid-in capital of \$0.6 million for the three months ended March 31, 2018 and \$2.5 million for the three months ended March 31, 2017.

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Note 8. Stockholders' Equity

APAM - Stockholders' Equity

As of March 31, 2018 and December 31, 2017, APAM had the following authorized and outstanding equity:

| | Authorized | Outstanding | | Voting Rights ⁽¹⁾ | Economic Rights |
|-------------------------------------|-------------|----------------|-------------------|---------------------------------|-----------------|
| | | March 31, 2018 | December 31, 2017 | | |
| Common shares | | | | | |
| Class A, par value \$0.01 per share | 500,000,000 | 53,483,634 | 50,463,126 | 1 vote per share | Proportionate |
| Class B, par value \$0.01 per share | 200,000,000 | 9,707,506 | 11,922,192 | 1 vote per share ⁽²⁾ | None |
| Class C, par value \$0.01 per share | 400,000,000 | 13,796,501 | 13,184,527 | 1 vote per share | None |

⁽¹⁾ The Company's employees to whom Artisan has granted equity have entered into a stockholders agreement with respect to all shares of APAM common stock they have acquired from the Company and any shares they may acquire from the Company in the future, pursuant to which they granted an irrevocable voting proxy to a Stockholders Committee. As of March 31, 2018, Artisan's employees held 5,057,963 restricted shares of Class A common stock subject to the agreement and all 9,707,506 outstanding shares of Class B common stock.

⁽²⁾ On February 9, 2018, the Class B common shares changed from five votes per share to one vote per share.

APAM is dependent on cash generated by Holdings to fund any dividends. Generally, Holdings will make distributions to all of its partners, including APAM, based on the proportionate ownership each holds in Holdings. APAM will fund dividends to its stockholders from its proportionate share of those distributions after provision for its taxes and other obligations. APAM declared and paid the following dividends per share during the three months ended March 31, 2018 and 2017:

| Type of Dividend | Class of Stock | For the Three Months Ended March 31, 2018 2017 | |
|------------------|----------------|---|--------|
| Quarterly | Class A Common | \$0.60 | \$0.60 |
| Special Annual | Class A Common | \$0.79 | \$0.36 |

The following table summarizes APAM's stock transactions for the three months ended March 31, 2018:

| | Total Stock Outstanding | Class A Common Stock ⁽¹⁾ | Class B Common Stock | Class C Common Stock |
|---|----------------------------|---|----------------------------|----------------------------|
| Balance at December 31, 2017 | 75,569,845 | 50,463,126 | 11,922,192 | 13,184,527 |
| 2018 Follow-On Offering | — | 644,424 | (644,424) | — |
| Holdings Common Unit Exchanges | — | 958,288 | (449,066) | (509,222) |
| Restricted Share Award Grants | 1,510,570 | 1,510,570 | — | — |
| Restricted Share Award Net Share Settlement | (53,986) | (53,986) | — | — |
| Employee/Partner Terminations | (38,788) | (38,788) | (1,121,196) | 1,121,196 |
| Balance at March 31, 2018 | 76,987,641 | 53,483,634 | 9,707,506 | 13,796,501 |

⁽¹⁾ There were 246,581 and 218,089 restricted stock units outstanding at March 31, 2018 and December 31, 2017, respectively. Restricted stock units are not reflected in the table because they are not considered outstanding or issued stock.

Each Class A, Class B, Class D and Class E common unit of Holdings (together with the corresponding share of Class B or Class C common stock) is exchangeable for one share of Class A common stock. The corresponding shares of Class B and Class C common stock are immediately canceled upon any such exchange.

Upon termination of employment with Artisan, an employee-partner's Class B common units are exchanged for Class E common units and the corresponding shares of Class B common stock are canceled. APAM issues the former employee-partner a number of shares of Class C common stock equal to the former employee-partner's number of

Class E common units. Class E common units are exchangeable for Class A common stock subject to the same restrictions and limitations on exchange applicable to the other common units of Holdings.

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Artisan Partners Holdings - Partners' Equity

Holdings makes distributions of its net income to the holders of its partnership units for income taxes as required under the terms of the partnership agreement and also makes additional distributions under the terms of the partnership agreement. The distributions are recorded in the financial statements on the declaration date, or on the payment date in lieu of a declaration date. Holdings' partnership distributions for the three months ended March 31, 2018 and 2017, were as follows:

| | For the Three Months Ended March 31, | |
|--|--|----------|
| | 2018 | 2017 |
| Holdings Partnership Distributions to Limited Partners | \$22,683 | \$16,530 |
| Holdings Partnership Distributions to APAM | 45,593 | 21,633 |
| Total Holdings Partnership Distributions | \$68,276 | \$38,163 |

The distributions are recorded as a reduction to consolidated stockholders' equity, with the exception of distributions made to APAM, which are eliminated upon consolidation.

Note 9. Revenue From Contracts with Customers

Artisan's revenue is derived from contracts with customers in the form of investment management fees, performance-based fees and incentive allocations.

Investment Management Fees

Investment management fees are generally computed as a percentage of assets under management and are recognized as revenue at the end of each distinct service period. Fees for providing investment advisory services are computed and billed in accordance with the underlying investment management agreements, which is generally on a monthly or quarterly basis. Investment management fees are presented net of cash rebates and fees waived pursuant to contractual expense limitations of certain funds or voluntary waivers.

Performance Fees

A number of investment management agreements provide for performance-based fees or incentive allocations, collectively "performance fees". Performance fees, if earned, are recognized upon completion of the contractually determined measurement period, which is generally quarterly or annually. Performance fees are not subject to claw back as a result of performance declines subsequent to the most recent measurement date.

Revenue Recognition

Artisan accounts for asset management services as a single performance obligation that is satisfied over time, using a time-based measure of progress to recognize revenue. Customer consideration is variable due to the uncertainty of the value of assets under management during each distinct service period. At the end of each quarter, Artisan records revenue for the actual amount of investment management fees earned for that quarter because the uncertainty has been resolved.

Performance fees are subject to the uncertainty of market volatility, and as a result, the entire amount of the variable consideration related to performance fees is constrained until the end of each measurement period. At the end of the quarterly or annual measurement period, revenue is recorded for the actual amount of performance fees earned during that period because the uncertainty has been resolved. For performance fees with annual measurement periods, revenue recognized in the current quarter relates to performance obligations that were partially satisfied in prior periods. Artisan recognized performance fee revenues of \$42 thousand during the three months ended March 31, 2018. No performance fee revenue was recognized during the three months ended March 31, 2017.

Customer Rebates, Waivers and Expense Reimbursements

Artisan has contractually agreed to waive its investment management fees or reimburse for expenses incurred to the extent necessary to limit annualized ordinary operating expenses incurred by certain funds to not more than a fixed percentage of the funds' average daily net assets. Artisan may also contractually agree to pay fee rebates to certain clients. Artisan accounts for all waivers, reimbursements, and rebates as a reduction of the transaction price (and, hence, of revenue) because the billing adjustments and payments represent consideration payable to customers, and Artisan does not receive any distinct goods or services from the customers in exchange.

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Disaggregated Revenue

The following table presents a disaggregation of revenue by type and vehicle for the three months ended March 31, 2018 and 2017.

| | For the three months ended March 31, | |
|----------------------------------|--|-----------|
| | 2018 | 2017 |
| Management fees | | |
| Artisan Funds | \$125,253 | \$110,574 |
| Artisan Global Funds | 8,522 | 6,810 |
| Separate accounts ⁽¹⁾ | 78,191 | 66,690 |
| Performance fees | | |
| Separate accounts ⁽¹⁾ | 42 | — |
| Total revenues | \$212,008 | \$184,074 |

⁽¹⁾ Separate account revenue consists of management fees and performance fees from vehicles other than Artisan Funds or Artisan Global Funds. Separate account revenue includes fees earned from traditional separate accounts and privately offered funds, as well as fees earned from Artisan-branded collective investment trusts and funds (both public and private) that Artisan sub-advises. All management fees and performance fees from privately offered funds were eliminated upon consolidation and therefore are omitted from this table.

The following table presents the balances of receivables related to contracts with customers.

| | As of March 31, 2018 | As of December 31, 2017 |
|---|-------------------------------|-------------------------------|
| Customer | | |
| Artisan Funds | \$— | \$ 4 |
| Artisan Global Funds | 2,642 | 5,105 |
| Separate accounts | 68,813 | 68,019 |
| Total receivables from contracts with customers | \$71,455 | \$ 73,128 |
| Other receivables | 3,303 | 3,565 |
| Accounts receivable | \$74,758 | \$ 76,693 |

Artisan Funds and Artisan Global Funds are billed on the last day of each month. Artisan Funds makes payments on the same day the invoice is received and Artisan Global Funds generally makes payments in the month following receipt of the invoice. Separate account clients are generally billed on a monthly or quarterly basis, with payments due within 30 days of billing.

Artisan had no contract assets or liabilities from contracts with customers as of March 31, 2018 or December 31, 2017.

Note 10. Compensation and Benefits

Total compensation and benefits consists of the following:

| | For the Three Months Ended March 31, | |
|--|--|----------|
| | 2018 | 2017 |
| Salaries, incentive compensation and benefits ⁽¹⁾ | \$91,381 | \$81,482 |
| Restricted share-based award compensation expense | 13,843 | 11,767 |
| Total salaries, incentive compensation and benefits | 105,224 | 93,249 |
| Pre-offering related compensation - share-based awards | — | 6,339 |
| Total compensation and benefits | \$105,224 | \$99,588 |

⁽¹⁾ Excluding restricted share-based award compensation expense

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Incentive compensation

Cash incentive compensation paid to members of Artisan’s investment teams and members of its distribution teams is generally based on formulas that are tied directly to revenues. These payments are made in the quarter following the quarter in which the incentive was earned with the exception of fourth quarter payments which are paid in the fourth quarter of the year. Cash incentive compensation paid to most other employees is discretionary and subjectively determined based on individual performance and Artisan’s overall results during the applicable year and is generally paid on an annual basis.

Restricted share-based awards

Artisan has registered 14,000,000 shares of Class A common stock for issuance under the 2013 Omnibus Incentive Compensation Plan (the “Plan”). Pursuant to the Plan, APAM has granted a combination of restricted stock awards and restricted stock units (collectively referred to as “restricted share-based awards”) of Class A common stock to employees. The restricted share-based awards generally vest on a pro rata basis over five years. Certain share-based awards will vest upon a combination of both (1) pro-rata annual time vesting and (2) qualifying retirement (as defined in the award agreements).

Unvested awards are subject to forfeiture upon termination of employment. Grantees receiving the awards are entitled to dividends on unvested and vested shares and units. 6,525,686 shares of Class A common stock were reserved and available for issuance under the Plan as of March 31, 2018.

During the three months ended March 31, 2018, Artisan granted 1,510,570 restricted stock awards and 1,250 restricted stock units of Class A common stock to employees of the Company. Total compensation expense associated with the 2018 grants is expected to be approximately \$59.5 million. Compensation expense related to the restricted share-based awards is recognized based on the estimated grant date fair value on a straight-line basis over the requisite service period of the award. The initial requisite service period is generally five years for restricted share-based awards.

The Company’s accounting policy is to record the impact of forfeitures when they occur. The following table summarizes the restricted share-based award activity for the three months ended March 31, 2018:

| | Weighted-Average Grant Date Fair Value | Number of Awards |
|-----------------------------|--|---------------------|
| Unvested at January 1, 2018 | \$ 38.79 | 4,013,986 |
| Granted | 39.35 | 1,511,820 |
| Forfeited | 38.62 | (38,788) |
| Vested | 32.92 | (325,930) |
| Unvested at March 31, 2018 | \$ 39.33 | 5,161,088 |

Compensation expense recognized related to the restricted share-based awards was \$13.8 million and \$11.8 million for the three months ended March 31, 2018 and 2017, respectively. The unrecognized compensation expense for the unvested awards as of March 31, 2018 was \$142.1 million with a weighted average recognition period of 3.7 years remaining.

During the three months ended March 31, 2018, the Company withheld a total of 53,986 restricted shares as a result of net share settlements to satisfy employee tax withholding obligations. The Company paid \$1.8 million in employee tax withholding obligations related to these settlements during the three months ended March 31, 2018. These net share settlements had the effect of shares repurchased and retired by the Company, as they reduced the number of shares outstanding.

Pre-offering related compensation - share-based awards

Prior to the IPO, Holdings granted Class B share-based awards to certain employees. These awards vested over a period of five years and became fully vested on July 1, 2017. Compensation expense recognized related to the Class B awards was \$6.3 million for the three months ended March 31, 2017.

Note 11. Income Taxes and Related Payments

APAM is subject to U.S. federal, state and local income taxation on APAM’s allocable portion of Holdings’ income. APAM’s effective income tax rate was lower than the U.S. federal statutory rate of 21% primarily due to a rate benefit attributable to the fact that, for the three months ended March 31, 2018, approximately 33% of Artisan Partners

Holdings' full year projected taxable earnings were attributable to other partners and not subject to corporate-level taxes. The effective tax rate was also lower than the statutory rate due to dividends paid on unvested share-based awards during the quarter.

The Tax Cuts and Jobs Act ("Tax Reform") was enacted in December 2017. As a result of Tax Reform, the U.S. federal corporate tax rate decreased from 35% to 21%, which was the largest driver of lowering APAM's effective tax rate from 23.1% for three months ended March 31, 2017 to 14.6% for the three months ended March 31, 2018.

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Components of the provision for income taxes consist of the following:

| | For the Three Months Ended March 31, 2018 2017 | |
|--------------------|---|----------|
| Current: | | |
| Federal | \$4,149 | \$2,623 |
| State and local | 767 | 361 |
| Foreign | 117 | 108 |
| Total | 5,033 | 3,092 |
| Deferred: | | |
| Federal | 6,480 | 9,135 |
| State and local | 772 | 522 |
| Total | 7,252 | 9,657 |
| Income tax expense | \$12,285 | \$12,749 |

In connection with the IPO, APAM entered into two tax receivable agreements (“TRAs”). The first TRA generally provides for the payment by APAM to a private equity fund (the “Pre-H&F Corp Merger Shareholder”) of 85% of the applicable cash savings, if any, of U.S. federal, state and local income taxes that APAM actually realizes (or is deemed to realize in certain circumstances) as a result of (i) the tax attributes of the preferred units APAM acquired in the merger of a wholly-owned subsidiary of the Pre-H&F Corp Merger Shareholder into APAM in March 2013, (ii) net operating losses available as a result of the merger and (iii) tax benefits related to imputed interest.

The second TRA generally provides for the payment by APAM to current or former limited partners of Holdings of 85% of the applicable cash savings, if any, of U.S. federal, state and local income taxes that APAM actually realizes (or is deemed to realize in certain circumstances) as a result of (i) certain tax attributes of their partnership units sold to APAM or exchanged (for shares of Class A common stock, convertible preferred stock or other consideration) and that are created as a result of such sales or exchanges and payments under the TRAs and (ii) tax benefits related to imputed interest. Under both agreements, APAM generally will retain the benefit of the remaining 15% of the applicable tax savings.

For purposes of the TRAs, cash savings of income taxes are calculated by comparing APAM’s actual income tax liability to the amount it would have been required to pay had it not been able to utilize any of the tax benefits subject to the TRAs, unless certain assumptions apply. The TRAs will continue in effect until all such tax benefits have been utilized or expired, unless APAM exercises its right to terminate the agreements or payments under the agreements are accelerated in the event that APAM materially breaches any of its material obligations under the agreements.

The actual increase in tax basis, as well as the amount and timing of any payments under these agreements, will vary depending upon a number of factors, including the timing of sales or exchanges by the holders of limited partnership units, the price of the Class A common stock at the time of such sales or exchanges, whether such sales or exchanges are taxable, the amount and timing of the taxable income APAM generates in the future and the tax rate then applicable and the portion of APAM’s payments under the TRAs constituting imputed interest or depreciable basis or amortizable basis.

Payments under the TRAs, if any, will be made pro rata among all TRA counterparties entitled to payments on an annual basis to the extent APAM has sufficient taxable income to utilize the increased depreciation and amortization charges and imputed interest deductions. Artisan expects to make one or more payments under the TRAs, to the extent they are required, prior to or within 125 days after APAM’s U.S. federal income tax return is filed for each fiscal year. Interest on the TRA payments will accrue at a rate equal to one-year LIBOR plus 100 basis points from the due date (without extension) of such tax return until such payments are made.

Amounts payable under tax receivable agreements are estimates which may be impacted by factors, including but not limited to, expected tax rates, projected taxable income, and projected ownership levels and are subject to change. Changes in the estimates of amounts payable under tax receivable agreements are recorded as non-operating income (loss) in the Consolidated Statements of Operations.

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The change in the Company's deferred tax assets related to the tax benefits described above and the change in corresponding amounts payable under the TRAs for the three months ended March 31, 2018 is summarized as follows:

| | Deferred Tax Asset - Amortizable basis | Amounts payable under tax receivable agreements |
|-------------------------------------|---|---|
| December 31, 2017 | \$ 410,690 | \$ 385,413 |
| 2018 Follow-On Offering | 7,687 | 6,534 |
| 2018 Holdings Common Unit Exchanges | 10,023 | 8,520 |
| Amortization | (7,314) | — |
| March 31, 2018 | \$ 421,086 | \$ 400,467 |

Net deferred tax assets comprise the following:

| | As of March 31, 2018 | As of December 31, 2017 |
|--|----------------------------|-------------------------------|
| Deferred tax assets: | | |
| Amortizable basis ⁽¹⁾ | \$421,086 | \$ 410,690 |
| Other ⁽²⁾ | 19,297 | 18,522 |
| Total deferred tax assets | 440,383 | 429,212 |
| Less: valuation allowance ⁽³⁾ | — | — |
| Net deferred tax assets | \$440,383 | \$ 429,212 |

⁽¹⁾ Represents the unamortized step-up of tax basis and other tax attributes from the merger and partnership unit sales and exchanges described above. These future tax benefits are subject to the TRA agreements.

⁽²⁾ Represents the net deferred tax assets associated with the merger described above and other miscellaneous deferred tax assets. These future tax benefits are not subject to the TRA agreements.

⁽³⁾ Artisan assessed whether the deferred tax assets would be realizable and determined based on its history of taxable income that the benefits would more likely than not be realized. Accordingly, no valuation allowance is required.

Accounting standards establish a minimum threshold for recognizing, and a system for measuring, the benefits of income tax return positions in financial statements. There were no uncertain tax positions recorded as of March 31, 2018 and December 31, 2017.

In the normal course of business, Artisan is subject to examination by federal and certain state, local and foreign tax regulators. As of March 31, 2018, U.S. federal income tax returns for the years 2014 through 2016 are open and therefore subject to examination. State and local tax returns are generally subject to examination from 2013 to 2016. Foreign tax returns are generally subject to examination from 2013 to 2016.

Note 12. Accumulated Other Comprehensive Income (Loss)

Accumulated Other Comprehensive Income (Loss), net of tax, in the accompanying Condensed Consolidated Statements of Financial Condition represents the portion of accumulated other comprehensive income attributable to APAM, and consists of the following:

| | As of March | As of December |
|--|----------------|-------------------|
|--|----------------|-------------------|

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| | 31, 2018 | 31, 2017 |
|---|----------|-----------|
| Unrealized gain on investments, net of tax | \$— | \$ 259 |
| Foreign currency translation gain (loss) | (739) | (1,132) |
| Accumulated Other Comprehensive Income (Loss) | \$(739) | \$(873) |

Comprehensive income (loss) attributable to noncontrolling interests - Artisan Partners Holdings in the Consolidated Statements of Comprehensive Income (Loss) represents the portion of comprehensive income (loss) attributable to the equity ownership interests in Holdings held by the limited partners of Holdings.

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Note 13. Earnings Per Share

Basic earnings per share is computed under the two-class method by dividing income available to Class A common stockholders by the weighted average number of Class A common shares outstanding during the period. Unvested restricted share-based awards are excluded from the number of Class A common shares outstanding for the basic earnings per share calculation because the shares have not yet been earned by employees. Income available to Class A common stockholders is computed by reducing net income attributable to APAM by earnings (distributed and undistributed) allocated to participating securities, according to their respective rights to participate in those earnings. Unvested share-based awards are participating securities because the awards include non-forfeitable dividend rights during the vesting period. Class B and Class C common shares do not share in profits of APAM and therefore are not reflected in the calculations.

The computation of basic and diluted earnings per share under the two-class method for the three months ended March 31, 2018 and 2017 were as follows:

| Basic and Diluted Earnings Per Share | For the Three Months Ended March 31, | |
|--|--|------------|
| | 2018 | 2017 |
| Numerator: | | |
| Net income attributable to APAM | \$41,274 | \$ 19,795 |
| Less: Allocation to participating securities | 5,924 | 4,426 |
| Net income available to common stockholders | \$35,350 | \$ 15,369 |
| Denominator: | | |
| Weighted average shares outstanding | 47,360,438 | 38,019,598 |
| Earnings per share | \$0.75 | \$ 0.37 |

Allocation to participating securities in the table above primarily represents dividends paid to holders of unvested restricted share-based awards, which reduces net income available to common stockholders.

There were no dilutive securities outstanding during the three months ended March 31, 2018 and 2017. The Holdings limited partnership units are anti-dilutive primarily due to the impact of public company expenses. Unvested restricted share-based awards are considered participating securities and are therefore anti-dilutive. The following table summarizes the weighted-average shares outstanding that are excluded from the calculation of diluted earnings per share because their effect would have been anti-dilutive:

| Anti-Dilutive Weighted Average Shares Outstanding | For the Three Months Ended March 31, | |
|---|---|------------|
| | 2018 | 2017 |
| Holdings limited partnership units | 24,558,161 | 30,218,943 |
| Unvested restricted share-based awards | 4,564,084 | 3,912,879 |
| Total | 29,122,245 | 34,131,822 |

Note 14. Indemnifications

In the normal course of business, APAM enters into agreements that include indemnities in favor of third parties. Holdings has also agreed to indemnify APAM as its general partner, Artisan Investment Corporation ("AIC") as its former general partner, the directors and officers of APAM, the directors and officers of AIC as its former general partner, the members of its former Advisory Committee, and its partners, directors, officers, employees and agents. Holdings' subsidiaries may also have similar agreements to indemnify their respective general partner(s), directors, officers, directors and officers of their general partner(s), partners, members, employees, and agents. The Company's maximum exposure under these arrangements is unknown, as this would involve future claims that may be made against us that have not yet occurred. APAM maintains insurance policies that may provide coverage against certain claims under these indemnities.

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Note 15. Related Party Transactions

Several of the current executive officers of APAM and certain members of APAM's board (or their affiliates) are limited partners of Holdings. As a result, certain transactions (such as TRA payments) between Artisan and the limited partners of Holdings are considered to be related party transactions with respect to these persons.

Affiliate transactions—Artisan Funds

Artisan has an agreement to serve as the investment adviser to Artisan Funds, with which certain Artisan employees are affiliated. Under the terms of the agreement, which generally is reviewed and continued by the board of directors of Artisan Funds annually, a fee is paid to Artisan based on an annual percentage of the average daily net assets of each Artisan Fund ranging from 0.625% to 1.25%. Artisan generally collects revenues related to these services on the last business day of each month and records them in Management Fees in the Consolidated Statement of Operations. Artisan has contractually agreed to waive its management fees or reimburse for expenses incurred to the extent necessary to limit annualized ordinary operating expenses incurred by certain of the Artisan Funds to not more than a fixed percentage (ranging from 0.88% to 1.50%) of a Fund's average daily net assets. In addition, Artisan may voluntarily waive fees or reimburse any of the Artisan Funds for other expenses. The officers and a director of Artisan Funds who are affiliated with Artisan receive no compensation from the funds.

Fees for managing the Funds and amounts waived or reimbursed by Artisan for fees and expenses (including management fees) are as follows:

| | For the Three Months Ended March 31, 2018 2017 | |
|---|--|------------|
| Investment management fees (Gross of fee waivers/expense reimbursements): | | |
| Artisan Funds | \$ 125,362 | \$ 110,574 |
| Fee waiver / expense reimbursement: | | |
| Artisan Funds | \$ 109 | \$ 197 |

Affiliate transactions—Artisan Global Funds

Artisan has an agreement to serve as the investment manager to Artisan Global Funds, with which certain Artisan employees are affiliated. Under the terms of these agreements, a fee is paid based on an annual percentage of the average daily net assets of each fund ranging from 0.75% to 1.75%. Artisan reimburses each sub-fund of Artisan Global Funds to the extent that sub-fund's expenses, not including Artisan's fee, exceed certain levels, which range from 0.10% to 0.20%. In addition, Artisan may voluntarily waive fees or reimburse any of the Artisan Global Funds for other expenses. The directors of Artisan Global Funds who are affiliated with Artisan receive no compensation from the funds. Fees for managing Artisan Global Funds and amounts reimbursed to Artisan Global Funds by Artisan are as follows:

| | For the Three Months Ended March 31, 2018 2017 | |
|---|--|----------|
| Investment management fees (Gross of fee waivers/expense reimbursements): | | |
| Artisan Global Funds | \$ 8,526 | \$ 6,810 |
| Fee waiver / expense reimbursement: | | |
| Artisan Global Funds | \$ 4 | \$ 17 |

Affiliate transactions—Artisan Sponsored Private Funds

Pursuant to written agreements, Artisan serves as the investment manager of certain Artisan sponsored private funds. Under the terms of these agreements, Artisan earns a management fee and is entitled to receive an allocation of profits. In 2017, Artisan made seed investments of \$32.3 million in the private funds. Certain related parties, including employees, officers and members of the Company's board invested an additional \$34.6 million in the funds. These related party investors currently do not pay a management fee or incentive allocation. In addition, for a period of time following the formation of the private funds, Artisan has agreed to reimburse the funds to the extent that expenses,

excluding Artisan's management fee and transaction related costs, exceed 1.00% per annum of the net assets of the funds. Artisan may also voluntarily waive fees or reimburse the funds for other expenses. Gross fees for managing the privately offered funds were \$98 thousand for the three months ended March 31, 2018, which were eliminated from revenue upon consolidation. Expense reimbursements totaled \$9 thousand for the three months ended March 31, 2018.

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Note 16. Subsequent Events

Distributions and dividends

On April 26, 2018, APAM, acting as the general partner of Artisan Partners Holdings, declared a distribution by Artisan Partners Holdings of \$27.6 million to holders of Artisan Partners Holdings partnership units, including APAM. On the same date, the board of directors of APAM declared a quarterly dividend of \$0.60 per share of Class A common stock. The APAM dividend is payable on May 31, 2018, to shareholders of record as of May 17, 2018.

Holdings Unit Exchanges

On April 2, 2018, limited partners of Artisan Partners Holdings exchanged 452,628 common units for 452,628 Class A common shares. The exchange increased APAM's equity ownership interest in Holdings and resulted in an \$4.4 million increase in deferred tax assets and \$3.8 million increase in amounts payable under the tax receivable agreements.

TRA Payments

On April 17, 2018, the Company made a payment of \$27.3 million under the tax receivable agreements representing a portion of the Company's estimated total 2018 TRA payments.

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Overview and Recent Highlights

We are an investment management firm focused on providing high-value added, active investment strategies to sophisticated clients globally. As of March 31, 2018, our eight autonomous investment teams managed a total of 17 investment strategies across multiple asset classes and investment styles. Over our firm's history, we have created new investment strategies that can use a broad array of securities, instruments, and techniques (which we call degrees of freedom) to differentiate returns and manage risk.

We focus our distribution efforts on sophisticated investors and asset allocators, including institutions and intermediaries that operate with institutional-like decision-making processes. We offer our investment strategies to clients and investors through multiple investment vehicles, including separate accounts and different types of pooled vehicles. As of March 31, 2018, approximately 80% of our assets under management were managed for clients and investors domiciled in the U.S. and 20% of our assets under management were managed for clients and investors domiciled outside of the U.S. Over the last five years we have grown our assets under management from clients and investors domiciled outside of the U.S. from \$9.2 billion as of March 31, 2013, to \$23.0 billion as of March 31, 2018. As a high-value added investment manager we expect that long-term investment performance will be the primary driver of our long-term business and financial results. If we maintain and evolve existing investment strategies and launch new investment strategies that meet the needs of and generate attractive outcomes for sophisticated asset allocators, we are confident that we will continue to generate strong business and financial results.

Over shorter time periods, changes in our business and financial results are largely driven by market conditions and fluctuations in our assets under management that may not necessarily be the result of our long-term investment performance or the long-term demand for our strategies. For this reason, we expect that our business and financial results will be lumpy over time. During the first quarter of 2018, our assets under management decreased to \$114.8 billion, a decrease of \$0.7 billion, or 0.6%, compared to \$115.5 billion at December 31, 2017, as a result of \$0.6 billion in net client cash outflows and \$0.1 billion of market depreciation.

Compared to March 31, 2017, assets under management increased \$11.1 billion, or 10.7%, due to \$16.8 billion in market appreciation, partially offset by \$5.7 billion of net client cash outflows. Average assets under management for the March quarter of 2018 was \$118.3 billion, an increase of 17.0% from the average of \$101.1 billion for the March quarter of 2017.

We strive to maintain a financial model that is transparent and predictable. We derive essentially all of our revenues from investment management fees, nearly all of which are based on a specified percentage of clients' average assets under management. A majority of our expenses, including most of our compensation expense, vary directly with changes in our revenues. We invest thoughtfully to support our investment teams and future growth, while also paying out to shareholders and partners a majority of the cash that we generate from operations through distributions and dividends.

Revenues were \$212.0 million for the three months ended March 31, 2018, a 15% increase from revenues of \$184.1 million for the three months ended March 31, 2017. GAAP operating margin was 37.7% for the three months ended March 31, 2018, compared to 31.5% for the three months ended March 31, 2017. Adjusted operating margin was 37.7% for the three months ended March 31, 2018, compared to 35.0% for the three months ended March 31, 2017. The Tax Cuts and Jobs Act ("Tax Reform") was enacted in December 2017. As a result of Tax Reform, the U.S. federal corporate tax rate decreased from 35% to 21%, which was the largest driver of lowering APAM's effective tax rate from 23.1% for three months ended March 31, 2017, to 14.6% for the three months ended March 31, 2018. The estimated adjusted effective tax rate decreased from 37% to 23.5%.

Business highlights for the first quarter of 2018 included:

- Our assets under management as of March 31, 2018 were \$114.8 billion and average assets under management for the first quarter were \$118.3 billion.

- Our investment teams continue to generate strong absolute and relative investment returns for clients and investors.

- Eleven of our 13 investment strategies with at least a one-year track record have outperformed their broad-based benchmarks since inception, net of fees.

-

We declared and paid dividends of \$1.39 per share of Class A common stock. With the \$0.79 special annual dividend paid in the first quarter, we paid a total of \$3.19 per share of dividends with respect to 2017.

• We successfully completed our February 2018 follow-on offering, continuing the evolution of our capital structure.

• We granted 1,510,570 restricted stock awards and 1,250 restricted stock units of Class A common stock to employees of the Company.

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Organizational Structure

Organizational Structure

Our operations are conducted through Artisan Partners Holdings (“Holdings”) and its subsidiaries. On March 12, 2013, Artisan Partners Asset Management Inc. (“APAM”) and Artisan Partners Holdings LP completed a series of transactions (“the IPO Reorganization”) to reorganize their capital structures in connection with the initial public offering (“IPO”) of APAM’s Class A common stock. The IPO Reorganization and IPO were completed on March 12, 2013. The IPO Reorganization was designed to create a capital structure that preserves our ability to conduct our business through Holdings, while permitting us to raise additional capital and provide access to liquidity through a public company. Our employees and other limited partners of Holdings held approximately 31% of the equity interests in Holdings as of March 31, 2018. As a result, our results reflect that significant noncontrolling interest.

We operate our business in a single segment.

2018 Follow-On Offering and Holdings Unit Exchanges

On February 27, 2018, APAM completed an offering of 644,424 shares of Class A common stock and utilized all of the proceeds to purchase an aggregate of 644,424 common units from certain limited partners of Holdings. In connection with the offering, APAM received 644,424 GP units of Holdings.

During the three months ended March 31, 2018, certain limited partners of Holdings exchanged 958,288 common units (along with a corresponding number of shares of Class B or C common stock of APAM) for 958,288 shares of Class A common stock. In connection with the exchanges, APAM received 958,288 GP units of Holdings.

APAM’s equity ownership interest in Holdings increased from 67% at December 31, 2017 to 69% at March 31, 2018, as a result of these transactions and other equity transactions during the period.

Financial Overview

Economic Environment

Global equity and debt market conditions can materially affect our financial performance. The following table presents the total returns of relevant market indices for the three months ended March 31, 2018 and 2017:

| | For the Three Months Ended March 31 | |
|---|---|-------|
| | 2018 | 2017 |
| S&P 500 total returns | (0.8)% | 6.1 % |
| MSCI All Country World total returns | (1.0)% | 6.9 % |
| MSCI EAFE total returns | (1.5)% | 7.3 % |
| Russell Midcap [®] total returns | (0.5)% | 5.2 % |
| MSCI Emerging Markets Index | 1.4 % | 11.4% |
| ICE BofA Merrill Lynch U.S. High Yield Master II Total Return Index | (0.9)% | 2.7 % |

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Key Performance Indicators

When we review our business and financial performance we consider, among other things, the following:

| | For the Three Months Ended | | | |
|--|----------------------------------|------------|------|-----|
| | March 31, | | | |
| | 2018 | 2017 | | |
| | (unaudited; dollars in millions) | | | |
| Assets under management at period end | \$ 114,816 | \$ 103,762 | | |
| Average assets under management ⁽¹⁾ | \$ 118,275 | \$ 101,132 | | |
| Net client cash flows | \$(603) | \$(272) | | |
| Total revenues | \$212.0 | \$184.1 | | |
| Weighted average fee ⁽²⁾ | 72.8 | bps | 73.7 | bps |
| Operating margin | 37.7 | % | 31.5 | % |
| Adjusted operating margin ⁽³⁾ | 37.7 | % | 35.0 | % |

⁽¹⁾ We compute average assets under management by averaging day-end assets under management for the applicable period.

⁽²⁾ We compute our weighted average fee by dividing annualized investment management fees by average assets under management for the applicable period.

⁽³⁾ Adjusted measures are non-GAAP measures and are explained and reconciled to the comparable GAAP measures in “Supplemental Non-GAAP Financial Information” below.

The period-over-period changes in these metrics are discussed below. The decrease in the weighted average fee rate is primarily a result of the shift in the mix of our assets under management between our investment strategies and vehicles, primarily the increase in the proportion of total assets managed in separate accounts.

Management fees and assets under management within our consolidated investment products are excluded from the weighted average fee calculations and from total revenues, since any such revenues are eliminated upon consolidation. Assets under management within Artisan sponsored private funds are included in the reported firm-wide, separate account, and institutional assets under management figures reported below.

Assets Under Management and Investment Performance

Changes to our operating results from one period to another are primarily caused by changes in the amount of our assets under management. Changes in the relative composition of our assets under management among our investment strategies and vehicles and the effective fee rates on our products also impact our operating results.

The amount and composition of our assets under management are, and will continue to be, influenced by a variety of factors including, among others:

- investment performance, including fluctuations in both the financial markets and foreign currency exchange rates and the quality of our investment decisions;
- flows of client assets into and out of our various strategies and investment vehicles;
- our decision to close strategies or limit the growth of assets in a strategy or a vehicle when we believe it is in the best interest of our clients; as well as our decision to re-open strategies, in part or entirely;
- our ability to attract and retain qualified investment, management, and marketing and client service professionals;
- industry trends towards products or strategies that we do not offer;
- competitive conditions in the investment management and broader financial services sectors; and
- investor sentiment and confidence.

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The table below sets forth changes in our total assets under management:

| | For the Three Months Ended March 31, | | Period-to-Period | | |
|---|---|------------|------------------|---------|---|
| | 2018 | 2017 | \$ | % | |
| | (unaudited; in millions) | | | | |
| Beginning assets under management | \$ 115,494 | \$ 96,845 | \$ 18,649 | 19.3 | % |
| Gross client cash inflows | 5,419 | 5,160 | 259 | 5.0 | % |
| Gross client cash outflows | (6,022) | (5,432) | (590) | (10.9) | % |
| Net client cash flows | (603) | (272) | (331) | (121.7) | % |
| Market appreciation (depreciation) ⁽¹⁾ | (75) | 7,189 | (7,264) | (101.0) | % |
| Net transfers ⁽²⁾ | — | — | — | — | % |
| Ending assets under management | \$ 114,816 | \$ 103,762 | \$ 11,054 | 10.7 | % |
| Average assets under management | \$ 118,275 | \$ 101,132 | \$ 17,143 | 17.0 | % |

⁽¹⁾ Includes the impact of translating the value of assets under management denominated in non-USD currencies into U.S. dollars. The impact was immaterial for the periods presented.

⁽²⁾ Net transfers represent certain amounts that we have identified as having been transferred out of one investment strategy or investment vehicle and into another strategy or vehicle.

Across the firm, we experienced total net outflows of \$0.6 billion during the three months ended March 31, 2018. During the period, our U.S. Mid-Cap Growth and Non-U.S. Growth strategies had net outflows of \$1.1 billion and \$0.7 billion, respectively. We anticipate that these trends will continue further into 2018.

We monitor the availability of attractive investment opportunities relative to the amount of assets we manage in each of our investment strategies. When appropriate, we will close a strategy to new investors or otherwise take action to slow or restrict its growth, even though our aggregate assets under management may be negatively impacted in the short term. We may also re-open a strategy, widely or selectively, to fill available capacity or manage the diversification of our client base in that strategy. We believe that management of our investment capacity protects our ability to manage assets successfully, which protects the interests of our clients and, in the long term, protects our ability to retain client assets and maintain our profit margins.

As of the date of this filing, our Non-U.S. Growth, Non-U.S. Small-Cap Growth, Non-U.S. Value, U.S. Mid-Cap Growth and U.S. Small-Cap Growth strategies are closed to most new investors and client relationships. Our Global Value and Global Opportunities strategies are open across pooled vehicles, but closed to most new separate account clients. We may selectively accept additional separate account clients in those strategies, but we are managing asset flows into those strategies with a bias towards assets from pooled vehicles.

When we close or otherwise restrict the growth of a strategy, we typically continue to allow additional investments in the strategy by existing clients and certain related entities. We may also permit new investments by other eligible investors in our discretion. As a result, during a given period we may have net client cash inflows in a closed strategy. However, when a strategy is closed or its growth is restricted we expect there to be periods of net client cash outflows. The table below sets forth the total assets under management for our investment teams and strategies as of March 31, 2018, the inception date for each investment composite, and the average annual total returns for each composite (gross of fees) and its respective broad-based benchmark (and style benchmark, if applicable) over a multi-horizon time period as of March 31, 2018. Returns for periods less than one year are not annualized.

We measure investment performance based upon the results of our “composites”, which represent the aggregate performance of all discretionary client accounts, including mutual funds, invested in the same strategy except those accounts with respect to which we believe client-imposed investment restrictions may have a material impact on portfolio construction and those accounts managed in a currency other than U.S. dollars. The results of these excluded accounts, which represented approximately 11% of our assets under management at March 31, 2018, are maintained in separate composites the results of which are not included below.

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| Investment Team and Strategy | Inception Date | Strategy AUM (in \$MM) | Average Annual Total Returns (gross) (%) | | | | | Average Annual Value-Added ⁽¹⁾ Since Inception (bps) |
|---|----------------|------------------------|--|--------|--------|--------|-----------|---|
| | | | 1 YR | 3 YR | 5 YR | 10 YR | Inception | |
| Growth Team | | | | | | | | |
| Global Opportunities Strategy | 2/1/2007 | \$16,271 | 23.71% | 14.42% | 14.17% | 12.35% | 11.06% | 605 |
| MSCI All Country World Index | | | 14.85% | 8.11% | 9.20% | 5.57% | 5.00% | |
| Global Discovery Strategy | 9/1/2017 | \$37 | N/A | N/A | N/A | N/A | 11.39% | 465 |
| MSCI All Country World Index | | | N/A | N/A | N/A | N/A | 6.74% | |
| U.S. Mid-Cap Growth Strategy | 4/1/1997 | \$12,178 | 17.31% | 8.14% | 12.41% | 11.90% | 15.09% | 471 |
| Russell Midcap® Index | | | 12.20% | 8.00% | 12.08% | 10.21% | 10.38% | |
| Russell Midcap® Growth Index | | | 19.74% | 9.16% | 13.30% | 10.61% | 9.28% | |
| U.S. Small-Cap Growth Strategy | 4/1/1995 | \$2,385 | 26.12% | 13.60% | 14.26% | 12.86% | 10.81% | 136 |
| Russell 2000® Index | | | 11.79% | 8.38% | 11.46% | 9.84% | 9.45% | |
| Russell 2000® Growth Index | | | 18.63% | 8.76% | 12.89% | 10.94% | 7.99% | |
| Global Equity Team | | | | | | | | |
| Global Equity Strategy | 4/1/2010 | \$1,412 | 28.67% | 10.16% | 11.64% | N/A | 13.23% | 457 |
| MSCI All Country World Index | | | 14.85% | 8.11% | 9.20% | N/A | 8.66% | |
| Non-U.S. Growth Strategy | 1/1/1996 | \$26,501 | 21.68% | 4.24% | 7.19% | 5.12% | 10.43% | 544 |
| MSCI EAFE Index | | | 14.80% | 5.55% | 6.49% | 2.74% | 4.99% | |
| Non-U.S. Small-Cap Growth Strategy | 1/1/2002 | \$698 | 29.81% | 9.38% | 8.61% | 6.91% | 13.78% | 308 |
| MSCI EAFE Small Cap Index | | | 23.49% | 12.24% | 11.09% | 6.48% | 10.70% | |
| U.S. Value Team | | | | | | | | |
| Value Equity Strategy | 7/1/2005 | \$2,196 | 7.78% | 9.21% | 9.97% | 8.44% | 8.44% | (37) |
| Russell 1000® Index | | | 13.98% | 10.38% | 13.16% | 9.60% | 8.81% | |
| Russell 1000® Value Index | | | 6.95% | 7.87% | 10.78% | 7.77% | 7.37% | |
| U.S. Mid-Cap Value Strategy | 4/1/1999 | \$5,999 | 7.96% | 7.11% | 8.77% | 10.23% | 13.20% | 373 |
| Russell Midcap® Index | | | 12.20% | 8.00% | 12.08% | 10.21% | 9.47% | |
| Russell Midcap® Value Index | | | 6.50% | 7.22% | 11.10% | 9.80% | 9.91% | |
| Global Value Team | | | | | | | | |
| Global Value Strategy | 7/1/2007 | \$20,195 | 14.21% | 9.62% | 11.44% | 11.02% | 8.99% | 461 |
| MSCI All Country World Index | | | 14.85% | 8.11% | 9.20% | 5.57% | 4.38% | |
| Non-U.S. Value Strategy | 7/1/2002 | \$21,363 | 13.59% | 7.44% | 9.70% | 9.26% | 12.58% | 605 |
| MSCI EAFE Index | | | 14.80% | 5.55% | 6.49% | 2.74% | 6.53% | |
| Emerging Markets Team | | | | | | | | |
| Emerging Markets Strategy | 7/1/2006 | \$292 | 29.04% | 14.30% | 8.00% | 3.20% | 6.95% | 61 |
| MSCI Emerging Markets Index | | | 24.93% | 8.80% | 4.98% | 3.02% | 6.34% | |
| Credit Team | | | | | | | | |
| High Income Strategy | 4/1/2014 | \$2,619 | 7.01% | 8.09% | N/A | N/A | 7.55% | 316 |
| ICE BofAML US High Yield Master II Total Return Index | | | 3.69% | 5.17% | N/A | N/A | 4.39% | |
| Developing World Team | | | | | | | | |
| Developing World Strategy | 7/1/2015 | \$2,509 | 22.60% | N/A | N/A | N/A | 12.16% | 280 |
| MSCI Emerging Markets Index | | | 24.93% | N/A | N/A | N/A | 9.36% | |
| Thematic Team | | | | | | | | |
| Thematic Strategy | 5/1/2017 | \$45 | N/A | N/A | N/A | N/A | 38.94% | 2,610 |
| S&P 500 Market Index (Total Return) | | | N/A | N/A | N/A | N/A | 12.83% | |
| Other Assets Under Management ² | | \$116 | | | | | | |

Total Assets Under Management \$ 114,816

(1) Value-added is the amount in basis points by which the average annual gross composite return of each of our strategies has outperformed the broad-based market index most commonly used by our clients to compare the performance of the relevant strategy. Value-added for periods less than one year is not annualized. The Artisan High Income Strategy may hold loans and other security types that may not be included in the ICE BofA Merrill Lynch U.S. High Yield Master II Total Return Index. At times, this causes material differences in relative performance. The Global Equity, Global Discovery, and Thematic strategies' investments in initial public offerings (IPOs) made a material contribution to performance. IPO investments may contribute significantly to a small portfolio's return, an effect that will generally decrease as assets grow. IPO investments may be unavailable in the future.

(2) Other Assets Under Management includes AUM managed by the Credit Team in the Credit Opportunities strategy and by the Thematic Team in the Thematic Long/Short strategy, respectively. Strategy specific information has been omitted.

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The tables below set forth changes in our assets under management by investment team:

| Three Months Ended | Growth | By Investment Team | | | | | | | Total |
|------------------------------------|----------|--------------------|------------|--------------|------------------|---------|------------------|----------|-----------|
| | | Global Equity | U.S. Value | Global Value | Emerging Markets | Credit | Developing World | Thematic | |
| March 31, 2018 | | | | | | | | | |
| Beginning assets under management | \$30,628 | \$29,235 | \$8,765 | \$41,687 | \$282 | \$2,554 | \$2,253 | \$90 | \$115,494 |
| Gross client cash inflows | 1,282 | 1,046 | 250 | 2,124 | 7 | 352 | 331 | 27 | 5,419 |
| Gross client cash outflows | (2,186) | (1,798) | (584) | (1,118) | (4) | (258) | (72) | (2) | (6,022) |
| Net client cash flows | (904) | (752) | (334) | 1,006 | 3 | 94 | 259 | 25 | (603) |
| Market appreciation (depreciation) | 1,147 | 128 | (236) | (1,135) | 7 | 10 | (3) | 7 | (75) |
| Net transfers ⁽¹⁾ | — | — | — | — | — | — | — | — | — |
| Ending assets under management | \$30,871 | \$28,611 | \$8,195 | \$41,558 | \$292 | \$2,658 | \$2,509 | \$122 | \$114,816 |
| Average assets under management | \$31,861 | \$29,678 | \$8,614 | \$42,633 | \$294 | \$2,633 | \$2,450 | \$112 | \$118,275 |
| March 31, 2017 | | | | | | | | | |
| Beginning assets under management | \$25,714 | \$25,510 | \$8,588 | \$33,940 | \$228 | \$1,878 | 987 | \$— | \$96,845 |
| Gross client cash inflows | 1,153 | 1,170 | 739 | 1,475 | 4 | 399 | 220 | — | 5,160 |
| Gross client cash outflows | (1,473) | (1,660) | (657) | (1,423) | (2) | (183) | (34) | — | (5,432) |
| Net client cash flows | (320) | (490) | 82 | 52 | 2 | 216 | 186 | — | (272) |
| Market appreciation (depreciation) | 2,343 | 2,252 | 257 | 2,134 | 28 | 51 | 124 | — | 7,189 |
| Net transfers ⁽¹⁾ | — | — | — | — | — | — | — | — | — |
| Ending assets under management | \$27,737 | \$27,272 | \$8,927 | \$36,126 | \$258 | \$2,145 | 1,297 | — | \$103,762 |
| Average assets under management | \$27,140 | \$26,669 | \$8,784 | \$35,107 | \$247 | \$2,030 | 1,155 | \$— | \$101,132 |

⁽¹⁾ Net transfers represent certain amounts that we have identified as having been transferred out of one investment strategy or investment vehicle and into another strategy or vehicle.

The goal of our marketing, distribution and client services efforts is to establish and maintain a client base that is diversified by investment strategy, investment vehicle and distribution channel. As distribution channels have evolved to have more institutional-like decision making processes and longer-term investment horizons, we have expanded our distribution efforts into those areas.

The table below sets forth our assets under management by distribution channel:

| | As of March 31, 2018 ⁽¹⁾ | | As of March 31, 2017 ⁽¹⁾ | |
|--------------------------------|-------------------------------------|------------|-------------------------------------|------------|
| | \$ in millions (unaudited) | % of total | \$ in millions (unaudited) | % of total |
| Institutional | \$75,008 | 65.3 % | \$68,716 | 66.2 % |
| Intermediary | 34,754 | 30.3 % | 30,158 | 29.1 % |
| Retail | 5,054 | 4.4 % | 4,888 | 4.7 % |
| Ending Assets Under Management | \$114,816 | 100.0% | \$103,762 | 100.0% |

⁽¹⁾ The allocation of assets under management by distribution channel involves the use of estimates and the exercise of judgment.

Our institutional channel includes assets under management sourced from defined contribution plan clients, which makes up approximately 13% of our total assets under management as of March 31, 2018.

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The following tables set forth the changes in our assets under management for Artisan Funds, Artisan Global Funds and separate accounts:

| Three Months Ended | Artisan Funds & Artisan Global Funds | Separate Accounts | Total |
|------------------------------------|--|----------------------|-----------|
| March 31, 2018 | (unaudited; in millions) | | |
| Beginning assets under management | \$57,349 | \$58,145 | \$115,494 |
| Gross client cash inflows | 4,538 | 881 | 5,419 |
| Gross client cash outflows | (3,458) | (2,564) | (6,022) |
| Net client cash flows | 1,080 | (1,683) | (603) |
| Market appreciation (depreciation) | (243) | 168 | (75) |
| Net transfers ⁽¹⁾ | (236) | 236 | — |
| Ending assets under management | \$57,950 | \$56,866 | \$114,816 |
| Average assets under management | \$58,876 | \$59,399 | \$118,275 |
| March 31, 2017 | | | |
| Beginning assets under management | \$49,367 | \$47,478 | \$96,845 |
| Gross client cash inflows | 3,825 | 1,335 | 5,160 |
| Gross client cash outflows | (4,146) | (1,286) | (5,432) |
| Net client cash flows | (321) | 49 | (272) |
| Market appreciation (depreciation) | 3,555 | 3,634 | 7,189 |
| Net transfers ⁽¹⁾ | (46) | 46 | — |
| Ending assets under management | \$52,555 | \$51,207 | \$103,762 |
| Average assets under management | \$51,678 | \$49,454 | \$101,132 |

⁽¹⁾ Net transfers represent certain amounts that we have identified as having been transferred out of one investment strategy or investment vehicle and into another strategy or vehicle.

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Results of Operations

Three months ended March 31, 2018, Compared to Three months ended March 31, 2017

| | For the Three Months Ended March 31, | | For the Period-to-Period | | |
|---|---|------------|--------------------------|-------|---|
| | 2018 | 2017 | \$ | % | |
| Statements of operations data: | (unaudited; in millions, except per share data) | | | | |
| Revenues | \$212.0 | \$ 184.1 | \$27.9 | 15 | % |
| Operating Expenses | | | | | |
| Total compensation and benefits | 105.2 | 99.6 | 5.6 | 6 | % |
| Other operating expenses | 26.8 | 26.5 | 0.3 | 1 | % |
| Total operating expenses | 132.0 | 126.1 | 5.9 | 5 | % |
| Total operating income | 80.0 | 58.0 | 22.0 | 38 | % |
| Non-operating income (loss) | | | | | |
| Interest expense | (2.8) | (2.9) | 0.1 | 3 | % |
| Other non-operating income | 6.7 | 0.2 | 6.5 | 3,250 | % |
| Total non-operating income (loss) | 3.9 | (2.7) | 6.6 | 244 | % |
| Income before income taxes | 83.9 | 55.3 | 28.6 | 52 | % |
| Provision for income taxes | 12.2 | 12.7 | (0.5) | (4) | % |
| Net income before noncontrolling interests | 71.7 | 42.6 | 29.1 | 68 | % |
| Less: Noncontrolling interests - Artisan Partners Holdings | 26.1 | 22.8 | 3.3 | 14 | % |
| Less: Noncontrolling interests - consolidated investment products | 4.3 | — | 4.3 | 100 | % |
| Net income attributable to Artisan Partners Asset Management Inc. | \$41.3 | \$ 19.8 | \$21.5 | 109 | % |
| Per Share Data | | | | | |
| Net income available to Class A common stock per basic and diluted share | \$0.75 | \$ 0.37 | | | |
| Weighted average basic and diluted shares of Class A common stock outstanding | 47,360,438 | 48,019,598 | | | |

Revenues

Essentially all of our revenues consist of investment management fees earned from managing clients' assets. Our investment management fees fluctuate based on a number of factors, including the total value of our assets under management, the composition of assets under management among investment vehicles and our investment strategies, changes in the investment management fee rates on our products, the extent to which we enter into fee arrangements that differ from our standard fee schedules, which can be affected by custom and the competitive landscape in the relevant market, and, for the accounts on which we earn performance-based fees, the investment performance of those accounts relative to their designated benchmarks.

The increase in revenues of \$27.9 million, or 15%, for the three months ended March 31, 2018, compared to the three months ended March 31, 2017, was driven primarily by a \$17.1 billion, or 17%, increase in our average assets under management, partially offset by a decline in the weighted average investment management fee. The weighted average investment management fee of 72.8 basis points for the three months ended March 31, 2018 decreased from 73.7 basis points for the three months ended March 31, 2017, primarily due to the increase in the proportion of total assets managed in separate accounts.

The following table sets forth the weighted average fee and composition of revenue and assets under management by investment vehicle:

| | Separate Accounts | | Artisan Funds and Artisan Global Funds | |
|--------------------------------------|----------------------------------|------|--|------|
| | 2018 | 2017 | 2018 | 2017 |
| For the Three Months Ended March 31, | (unaudited; dollars in millions) | | | |

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| | | | | |
|----------------------------|--------|--------|---------|---------|
| Investment management fees | \$78.2 | \$66.7 | \$133.8 | \$117.4 |
| | 53.5 | 54.5 | 92.2 | 92.1 |
| Weighted average fee | basis | basis | basis | basis |
| | points | points | points | points |
| Percentage of ending AUM | 50 | % 49 | % 50 | % 51 |
| | | % | % | % |

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Separate account assets under management consist of the assets we manage in or through vehicles other than Artisan Funds or Artisan Global Funds, including assets we manage in traditional separate accounts, as well as assets we manage in Artisan-branded collective investment trusts, in funds (both public and private) that we sub-advise, and in our own privately offered funds.

Operating Expenses

The increase in total operating expenses of \$5.9 million for the three months ended March 31, 2018, compared to the three months ended March 31, 2017, was primarily as a result of higher compensation expense due to increased revenues and additional post-IPO equity grants. These increases were partially offset by the elimination of pre-offering related equity compensation expense in 2017.

Compensation and Benefits

| | For the Three Months Ended March 31, | | Period-to-Period | | |
|--|--------------------------------------|--------|------------------|-------|---|
| | 2018 | 2017 | \$ | % | |
| | (unaudited; in millions) | | | | |
| Salaries, incentive compensation and benefits ⁽¹⁾ | \$91.4 | \$81.5 | \$9.9 | 12 | % |
| Restricted share-based award compensation expense | 13.8 | 11.8 | 2.0 | 17 | % |
| Total salaries, incentive compensation and benefits | 105.2 | 93.3 | 11.9 | 13 | % |
| Pre-offering related compensation - share-based awards | — | 6.3 | (6.3) | (100) | % |
| Total compensation and benefits | \$105.2 | \$99.6 | \$5.6 | 6 | % |

⁽¹⁾ Excluding restricted share-based award compensation expense

The increase in salaries, incentive compensation, and benefits was driven primarily by a \$8.5 million increase in incentive compensation paid to our investment and marketing professionals as a result of the increase in revenue. Restricted share-based award compensation expense increased \$2.0 million primarily as a result of our February 2018 grant of 1,510,570 restricted stock awards and 1,250 restricted stock units of Class A common stock to certain of our employees. Total compensation expense associated with the 2018 grants is expected to be approximately \$59.5 million over the recognition period.

Pre-offering related compensation expense, which consists of the amortization expense on pre-offering Class B awards, decreased \$6.3 million as the remaining awards became fully vested during 2017. As of July 1, 2017, all Class B awards were fully vested.

Total salaries, incentive compensation and benefits was 50% and 51% of our revenues for the three months ended March 31, 2018, and 2017, respectively.

Non-Operating Income (Loss)

Non-operating income (loss) for the three months ended March 31, 2018 includes \$6.3 million of income related to investment gains of consolidated investment products and \$0.3 million of income related to investment gains on unconsolidated investment products.

Provision for Income Taxes

The provision for income taxes primarily represents APAM's U.S. federal, state and local income taxes on its allocable portion of Holdings' income, as well as foreign income taxes payable by Holdings' subsidiaries. APAM's effective income tax rate for the three months ended March 31, 2018 was 14.6%. The decrease in effective income tax rate from 23.1% for the three months ended March 31, 2017 was primarily due to Tax Reform, which reduced the U.S. federal corporate tax rate from 35% to 21%. The 2018 effective tax rate was also lower than 2017 due to pre-IPO share-based compensation expenses incurred in 2017 that were not deductible for tax purposes. Pre-IPO share-based compensation expenses and the related impact to the effective tax rate no longer exist after the awards were fully vested on July 1, 2017.

Several factors contribute to the effective tax rate, including a rate benefit attributable to the fact that approximately 33% and 39% of Holdings' full year projected taxable earnings were not subject to corporate-level taxes for the three

months ended March 31, 2018 and 2017, respectively. Thus, income before income taxes includes amounts that are attributable to noncontrolling interests and not taxable to APAM and its subsidiaries, which reduces the effective tax rate. As APAM's equity ownership in Holdings increases, the effective tax rate will likewise increase as more income will be subject to corporate-level taxes. The effective tax rate in both periods was also lower than the statutory rate due to dividends paid on unvested share-based awards.

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Earnings Per Share

Weighted average basic and diluted shares of Class A common stock outstanding were higher for the three months ended March 31, 2018, compared to the three months ended March 31, 2017, as a result of the 2018 Follow-On Offering, Holdings Common Unit Exchanges, and equity award grants. See Note 13, "Earnings Per Share" in the Notes to the Unaudited Consolidated Financial Statements for further discussion of earnings per share.

Supplemental Non-GAAP Financial Information

Our management uses non-GAAP measures (referred to as "adjusted" measures) of net income and operating income to evaluate the profitability and efficiency of the underlying operations of our business and as a factor when considering net income available for distributions and dividends. These adjusted measures remove the impact of (1) pre-offering related compensation, (2) net gain (loss) on the tax receivable agreements (if any), and (3) net investment gain (loss) of investment products. These adjustments also remove the non-operational complexities of our structure by adding back non-controlling interests and assuming all income of Artisan Partners Holdings is allocated to APAM.

Management believes these non-GAAP measures provide more meaningful information to analyze our profitability and efficiency between periods and over time. We have included these non-GAAP measures to provide investors with the same financial metrics used by management to manage the company.

Non-GAAP measures should be considered in addition to, and not as a substitute for, financial measures prepared in accordance with GAAP. Our non-GAAP measures may differ from similar measures used by other companies, even if similar terms are used to identify such measures. Our non-GAAP measures are as follows:

Adjusted net income represents net income excluding the impact of (1) pre-offering related compensation, (2) net gain (loss) on the tax receivable agreements (if any), and (3) net investment gain (loss) of investment products. Adjusted net income also reflects income taxes assuming the vesting of all unvested Class A share-based awards and as if all outstanding limited partnership units of Artisan Partners Holdings had been exchanged for Class A common stock of APAM on a one-for-one basis. Assuming full vesting and exchange, all income of Artisan Partners Holdings is treated as if it were allocated to APAM, and the adjusted provision for income taxes represents an estimate of income tax expense at an effective rate reflecting assumed federal, state, and local income taxes. The estimated adjusted effective tax rate was 23.5% for the three months ended March 31, 2018, and 37.0% for the three months ended March 31, 2017.

Adjusted net income per adjusted share is calculated by dividing adjusted net income by adjusted shares. The number of adjusted shares is derived by assuming the vesting of all unvested Class A share-based awards and the exchange of all outstanding limited partnership units of Artisan Partners Holdings for Class A common stock of APAM on a one-for-one basis.

Adjusted operating income represents the operating income of the consolidated company excluding pre-offering related compensation.

Adjusted operating margin is calculated by dividing adjusted operating income by total revenues.

Adjusted EBITDA represents adjusted net income before interest expense, income taxes, depreciation and amortization expense.

Pre-offering related compensation includes the amortization of unvested Class B common units of Artisan Partners Holdings that were granted before and were unvested at our IPO, which closed on March 12, 2013. As of July 1, 2017, all Class B common units of Artisan Partners Holdings were fully vested and expensed.

Net gain (loss) on the tax receivable agreements represents the income (expense) associated with the change in estimate of amounts payable under the tax receivable agreements entered into in connection with APAM's initial public offering and related reorganization.

Net investment gain (loss) of investment products represents the non-operating income (loss) related to the Company's seed investments, in both consolidated investment products and unconsolidated investment products. Excluding these non-operating market gains or losses on seed investments provides greater transparency to evaluate the profitability and efficiency of the underlying operations of the business.

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The following table sets forth, for the periods indicated, a reconciliation from GAAP financial measures to non-GAAP measures:

| | For the Three Months Ended March 31, 2018 2017 (unaudited; in millions, except per share data) | |
|---|---|--------|
| Reconciliation of non-GAAP financial measures: | | |
| Net income attributable to Artisan Partners Asset Management Inc. (GAAP) | \$41.3 | \$19.8 |
| Add back: Net income attributable to noncontrolling interests - Artisan Partners Holdings | 26.1 | 22.8 |
| Add back: Provision for income taxes | 12.2 | 12.7 |
| Add back: Pre-offering related compensation - share-based awards | — | 6.3 |
| Add back: Net (gain) loss on the tax receivable agreements | — | — |
| Add back: Net investment (gain) loss of investment products attributable to APAM | (2.0) | — |
| Less: Adjusted provision for income taxes | 18.3 | 22.8 |
| Adjusted net income (Non-GAAP) | \$59.3 | \$38.8 |
| Average shares outstanding | | |
| Class A common shares | 47.4 | 41.0 |
| Assumed vesting or exchange of: | | |
| Unvested Class A restricted share-based awards | 4.5 | 3.9 |
| Artisan Partners Holdings units outstanding (noncontrolling interest) | 24.6 | 30.3 |
| Adjusted shares | 76.5 | 75.2 |
| Basic and diluted earnings per share (GAAP) | | |
| Adjusted net income per adjusted share (Non-GAAP) | \$0.78 | \$0.52 |
| Operating income (GAAP) | | |
| Add back: Pre-offering related compensation - share-based awards | — | 6.3 |
| Adjusted operating income (Non-GAAP) | \$80.0 | \$64.3 |
| Operating margin (GAAP) | | |
| Adjusted operating margin (Non-GAAP) | 37.7 % | 31.5 % |
| Operating margin (Non-GAAP) | | |
| Adjusted operating margin (Non-GAAP) | 37.7 % | 35.0 % |
| Net income attributable to Artisan Partners Asset Management Inc. (GAAP) | | |
| Add back: Net income attributable to noncontrolling interests - Artisan Partners Holdings | 26.1 | 22.8 |
| Add back: Pre-offering related compensation - share-based awards | — | 6.3 |
| Add back: Net (gain) loss on the tax receivable agreements | — | — |
| Add back: Net investment (gain) loss of investment products attributable to APAM | (2.0) | — |
| Add back: Interest expense | 2.8 | 2.9 |
| Add back: Provision for income taxes | 12.2 | 12.7 |
| Add back: Depreciation and amortization | 1.2 | 1.3 |
| Adjusted EBITDA (Non-GAAP) | \$81.6 | \$65.8 |

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Liquidity and Capital Resources

Our working capital needs, including accrued incentive compensation payments, have been and are expected to be met primarily through cash generated by our operations. The assets and liabilities of consolidated investment products attributable to third-party investors do not impact our liquidity and capital resources. We have no right to the benefits from, nor do we bear the risks associated with, the assets and liabilities of consolidated investment products, beyond our direct equity investment and any investment management fees and incentive allocations earned. Accordingly, assets and liabilities of consolidated investment products attributable to third party investors are excluded from the amounts and discussions below. The following table shows our liquidity position as of March 31, 2018, and December 31, 2017.

| | March 31, 2018 | December 31, 2017 |
|---|-----------------------------|----------------------|
| | (unaudited; in millions) | |
| Cash and cash equivalents | \$200.8 | \$ 137.3 |
| Accounts receivable | \$74.8 | \$ 76.7 |
| Seed investments ⁽¹⁾ | \$42.4 | \$ 40.3 |
| Undrawn commitment on revolving credit facility | \$100.0 | \$ 100.0 |

⁽¹⁾ Seed investments includes investment securities in unconsolidated sponsored investment entities, as well as Artisan's direct equity investments in consolidated investment products.

We manage our cash balances in order to fund our day-to-day operations. Accounts receivable primarily represent investment management fees that have been earned, but not yet received from our clients. We perform a review of our receivables on a monthly basis to assess collectability. As of March 31, 2018, none of our receivables were considered uncollectable.

In August 2012, we issued \$200.0 million in unsecured notes and entered into a \$100.0 million five-year revolving credit facility. The notes were comprised of three series, Series A, Series B, and Series C, each with a balloon payment at maturity. The fixed interest rate on each series of unsecured notes is subject to a 100 basis point increase in the event Holdings receives a below-investment grade rating and any such increase will continue to apply until an investment grade rating is received.

In August 2017, we issued \$60 million of Series D notes and used the proceeds to repay the \$60 million Series A notes that matured on August 16, 2017. We also amended and extended the \$100 million revolving credit facility for an additional five-year period. The \$100.0 million revolving credit facility was unused as of and for the three months ended March 31, 2018.

In September 2017, we amended the 2012 Note Purchase Agreement with respect to the Series B and Series C notes that remain outstanding. Among other things, the amendment conformed certain terms and conditions applicable to the Series B and Series C notes to those applicable to the Series D notes.

These borrowings contain various restrictive covenants. Our failure to comply with any of the covenants could result in an event of default under the agreements, giving our lenders the ability to accelerate repayment of our obligations. We were in compliance with all debt covenants as of March 31, 2018.

Distributions and Dividends

Artisan Partners Holdings' distributions, including distributions to APAM for the three months ended March 31, 2018 and 2017, were as follows:

| | |
|--|------|
| For the Three Months Ended March 31, 2018 | 2017 |
|--|------|

| | (unaudited, in millions) | |
|--|-----------------------------|--------|
| Holdings Partnership Distributions to Limited Partners | \$22.7 | \$16.5 |
| Holdings Partnership Distributions to APAM | \$45.6 | \$21.7 |
| Total Holdings Partnership Distributions | \$68.3 | \$38.2 |

On April 26, 2018, we, acting as the general partner of Artisan Partners Holdings, declared a distribution of \$27.6 million, payable by Artisan Partners Holdings to holders of its partnership units, including us.

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APAM declared and paid the following dividends per share during the three months ended March 31, 2018 and 2017:

| Type of Dividend | Class of Stock | For the | |
|------------------|----------------|-----------|--------|
| | | Three | Months |
| | | Ended | |
| | | March 31, | |
| | | 2018 | 2017 |
| Quarterly | Class A Common | \$0.60 | \$0.60 |
| Special Annual | Class A Common | \$0.79 | \$0.36 |

On April 26, 2018, our board declared a quarterly dividend of \$0.60 per share of Class A common stock payable on May 31, 2018 to shareholders of record as of May 17, 2018.

Subject to board approval each quarter, we currently expect to pay a quarterly dividend during 2018. After the end of the year, our board will consider paying a special dividend that will take into consideration our annual adjusted earnings, business conditions and the amount of cash we want to retain at that time. Although we expect to pay dividends according to our dividend policy, we may not pay dividends according to our policy or at all. We expect that our management and board will consider changes to our dividend policy during the course of 2018, including consideration of a variable quarterly dividend.

Tax Receivable Agreements (“TRAs”)

In addition to funding our normal operations, we will be required to fund amounts payable under the TRAs that we entered into in connection with the IPO, which resulted in the recognition of a \$400.5 million liability as of March 31, 2018. The liability generally represents 85% of the tax benefits APAM expects to realize as a result of the merger of an entity into APAM as part of the IPO Reorganization, our purchase of partnership units from limited partners of Holdings and the exchange of partnership units (for shares of Class A common stock or other consideration). The estimated liability assumes no material changes in the relevant tax law and that APAM earns sufficient taxable income to realize all tax benefits subject to the TRAs. An increase or decrease in future tax rates will increase or decrease, respectively, the expected tax benefits APAM would realize and the amounts payable under the TRAs. Changes in the estimate of expected tax benefits APAM would realize and the amounts payable under the TRAs as a result of change in tax rates would be recorded in net income.

The liability will increase upon future purchases or exchanges of limited partnership units with the increase representing amounts payable under the TRAs equal to 85% of the estimated future tax benefits, if any, resulting from such purchases or exchanges. We intend to fund the payment of amounts due under the TRAs out of the reduced tax payments that APAM realizes in respect of the tax attributes to which the TRAs relate.

The actual increase in tax basis, as well as the amount and timing of any payments under these agreements, will vary depending upon a number of factors, including the timing of sales or exchanges by the holders of limited partnership units, the price of the Class A common stock at the time of such sales or exchanges, whether such sales or exchanges are taxable, the amount and timing of the taxable income APAM generates in the future and the tax rate then applicable and the portion of APAM’s payments under the TRAs constituting imputed interest or depreciable basis or amortizable basis. In certain cases, payments under the TRAs may be accelerated and/or significantly exceed the actual benefits we realize in respect of the tax attributes subject to the TRAs. In such cases, we intend to fund those payments with cash on hand, although we may have to borrow funds depending on the amount and timing of the payments. We expect to make payments of approximately \$36 million in 2018 related to the TRAs, \$27.3 million of which we paid on April 17, 2018.

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Cash Flows

| | For the Three Months Ended March 31, 2018 2017 (unaudited; in millions) | |
|--|---|----------|
| Cash, cash equivalents and restricted cash as of January 1 | \$ 159.8 | \$ 157.4 |
| Net cash provided by operating activities | 167.3 | 119.0 |
| Net cash provided by (used in) investing activities | (0.8) | 4.6 |
| Net cash used in financing activities | (80.1) | (58.2) |
| Cash, cash equivalents and restricted cash as of March 31 | \$ 246.2 | \$ 222.8 |

Net cash provided by operating activities increased \$48.3 million for the three months ended March 31, 2018 compared to the three months ended March 31, 2017, primarily due to timing differences in working capital accounts in addition to increased revenues and operating income resulting from an increase in average assets under management. Timing differences in working capital accounts increased operating cash flows by \$23.7 million for the comparative periods, primarily due to the timing of executive bonus payments. For the three months ended March 31, 2018, compared to the three months ended March 31, 2017, our operating income, excluding share-based and pre-offering related compensation expenses, increased \$17.7 million.

Investing activities consist primarily of acquiring and selling property and equipment, leasehold improvements and the purchase and sale of available-for-sale securities. Net cash used in investment activities increased \$5.4 million for the three months ended March 31, 2018 compared to the three months ended March 31, 2017, primarily due to a \$6.1 million decrease in net proceeds from the sale of investment securities.

Financing activities consist primarily of partnership distributions to non-controlling interests, dividend payments to holders of our Class A common stock, proceeds from the issuance of Class A common stock in follow-on offerings, payments to purchase Holdings partnership units, and payments of amounts owed under the tax receivable agreements. Net cash used by financing activities increased \$21.9 million for the three months ended March 31, 2018 compared to the three months ended March 31, 2017, primarily due to a \$29.5 million increase in dividends paid to holders of our Class A common stock and a \$6.2 million increase in distributions to limited partners, partially offset by \$14.7 million of contributions from non-controlling interests in our consolidated investment products.

Certain Contractual Obligations

As of March 31, 2018, there have been no material changes to our contractual obligations outside the ordinary course of business from those listed in the “Certain Contractual Obligations” table and related notes to the table in our Annual Report on Form 10-K for the year ended December 31, 2017, filed with the SEC on February 21, 2018, except for the increases in the TRA liability during the year.

As previously discussed in this report, the TRA liability increased from \$385.4 million at December 31, 2017 to \$400.5 million at March 31, 2018. Amounts payable under the TRAs will increase upon exchanges of Holdings units for our Class A common stock or sales of Holdings units to us, with the increase representing 85% of the estimated future tax benefits, if any, resulting from such exchanges or sales. The actual amount and timing of payments associated with our existing payable under the TRAs or future exchanges or sales, and associated tax benefits, will vary depending upon a number of factors as described under “Liquidity and Capital Resources.” As a result, the timing of payments by period is currently unknown. We expect to make payments of approximately \$36 million in 2018 related to the TRAs, \$27.3 million of which we paid on April 17, 2018.

Off-Balance Sheet Arrangements

As of March 31, 2018, we did not have any off-balance sheet arrangements that have, or are reasonably likely to have, a material current or future effect on our financial condition, results of operations, liquidity or capital resources.

Critical Accounting Policies and Estimates

There have been no updates to our critical accounting policies from those disclosed in Management’s Discussion and Analysis of Financial Condition and Results of Operations in our Form 10-K for the year ended December 31, 2017,

except for the impact of adopting the new revenue recognition standard.

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Revenue Recognition

Investment management fees are generally computed as a percentage of assets under management and are recognized as revenue at the end of each distinct service period. Fees for providing investment management services are computed and billed in accordance with the underlying investment management agreements, which is generally on a monthly or quarterly basis. Investment management fees are presented net of cash rebates and fees waived pursuant to contractual expense limitations of the funds or voluntary waivers.

A number of investment management agreements provide for performance-based fees or incentive allocations, collectively “performance fees”. Performance fees, if earned, are recognized upon completion of the contractually determined measurement period, which is generally quarterly or annually. Performance fees generally are not subject to claw back as a result of performance declines subsequent to the most recent measurement date.

Artisan accounts for asset management services as a single performance obligation that is satisfied over time, using a time-based measure of progress to recognize revenue. Customer consideration is variable due to the uncertainty of the value of assets under management during each distinct service period. At the end of each quarter, Artisan records revenue for the actual amount of investment management fees for that quarter because the uncertainty has been resolved.

Performance fees are subject to the uncertainty of market volatility, and as a result, the entire amount of the variable consideration related to performance fees is constrained until the end of each measurement period. At the end of the quarterly or annual measurement period, revenue is recorded for the actual amount of performance fees earned during that period because the uncertainty has been resolved

The investment management fees that we receive are calculated based on the values of the securities held in the accounts that we manage for our clients. For our U.S.-registered mutual fund clients and UCITS, including Artisan Funds and Artisan Global Funds, and for our own sponsored private funds, our fees are based on the values of the funds’ assets as determined for purposes of calculating their net asset values.

Securities held by U.S.-registered mutual funds, including Artisan Funds, are generally valued at closing market prices, or if closing market prices are not readily available or are not considered reliable, at a fair value determined under procedures established by the fund’s board (fair value pricing). A U.S.-registered mutual fund typically considers a closing market price not to be readily available, and therefore uses fair value pricing, if, among other things, the value of the security might have been materially affected by events occurring after the close of the market in which the security was principally traded but before the time for determination of the fund’s net asset value. A subsequent event might be a company-specific development, a development affecting an entire market or region, or a development that might be expected to have global implications. A significant change in securities prices in U.S. markets may be deemed to be such a subsequent event with respect to non-U.S. securities.

Values of securities determined using fair value pricing are likely to be different than they would be if only closing market prices were used. As a result, over short periods of time, the revenues we generate from U.S.-registered mutual funds, including Artisan Funds, may be different than they would be if only closing prices were used in valuing portfolio securities. Over longer time periods, the differences in our fees resulting from fair value pricing are not material.

For our separate account clients other than U.S.-registered mutual funds, our fees may be based, at the client’s option, on the values of the securities in the portfolios we manage as determined by the client (or its custodian or other service provider) or by us in accordance with valuation procedures we have adopted. The valuation procedures we have adopted generally use closing market prices in the markets in which the securities trade, without adjustment for

subsequent events except in unusual circumstances. We believe that our fees based on valuations determined under our procedures are not materially different from the fees we receive that are based on valuations determined by clients, their custodians or other service providers.

With the exception of the assets managed by our Credit team (which represented approximately 2.2% of our assets under management at December 31, 2017), the portfolios of Artisan Funds and Artisan Global Funds, as well as the portfolios we manage for our separate account clients, are invested principally in publicly-traded equity securities for which public market values are readily available, with a portion of each portfolio held in cash or cash-like instruments.

New or Revised Accounting Standards

See Part I, Item 1, Unaudited Consolidated Financial Statements - Note 2, "Summary of Significant Accounting Policies."

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Item 3. Qualitative and Quantitative Disclosures Regarding Market Risk

There have been no material changes in our Quantitative and Qualitative Disclosures Regarding Market Risk from those previously reported in our Form 10-K for the year ended December 31, 2017.

Item 4. Controls and Procedures

Disclosure Controls and Procedures

We maintain disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) of the Exchange Act, that are designed to ensure that information required to be disclosed in our reports filed or submitted under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our principal executive and principal financial officers, as appropriate, to allow for timely decisions regarding required disclosure.

Our management, including our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) at March 31, 2018. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures are effective.

Changes in Internal Control over Financial Reporting

There have been no changes in internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the quarter ended March 31, 2018, that have materially affected or are reasonably likely to materially affect our internal control over financial reporting.

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Part II — Other Information

Item 1. Legal Proceedings

In the normal course of business, we may be subject to various legal and administrative proceedings. Currently, there are no legal or administrative proceedings that management believes may have a material effect on our consolidated financial position, cash flows or results of operations.

Item 1A. Risk Factors

For a discussion of our potential risks and uncertainties, see the information under the heading “Risk Factors” in our latest annual report on Form 10-K, which is accessible on the SEC’s website at www.sec.gov.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Unregistered Sales of Equity Securities

As described in Note 8, “Stockholders’ Equity”, to the Unaudited Consolidated Financial Statements included in Part I of this report, upon termination of employment with Artisan, an employee-partner’s Class B common units are exchanged for Class E common units and the corresponding shares of APAM Class B common stock are canceled. APAM issues the former employee-partner a number of shares of APAM Class C common stock equal to the former employee-partner’s number of Class E common units. Class E common units are exchangeable for Class A common stock subject to the same restrictions and limitations on exchange applicable to the other common units of Holdings. During the three months ended March 31, 2018, 1,121,196 shares of Class B common stock were canceled, and 1,121,196 shares of Class C common stock were issued, as a result of the termination of employment of an employee-partner.

Item 3. Defaults Upon Senior Securities

None

Item 4. Mine Safety Disclosures

Not applicable

Item 5. Other Information

None.

Item 6. Exhibits

| Exhibit No. | Description |
|-------------|--|
| 31.1 | <u>Certification of the Company’s Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</u> |
| 31.2 | <u>Certification of the Company’s Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</u> |
| 32.1 | <u>Certification of the Company’s Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002</u> |
| 32.2 | <u>Certification of the Company’s Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002</u> |
| 101 | The following Extensible Business Reporting Language (XBRL) documents are collectively included herewith as Exhibit 101: (i) the Unaudited Condensed Consolidated Statements of Financial Condition as of March 31, 2018 and December 31, 2017; (ii) the Unaudited Consolidated Statements of Operations for the three months ended March 31, 2018 and 2017; (iii) the Unaudited Consolidated Statements of Comprehensive Income for the three months ended March 31, 2018 and 2017; (iv) the Unaudited Consolidated Statements of Changes in Stockholders’ Equity for the three months ended March 31, 2018 and 2017; (v) the Unaudited Consolidated Statements of Cash Flows for the three months ended March 31, 2018 and 2017 (vi) the Notes to Unaudited Consolidated Financial Statements as of and for the three months ended March 31, 2018 and 2017 |

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Artisan Partners Asset Management Inc.

Dated: May 2, 2018

By:

/s/ Eric R. Colson

Eric R. Colson

President, Chief Executive Officer and Chairman of the Board

(principal executive officer)

/s/ Charles J. Daley, Jr.

Charles J. Daley, Jr.

Executive Vice President, Chief Financial Officer and Treasurer

(principal financial and accounting officer)