

FEDERATED INVESTORS INC /PA/  
Form 10-Q  
April 26, 2013  
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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

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FORM 10-Q

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(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, 2013

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 001-14818

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Federated Investors, Inc.  
(Exact name of registrant as specified in its charter)

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|  |                                      |
|--|--------------------------------------|
| Pennsylvania   | 25-1111467                           |
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |
| Federated Investors Tower                                      | 15222-3779                           |
| Pittsburgh, Pennsylvania                                       | (Zip Code)                           |
| (Address of principal executive offices)                       |                                      |
| (Registrant’s telephone number, including area code)           | 412-288-1900                         |

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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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No .

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

|                         |                                     |                           |                          |
|-------------------------|-------------------------------------|---------------------------|--------------------------|
| Large accelerated filer | <input checked="" type="checkbox"/> | Accelerated filer         | <input type="checkbox"/> |
| Non-accelerated filer   | <input type="checkbox"/>            | Smaller reporting company | <input type="checkbox"/> |

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

Indicate the number of shares outstanding of each of the issuer’s classes of common stock, as of the last practicable date: As of April 23, 2013, the Registrant had outstanding 9,000 shares of Class A Common Stock and 104,783,754

shares of Class B Common Stock.

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## Special Note Regarding Forward-Looking Information

Certain statements in this report on Form 10-Q including those related to asset flows and business mix; obligations to make additional contingent payments pursuant to acquisition agreements; obligations to make additional payments pursuant to employment arrangements; legal proceedings; future cash needs and management's expectations regarding borrowing; future principal uses of cash; performance indicators; impact of accounting policies and new accounting pronouncements; concentration risk; indemnification obligations; the impact of increased regulation including potential rule proposals by the Securities and Exchange Commission affecting money market funds or action taken by the Financial Stability Oversight Council; the prospect of increased distribution-related expenses; management's expectations regarding fee waivers, the impact of interest rates on such waivers and the impact of such waivers on revenues and net income; the ability to raise additional capital; possible impairment charges and the various items set forth under the section entitled Risk Factors included in Federated's Annual Report on Form 10-K for the fiscal year ended December 31, 2012 constitute forward-looking statements, which involve known and unknown risks, uncertainties and other factors that may cause the actual results, levels of activity, performance or achievements of Federated Investors, Inc. (Federated) or industry results, to be materially different from any future results, levels of activity, performance or achievements expressed or implied by such forward-looking statements. Among other risks and uncertainties, market conditions may change significantly resulting in changes to Federated's asset flows and business mix, which may cause a decline in revenues and net income, result in impairments and increase the amount of fee waivers incurred by Federated. The obligation to make contingent payments is based on certain growth and fund performance targets and will be affected by the achievement of such targets and the obligation to make additional payments pursuant to employment arrangements is based on satisfaction of certain conditions set forth in those arrangements. Future cash needs and future uses of cash will be impacted by a variety of factors, including the number and size of any acquisitions, Federated's success in distributing its products, as well as potential changes in assets under management and/or changes in the terms of distribution and shareholder services contracts with intermediaries who offer Federated's products to customers. Federated's risks and uncertainties also include liquidity and credit risks in Federated's money market funds and revenue risk, which will be affected by yield levels in money market fund products, changes in fair values of assets under management and the ability of Federated to collect fees in connection with the management of such products. Many of these factors may be more likely to occur as a result of the increased scrutiny of the mutual fund industry by federal and state regulators and the recent and ongoing disruption in global

financial markets. As a result, no assurance can be given as to future results, levels of activity, performance or achievements and neither Federated nor any other person assumes responsibility for the accuracy and completeness of such statements in the future. For more information on these items, see the section entitled Risk Factors included in Federated's Annual Report on Form 10-K for the fiscal year ended December 31, 2012.

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## Part I. Financial Information

## Item 1. Financial Statements

## Consolidated Balance Sheets

(dollars in thousands)

(unaudited)

|   | March 31,<br>2013 | December 31,<br>2012 |
|---|-------------------|----------------------|
| <b>ASSETS</b>   |                   |                      |
| Current Assets  |                   |                      |
| Cash and cash equivalents   | \$56,427          | \$67,585             |
| Investments—affiliates  | 129,702           | 136,023              |
| Investments—consolidated investment companies   | 116,465           | 51,073               |
| Investments—other   | 4,263             | 3,947                |
| Receivables, net of reserve of \$58 and \$50, respectively                                      | 24,607            | 24,120               |
| Prepaid expenses  | 10,252            | 12,986               |
| Other current assets  | 4,531             | 4,328                |
| Total current assets  | 346,247           | 300,062              |
| Long-Term Assets  |                   |                      |
| Goodwill  | 648,824           | 648,820              |
| Renewable investment advisory rights  | 68,455            | 68,455               |
| Other intangible assets, net of accumulated amortization of \$44,922 and \$44,224, respectively | 9,884             | 10,582               |
| Property and equipment, net of accumulated depreciation of \$52,504 and \$50,910, respectively  | 40,737            | 38,912               |
| Other long-term assets  | 23,121            | 23,230               |
| Total long-term assets  | 791,021           | 789,999              |
| Total assets  | \$1,137,268       | \$1,090,061          |
| <b>LIABILITIES</b>  |                   |                      |
| Current Liabilities   |                   |                      |
| Short-term debt   | \$42,500          | \$42,500             |
| Accounts payable and accrued expenses   | 44,810            | 45,255               |
| Accrued compensation and benefits   | 23,445            | 68,172               |
| Other current liabilities   | 26,786            | 25,207               |
| Total current liabilities   | 137,541           | 181,134              |
| Long-Term Liabilities   |                   |                      |
| Long-term debt  | 265,625           | 276,250              |
| Long-term deferred tax liability, net   | 110,774           | 99,399               |
| Other long-term liabilities   | 24,345            | 29,334               |
| Total long-term liabilities   | 400,744           | 404,983              |
| Total liabilities   | 538,285           | 586,117              |
| Commitments and contingencies (Note (12))   |                   |                      |
| <b>TEMPORARY EQUITY</b>   |                   |                      |
| Redeemable noncontrolling interest in subsidiaries  | 78,931            | 7,268                |
| <b>PERMANENT EQUITY</b>   |                   |                      |
| Federated Investors shareholders' equity  |                   |                      |
| Common stock:   |                   |                      |
| Class A, no par value, 20,000 shares authorized, 9,000 shares issued and outstanding            | 189               | 189                  |
| Class B, no par value, 900,000,000 shares authorized, 129,505,456 shares issued                 | 279,584           | 273,697              |

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|  |             |              |
|--|-------------|--------------|
| Retained earnings  | 991,018     | 984,505      |
| Treasury stock, at cost, 24,721,702 and 25,064,280 shares Class B common stock, respectively | (751,418    | ) (760,022 ) |
| Accumulated other comprehensive loss, net of tax   | (436        | ) (2,937 )   |
| Total Federated Investors, Inc. shareholders' equity   | 518,937     | 495,432      |
| Nonredeemable noncontrolling interest in subsidiary  | 1,115       | 1,244        |
| Total permanent equity   | 520,052     | 496,676      |
| Total liabilities, temporary equity and permanent equity                                     | \$1,137,268 | \$1,090,061  |

(The accompanying notes are an integral part of these Consolidated Financial Statements.)

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Consolidated Statements of Income  
(dollars in thousands, except per share data)  
(unaudited)

|   | Three Months Ended |            |
|---|--------------------|------------|
|   | March 31,          |            |
|   | 2013               | 2012       |
| Revenue   |                    |            |
| Investment advisory fees, net—affiliates                                      | \$ 132,128         | \$ 133,519 |
| Investment advisory fees, net—other   | 18,635             | 15,829     |
| Administrative service fees, net—affiliates                                   | 56,828             | 57,292     |
| Other service fees, net—affiliates  | 16,188             | 19,642     |
| Other service fees, net—other   | 3,144              | 3,013      |
| Other, net  | 1,049              | 986        |
| Total revenue   | 227,972            | 230,281    |
| Operating Expenses  |                    |            |
| Compensation and related  | 66,937             | 64,065     |
| Distribution  | 58,240             | 61,693     |
| Professional service fees   | 8,844              | 10,308     |
| Systems and communications  | 6,623              | 6,310      |
| Office and occupancy  | 6,432              | 6,253      |
| Advertising and promotional   | 3,422              | 2,928      |
| Travel and related  | 2,686              | 2,751      |
| Intangible asset related  | 763                | 21         |
| Other   | 5,826              | 5,605      |
| Total operating expenses  | 159,773            | 159,934    |
| Operating income  | 68,199             | 70,347     |
| Nonoperating Income (Expenses)  |                    |            |
| Investment income, net  | 1,535              | 1,296      |
| Gain on securities, net   | 2,893              | 2,050      |
| Debt expense  | (3,253)            | ) (3,711)  |
| Other, net  | (40)               | ) (37)     |
| Total nonoperating income (expenses), net                                     | 1,135              | (402)      |
| Income before income taxes  | 69,334             | 69,945     |
| Income tax provision  | 24,646             | 25,538     |
| Net income including noncontrolling interests in subsidiaries                 | 44,688             | 44,407     |
| Less: Net income attributable to the noncontrolling interests in subsidiaries | 1,694              | 2,082      |
| Net income  | \$42,994           | \$42,325   |
| Amounts attributable to Federated Investors, Inc.                             |                    |            |
| Earnings per common share—Basic and Diluted                                   | \$0.41             | \$0.41     |
| Cash dividends per share  | \$0.24             | \$0.24     |

(The accompanying notes are an integral part of these Consolidated Financial Statements.)

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## Consolidated Statements of Comprehensive Income

(dollars in thousands)

(unaudited)

|  | Three Months Ended<br>March 31, |          |
|--|---------------------------------|----------|
|  | 2013                            | 2012     |
| Net income including noncontrolling interests in subsidiaries                                  | \$44,688                        | \$44,407 |
| Other comprehensive income, net of tax   |                                 |          |
| Permanent equity   |                                 |          |
| Reclassification adjustment and unrealized loss on interest rate swap                          | 1,049                           | 444      |
| Unrealized gain on securities available for sale and reclassification adjustment               | 1,483                           | 3,971    |
| Foreign currency items   | (31                             | ) 17     |
| Temporary equity   |                                 |          |
| Foreign currency translation (loss) gain   | (35                             | ) 24     |
| Other comprehensive income   | 2,466                           | 4,456    |
| Comprehensive income including noncontrolling interests in subsidiaries                        | 47,154                          | 48,863   |
| Less: Comprehensive income attributable to redeemable noncontrolling interest in subsidiaries  | 3                               | 38       |
| Less: Comprehensive income attributable to nonredeemable noncontrolling interest in subsidiary | 1,656                           | 2,068    |
| Comprehensive income attributable to Federated Investors, Inc.                                 | \$45,495                        | \$46,757 |

(The accompanying notes are an integral part of these Consolidated Financial Statements.)

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## Consolidated Statements of Changes in Equity

(dollars in thousands)

(unaudited)

|   | Federated Investors, Inc. Shareholders |                   |                |  |                            |   |                        |  |
|---|--|-------------------|----------------|--|----------------------------|---|------------------------|--|
|   | Common Stock                           | Retained Earnings | Treasury Stock | Accumulated Other Comprehensive Loss, Net of Tax | Total Shareholders' Equity | Nonredeemable Noncontrolling Interest in Subsidiary | Total Permanent Equity | Redeemable Noncontrolling Interest in Subsidiaries/ Temporary Equity |
| Balance at December 31, 2011  | \$253,139                              | \$1,069,913       | \$(772,481)    | \$(8,612)  | \$541,959                  | \$718   | \$542,677              | \$506  |
| Net income  | 0                                      | 42,325            | 0              | 0  | 42,325                     | 2,068   | 44,393                 | 14   |
| Other comprehensive income, net of tax                                      | 0                                      | 0                 | 0              | 4,432  | 4,432                      | 0   | 4,432                  | 24   |
| Subscriptions—redeemable noncontrolling interest holders                    | 0                                      | 0                 | 0              | 0  | 0                          | 0   | 0                      | 347  |
| Stock award activity  | 5,516                                  | (7,640)           | 7,640          | 0  | 5,516                      | 0   | 5,516                  | 0  |
| Dividends declared/Distributions to noncontrolling interest in subsidiaries | 0                                      | (24,900)          | 0              | 0  | (24,900)                   | (1,681)   | (26,581)               | (9)  |
| Purchase of treasury stock  | 0                                      | 0                 | (1,064)        | 0  | (1,064)                    | 0   | (1,064)                | 0  |
| Balance at March 31, 2012   | \$258,655                              | \$1,079,698       | \$(765,905)    | \$(4,180)  | \$568,268                  | \$1,105   | \$569,373              | \$882  |
| Balance at December 31, 2012  | \$273,886                              | \$984,505         | \$(760,022)    | \$(2,937)  | \$495,432                  | \$1,244   | \$496,676              | \$7,268  |
| Net income  | 0                                      | 42,994            | 0              | 0  | 42,994                     | 1,656   | 44,650                 | 38   |
| Other comprehensive income (loss), net of tax                               | 0                                      | 0                 | 0              | 2,501  | 2,501                      | 0   | 2,501                  | (35)   |
| Subscriptions—redeemable noncontrolling interest holders                    | 0                                      | 0                 | 0              | 0  | 0                          | 0   | 0                      | 5,024  |
| Consolidation   | 0                                      | 0                 | 0              | 0  | 0                          | 0   | 0                      | 67,384   |
| Stock award activity  | 5,887                                  | (11,314)          | 11,314         | 0  | 5,887                      | 0   | 5,887                  | 0  |
| Dividends declared/Distributions to noncontrolling interest in subsidiaries | 0                                      | (25,063)          | 0              | 0  | (25,063)                   | (1,785)   | (26,848)               | (748)  |
| Purchase of treasury stock  | 0                                      | 0                 | (2,710)        | 0  | (2,710)                    | 0   | (2,710)                | 0  |
| Other   | 0                                      | (104)             | 0              | 0  | (104)                      | 0   | (104)                  | 0  |
| Balance at March 31, 2013   | \$279,773                              | \$991,018         | \$(751,418)    | \$(436)  | \$518,937                  | \$1,115   | \$520,052              | \$78,931   |

(The accompanying notes are an integral part of these Consolidated Financial Statements.)



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Consolidated Statements of Cash Flows  
(dollars in thousands)  
(unaudited)

|  | Three Months Ended |           |
|--|--------------------|-----------|
|  | March 31,          |           |
|  | 2013               | 2012      |
| Operating Activities   |                    |           |
| Net income including noncontrolling interests in subsidiaries                    | \$44,688           | \$44,407  |
| Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities |                    |           |
| Amortization of deferred sales commissions                                       | 2,113              | 1,625     |
| Depreciation and other amortization  | 2,492              | 2,767     |
| Share-based compensation expense   | 5,714              | 5,583     |
| Gain on disposal of assets   | (2,928)            | ) (683    |
| Provision for deferred income taxes  | 10,132             | 10,716    |
| Fair-value adjustments for contingent liabilities                                | (48)               | ) (1,000  |
| Tax benefit (detriment) from share-based compensation                            | 173                | (67       |
| Excess tax benefits from share-based compensation                                | (463)              | ) (463    |
| Net purchases of trading securities  | (1,145)            | ) (753    |
| Deferred sales commissions paid  | (3,157)            | ) (3,090  |
| Contingent deferred sales charges received                                       | 425                | 352       |
| Other changes in assets and liabilities:   |                    |           |
| Increase in receivables, net   | (487)              | ) (1,925  |
| Decrease in prepaid expenses and other assets                                    | 7,017              | 4,501     |
| Decrease in accounts payable and accrued expenses                                | (48,710)           | ) (36,449 |
| Increase in other liabilities  | 3,957              | 4,735     |
| Net cash provided by operating activities  | 19,773             | 30,256    |
| Investing Activities   |                    |           |
| Purchases of securities available for sale                                       | (859)              | ) (766    |
| Cash paid for business acquisitions  | (3,365)            | ) (5,868  |
| Proceeds from redemptions of securities available for sale                       | 11,758             | 17,949    |
| Cash paid for property and equipment   | (3,083)            | ) (1,656  |
| Net cash provided by investing activities  | 4,451              | 9,659     |
| Financing Activities   |                    |           |
| Dividends paid   | (25,063)           | ) (24,900 |
| Purchases of treasury stock  | (2,473)            | ) (1,133  |
| Distributions to noncontrolling interest in subsidiaries                         | (2,533)            | ) (1,690  |
| Contributions from noncontrolling interest in subsidiaries                       | 5,024              | 347       |
| Excess tax benefits from share-based compensation                                | 463                | 463       |
| Payments on debt   | (10,625)           | ) (10,625 |
| Other financing activities   | (175)              | ) (125    |
| Net cash used by financing activities  | (35,382)           | ) (37,663 |
| Net (decrease) increase in cash and cash equivalents                             | (11,158)           | ) 2,252   |
| Cash and cash equivalents, beginning of period                                   | 67,585             | 49,273    |
| Cash and cash equivalents, end of period   | \$56,427           | \$51,525  |

(The accompanying notes are an integral part of these Consolidated Financial Statements.)

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(unaudited)

## (1) Basis of Presentation

The interim consolidated financial statements of Federated Investors, Inc. and its subsidiaries (collectively, Federated) included herein have been prepared in accordance with U.S. generally accepted accounting principles (GAAP). In the opinion of management, the financial statements reflect all adjustments that are of a normal recurring nature and necessary for a fair presentation of the results for the interim periods presented.

In preparing the financial statements, management is required to make estimates and assumptions that affect the amounts reported in the Consolidated Financial Statements and accompanying notes. Actual results may differ from such estimates and such differences may be material to the Consolidated Financial Statements.

These financial statements should be read in conjunction with Federated's Annual Report on Form 10-K for the year ended December 31, 2012. Certain items previously reported have been reclassified to conform to the current period's presentation.

## (2) Significant Accounting Policies

For a listing of Federated's significant accounting policies, please refer to Federated's Annual Report on Form 10-K for the year ended December 31, 2012.

## (3) Recent Accounting Pronouncements

## Comprehensive Income

Effective January 1, 2013, Federated adopted a Financial Accounting Standards Board (FASB) accounting standards update relating to the presentation of comprehensive income. The update requires disclosure of the changes in accumulated other comprehensive income balances by component as well as additional disclosure related to amounts reclassified out of accumulated other comprehensive income. See Note (13) for this new disclosure. As the update affected disclosure only, the adoption of the update did not have a financial impact on Federated's Consolidated Financial Statements.

## (4) Concentration Risk

## (a) Revenue Concentration by Asset Class

The following table summarizes the percentage of total revenue earned from Federated's asset classes for the periods presented:

|                     | Three Months Ended |      |   |
|---------------------|--------------------|------|---|
|                     | March 31,          |      |   |
|                     | 2013               | 2012 |   |
| Money market assets | 43                 | % 46 | % |
| Equity assets       | 33                 | % 32 | % |
| Fixed-income assets | 23                 | % 21 | % |

The decline in the relative proportion of Federated's revenue attributable to money market assets from March 31, 2012 to March 31, 2013 was primarily the result of increases in fee waivers for certain money market funds to maintain positive or zero net yields. A significant change in Federated's money market business or a significant reduction in money market assets due to regulatory changes, changes in the financial markets including significant and rapid

increases in interest rates over a short period of time causing certain investors to prefer direct investments in interest-bearing securities, significant deterioration in investor confidence, further persistent declines in or additional prolonged periods of historically low short-term interest rates and resulting fee waivers or other circumstances, could have a material adverse effect on Federated's results of operations.

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Notes to the Consolidated Financial Statements (continued)  
(unaudited)

Current Regulatory Environment - Domestic

In January 2010, the Securities and Exchange Commission (SEC) adopted extensive amendments to Rule 2a-7 of the Investment Company Act of 1940 (Rule 2a-7) aimed at enhancing the resiliency of money market funds. These amendments included a series of enhancements including rules that require all money market funds to meet specific portfolio liquidity standards and rules that significantly enhance the public disclosure and regulatory reporting obligations of these funds. In 2010 and 2011, Federated dedicated internal resources to comply with these amendments including efforts to enhance its information systems and improve related reporting capabilities. These efforts were internally sourced and not material to Federated's financial position, results of operations or cash flows for those years. In Federated's view, the amendments of 2010 meaningfully and sufficiently strengthen money market funds. Recent experience demonstrated that the amendments of 2010 were effective in meeting heightened requests for redemptions occurring in connection with the U.S. credit rating downgrade in 2011 and the ongoing European debt crisis.

More recently, the SEC undertook a project to develop a proposal for additional reforms related to money market funds. In August 2012, then SEC Chairman Mary Schapiro issued a public statement announcing that she did not have sufficient votes from the other SEC commissioners to pursue certain proposed reforms relating to money market funds. In her statement, Ms. Schapiro stated that the SEC had been considering two alternative reform proposals, one which would have required a floating net asset value (NAV) and the other which would have imposed capital requirements coupled with some form of redemption restriction. In her statement, she invited other policymakers to take up the issue of reform. On September 27, 2012, then Treasury Secretary Timothy Geithner sent a letter to the members of the Financial Stability Oversight Council (FSOC) announcing his intent to pursue money market fund reform. His letter urged FSOC to use its authority under Section 120 of the Dodd-Frank Act to recommend that the SEC proceed with money market reform. Mr. Geithner outlined three potential options for reform in his letter and stated that he had asked his staff to begin drafting a formal recommendation for FSOC to consider at its November 2012 meeting.

In November 2012, FSOC issued Proposed Recommendations Regarding Mutual Fund Reform citing its authority under Section 120 of the Dodd-Frank Act (Proposed Recommendations). The Proposed Recommendations are in draft form and were subject to a public comment period which ended on February 15, 2013. The Proposed Recommendations include three main alternatives: a floating NAV for money market funds; an NAV capital buffer and minimum balance at risk (or 30-day hold back of up to 3% on certain redemptions); and an NAV capital buffer combined with other measures. In response to the Proposed Recommendations, Federated has filed multiple comment letters on the Proposed Recommendations pointing out, among other things, that: (1) FSOC exceeded its authority in how it used the Section 120 process; (2) FSOC has not provided justification for further reform efforts; (3) a floating NAV would not prevent "runs" on money market funds; (4) an NAV capital buffer of the kind proposed is impractical and not economically attainable in the current interest rate environment; and (5) the minimum-balance-at-risk concept would impair the utility of money market funds to investors and would be prohibitively costly for both fund groups and intermediaries to implement.

On November 30, 2012, the SEC Staff issued a study entitled Response to Questions Posed by Commissioners Aguilar, Parades and Gallagher. This study responded to questions posed by the Commissioners in response to potential reform measures being advanced by then SEC Chairman Mary Shapiro. The study addressed certain misconceptions about the role of money market funds in the financial crisis of 2008 and confirmed the effectiveness of the 2010 amendments to Rule 2a-7. Federated also filed a comment letter on the study commending the SEC Staff for its work while raising questions on some aspects of the study and recommending further analysis.

It has been reported that the SEC Staff is working on its own rule proposal and that proposal could include a floating NAV for certain money market funds, in particular prime funds. It could also include a floating NAV proposal for all money market funds as well as other reform measures. In April 2013, Commissioner Daniel Gallagher stated that the SEC Staff is actively working on the proposal and that he expects the SEC to issue the proposal in the "near term."

Federated believes the potential changes summarized above, if enacted, would significantly reduce the utility and attractiveness of money market funds for investors who, in Federated's view, value money market funds in their current form as an efficient and effective cash management investment product offering daily liquidity at par. If ultimately enacted, some or all of these changes would be detrimental to Federated's money market fund business and could materially and adversely affect Federated's operations. The very proposal of such amendments could have an adverse impact on Federated's money market fund business and operations and could also negatively impact the short-term credit markets.

Management is carefully monitoring developments in this area and plans to actively participate both individually and with industry groups in the public comment process that would accompany any rule change proposal. Federated is unable to assess the degree of any potential impact such additional reforms may have on its business and operations until such proposals are

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Notes to the Consolidated Financial Statements (continued)  
(unaudited)

issued. Even when issued, the final version of any rule amendment could vary significantly from the form in which it is proposed.

**Current Regulatory Environment - International**

The European Union (EU) recently agreed to allow certain of its members to move forward in drafting a proposal that would establish a financial transactions tax (FTT) in those countries. Preliminary details of the FTT include a 0.1 percent tax on trades in certain financial instruments, and a 0.01 percent tax on the notional value of derivatives trades, subject to certain limited exemptions. The imposition of the FTT and the potential breadth of its application could adversely impact the operations of a wide array of Federated products, including Federated's Irish- and U.K.-domiciled Undertakings for Collective Investment in Transferable Securities products, as well as Federated's domestic money market and fixed-income funds. Final terms of the proposed FTT will be subject to additional government approval prior to enactment.

In addition, European-based money market funds face regulatory reform pressure in Europe similar to that faced in the U.S. The European Commission has reportedly prepared a draft reform proposal which could include a floating NAV for money market funds and/or capital requirements.

Federated is unable to assess the degree of any potential impact such proposals may have on its business and operations until such proposals are issued. Even when issued, the final version of any rule amendment could vary significantly from the form in which it is proposed.

**Historically Low Short-Term Interest Rates**

For several years, the Federal Reserve has kept the near-zero federal funds rate unchanged and short-term interest rates continued at all-time low levels. In certain money market funds, the gross yield earned by the fund is not sufficient to cover all of the fund's operating expenses due to these historically low short-term interest rates. Since the fourth quarter 2008, Federated has voluntarily waived fees in order for certain funds to maintain positive or zero net yields. These fee waivers have been partially offset by related reductions in distribution expense and net income attributable to noncontrolling interests as a result of Federated's mutual understanding and agreement with third-party intermediaries to share the impact of the waivers.

These voluntary fee waivers are calculated as a percent of assets under management (AUM or managed assets) in certain money market funds and thus will vary dependent upon the asset levels in such funds. In addition, the level of waivers are dependent on several other factors including, but not limited to, available yields on instruments held by the money market funds, changes in expenses of the money market funds and changes in the mix of money market assets. In any given period, a combination of these factors drives the amount of fee waivers necessary in order for certain funds to maintain positive or zero net yields. As an isolated variable, an increase in yields on instruments held by the money market funds will cause the pre-tax impact of fee waivers to decrease. Conversely, as an isolated variable, an increase in expenses of the money market fund would cause the pre-tax impact of fee waivers to increase.

With regard to asset mix, changes in the relative amount of money market fund assets in prime and government money market funds as well as the distribution among certain share classes that vary in pricing structure will impact the level of fee waivers. Generally, prime money market funds waive less than government money market funds as a result of higher gross yields on the underlying investments. As such, as an isolated variable, an increase in the relative proportion of average managed assets invested in prime money market funds as compared to total average money market fund assets should typically result in lower waivers to maintain positive or zero net yields. Conversely, the opposite would also be true.

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The impact of such fee waivers on various components of Federated's Consolidated Statements of Income was as follows for the periods presented:

| (in millions)                              | Three Months Ended<br>March 31, |            |
|--|---------------------------------|------------|
|  | 2013                            | 2012       |
| Revenue                                    | \$ (87.3 )                      | \$ (80.4 ) |
| Less: Reduction in Distribution expense    | 64.8                            | 57.5       |
| Operating income                           | (22.5 )                         | (22.9 )    |
| Less: Reduction in Noncontrolling interest | 0.8                             | 0.6        |
| Pre-tax impact                             | \$(21.7 )                       | \$(22.3 )  |

The negative pre-tax impact of fee waivers to maintain positive or zero net yields on certain money market funds decreased for the first quarter 2013 as compared to the same quarter of 2012 primarily as a result of a change in the mix of average money market assets in addition to the impact of the leap year in 2012 compared to 2013.

Based on recent commentary from the Federal Reserve Bank in its March 20, 2013 press release, "the current highly accommodative stance of monetary policy will remain appropriate for a considerable time..." Federated is unable to predict when the Federal Reserve will increase its target for the federal funds rate. As such, fee waivers to maintain positive or zero net yields on certain money market funds and the related reduction in distribution expense and net income attributable to noncontrolling interests could continue for the foreseeable future. Assuming asset levels and mix remain constant and based on recent market conditions, fee waivers for the second quarter 2013 may result in a negative pre-tax impact on income of a similar amount as the first quarter 2013. See Management's Discussion and Analysis for additional information on management's expectations regarding fee waivers. While the level of fee waivers are impacted by various factors, increases in short-term interest rates that result in higher yields on securities purchased in money market fund portfolios would reduce the negative pre-tax impact of these waivers. The actual amount of future fee waivers are contingent on a number of variables including, but not limited to, changes in assets within the money market funds, available yields on instruments held by the money market funds, actions by the Federal Reserve, the U.S. Department of the Treasury, the SEC, FSOC and other governmental entities, changes in expenses of the money market funds, changes in the mix of money market customer assets, Federated's willingness to continue the fee waivers and changes in the extent to which the impact of the waivers is shared by third parties.

## (b) Revenue Concentration by Investment Fund

A significant portion of Federated's total revenue for the three-month period ended March 31, 2013 was derived from services provided to two sponsored funds, the Federated Prime Obligations Fund (10%) and the Federated Kaufmann Fund (10%). A significant and prolonged decline in the AUM in these funds could have a material adverse effect on Federated's future revenues and, to a lesser extent, net income, due to a related reduction to distribution expenses associated with these funds.

A listing of Federated's risk factors is included in Federated's Annual Report on Form 10-K for the fiscal year ended December 31, 2012.

## (5) Variable Interest Entities

Federated is involved with various entities in the normal course of business that may be deemed to be voting rights entities (VREs) or variable interest entities (VIEs). In accordance with Federated's consolidation accounting policy, Federated first determines whether the entity being evaluated is a VRE or a VIE. Once this determination is made, Federated proceeds with its evaluation of whether or not to consolidate the entity. The disclosures below represent the

results of such evaluations pertaining to March 31, 2013 and December 31, 2012.

(a) Consolidated Variable Interest Entities

From time to time, Federated invests in investment companies that meet the definition of a VIE for general corporate investment purposes or, in the case of newly launched products, in order to provide investable cash to establish a performance history. Most of Federated's sponsored investment companies meet the definition of a VIE primarily due to their typical series

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fund structure in which the shareholders of each participating portfolio underlying the series fund generally lack the ability as an individual group to make decisions through voting rights regarding the board of directors/trustees of the fund. Federated's investment in investment companies represents its maximum exposure to loss. Federated's conclusion to consolidate an investment company may vary from period to period, most commonly as a result of changes in its percentage interest in the entity resulting from changes in the number of shares held by either Federated or third parties. Given that the entities follow investment company accounting, which prescribes fair-value accounting, a deconsolidation generally does not result in gains or losses for Federated.

As of March 31, 2013 and December 31, 2012, Federated was deemed to be the primary beneficiary of and therefore consolidated several investment companies as a result of its majority ownership interest in the investment companies. In addition, during the quarter ended March 31, 2013, Federated consolidated a sponsored offshore fund for which it was deemed to be the primary beneficiary as a result of a vote by the fund board of directors to unwind the fund in the near term and the expectation that Federated will absorb the remaining net operating expenses of the fund. The total net operating expenses to be absorbed by Federated are estimated at \$50 thousand. The following table presents the balances related to the consolidated investment companies that were included on the Consolidated Balance Sheets as well as Federated's net interest in the investment companies for each period presented:

| (in millions)   | March 31, 2013 | December 31,<br>2012 |
|---|----------------|----------------------|
| Cash and cash equivalents                                     | \$4.9          | \$1.0                |
| Investments—consolidated investment companies                 | 116.5          | 51.1                 |
| Receivables   | 0.7            | 0.7                  |
| Less: Liabilities   | 2.2            | 2.0                  |
| Less: Redeemable noncontrolling interest in subsidiaries      | 78.9           | 7.3                  |
| Federated's net interest in consolidated investment companies | \$41.0         | \$43.5               |

Federated's net interest in the consolidated investment companies of \$41.0 million and \$43.5 million at March 31, 2013 and December 31, 2012, respectively, represents the value of Federated's economic ownership interest in these sponsored investment companies. The assets of the consolidated investment companies are restricted for use by the respective investment company. The liabilities of the consolidated investment companies primarily represent operating liabilities of the entities and, in the case of one fund, investments sold short and are primarily classified as Other current liabilities on Federated's Consolidated Balance Sheets.

Federated did not deconsolidate any investment companies during either of the three-month periods ended March 31, 2013 or 2012.

Neither creditors nor equity investors in the investment companies have any recourse to Federated's general credit. In the ordinary course of business, from time to time, Federated may choose to waive certain fees or assume operating expenses of sponsored investment companies for competitive, regulatory or contractual reasons (see Note (1)(o) of Federated's Annual Report on Form 10-K for the year ended December 31, 2012 for information regarding fee waivers). Federated has not provided financial support to any of these entities outside the ordinary course of business.

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## (b) Non-Consolidated Variable Interest Entities

At March 31, 2013 and December 31, 2012, Federated was involved with certain VIEs in which it held a variable interest but for which it was not the primary beneficiary. The assets and liabilities of these unconsolidated VIEs and Federated's maximum risk of loss related thereto were as follows:

| (in millions)                        | March 31, 2013               |                                   | Total<br>remaining<br>carrying value<br>of investment<br>and maximum<br>risk of loss | December 31, 2012            |                                   | Total<br>remaining<br>carrying value<br>of investment<br>and maximum<br>risk of loss |
|--------------------------------------|------------------------------|-----------------------------------|--|------------------------------|-----------------------------------|--|
|                                      | Unconsolidated<br>VIE assets | Unconsolidated<br>VIE Liabilities |  | Unconsolidated<br>VIE assets | Unconsolidated<br>VIE Liabilities |  |
| Investment<br>companies <sup>1</sup> | \$284,264.3                  | \$—                               | \$176.4  | \$295,414.3                  | \$—                               | \$205.3  |
| Equity investment                    | \$2.4                        | \$0.2                             | \$3.8  | \$2.8                        | \$0.3                             | \$3.8  |

<sup>1</sup> The unconsolidated VIE assets for the investment companies represent total net AUM for the related investment companies.

Investment Companies – Federated's involvement with certain investment companies that are deemed to be VIEs includes serving as the investment manager, or at times, holding a minority interest or both. Federated's variable interest is not deemed to absorb the majority of the variability of the entity's net assets. Therefore, Federated is not the primary beneficiary of these VIEs and has not consolidated these entities.

In the ordinary course of business, from time to time, Federated may choose to waive certain fees or assume operating expenses of these sponsored investment companies for competitive, regulatory or contractual reasons (see Note (1)(o) of Federated's Annual Report on Form 10-K for the year ended December 31, 2012 for information regarding fee waivers). Federated has not provided financial support to any of these entities outside the ordinary course of business.

Equity Investment – Federated holds a 12% non-voting, noncontrolling interest in a privately-held investment management firm that is registered as an investment adviser and a commodity trading adviser. This investment is accounted for using the equity-method of accounting. As of March 31, 2013, the equity-method investee managed over \$400 million in both absolute return and enhanced fixed-income mandates, including a hedge fund strategy and an enhanced cash strategy. Due primarily to the nature of the voting rights of the equity holders of the investee, the investee meets the definition of a VIE, however, with its non-voting 12% interest, Federated is not deemed to have power to direct the investee's activities and therefore is not the primary beneficiary. Federated has not provided financial support to the investee. Federated's investment is included in Other long-term assets on the Consolidated Balance Sheets. In 2012, Federated recorded a \$3.0 million impairment charge to write down the investment to a fair value of \$3.8 million as of December 31, 2012. See Note (7)(b) for additional information.

## (6) Investments

Investments on the Consolidated Balance Sheets as of March 31, 2013 and December 31, 2012 included available-for-sale and trading securities. At March 31, 2013 and December 31, 2012, Federated held investments totaling \$129.7 million and \$136.0 million, respectively, in fluctuating-value Federated-sponsored mutual funds that were classified as available-for-sale securities and were included in Investments—affiliates on the Consolidated Balance Sheets.

Available-for-sale securities were as follows:

| (in thousands)                       | March 31, 2013 |                  |          |                      | December 31, 2012 |                  |          |                      |
|--------------------------------------|----------------|------------------|----------|----------------------|-------------------|------------------|----------|----------------------|
|                                      | Cost           | Gross Unrealized |          | Estimated Fair Value | Cost              | Gross Unrealized |          | Estimated Fair Value |
|                                      |                | Gains            | (Losses) |                      |                   | Gains            | (Losses) |                      |
| Equity mutual funds                  | \$35,594       | \$7,432          | \$0      | \$43,026             | \$44,944          | \$4,814          | \$(5 )   | \$49,753             |
| Fixed-income mutual funds            | 85,602         | 1,201            | (127 )   | 86,676               | 84,855            | 1,436            | (21 )    | 86,270               |
| Total fluctuating-value mutual funds | \$121,196      | \$8,633          | \$(127 ) | \$129,702            | \$129,799         | \$6,250          | \$(26 )  | \$136,023            |

The decrease in available-for-sale securities at March 31, 2013 as compared to December 31, 2012, was primarily due to \$11.8 million in redemptions of equity mutual funds during the first three months of 2013 partially offset by purchases of \$0.9 million of fixed-income and equity mutual funds during the same period.

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Federated's trading securities totaled \$120.7 million and \$55.0 million at March 31, 2013 and December 31, 2012, respectively. Federated consolidates certain investment companies into its Consolidated Financial Statements as a result of Federated's controlling financial interest in the companies (see Note (5)). All investments held by these investment companies, which primarily represented Federated-sponsored investment companies, were included in Investments—consolidated investment companies on Federated's Consolidated Balance Sheets as of March 31, 2013 and December 31, 2012. Investments—other on the Consolidated Balance Sheets represented other trading investments held in separate accounts for which Federated is the beneficiary.

Federated's trading securities as of March 31, 2013 were primarily comprised of foreign and domestic debt securities totaling \$89.4 million (of which \$56.7 million represented high-quality short-term debt securities held by a consolidated, non-U.S. dollar, sponsored money market fund), stocks of large U.S. and international companies (\$14.6 million) and an offshore master fund invested in global project and trade finance transactions (\$8.7 million). Federated's trading securities as of December 31, 2012 were primarily comprised of domestic and foreign debt securities (\$28.4 million), stocks of large U.S. and international companies (\$13.9 million) held by various other consolidated investment companies and an offshore master fund invested in global project and trade finance transactions (\$12.1 million).

The following table presents gains and losses recognized in Gain on securities, net on the Consolidated Statements of Income in connection with investments and economic derivatives held by certain consolidated investment companies:

| (in thousands)                       | Three Months Ended |         |   |
|--------------------------------------|--------------------|---------|---|
|                                      | March 31,<br>2013  | 2012    |   |
| Unrealized (loss) gain               |                    |         |   |
| Trading securities                   | \$547              | \$1,259 |   |
| Derivatives <sup>1</sup>             | (587               | ) 75    |   |
| Realized gains <sup>2</sup>          |                    |         |   |
| Available-for-sale securities        | 2,322              | 503     |   |
| Trading securities                   | 349                | 354     |   |
| Derivatives <sup>1</sup>             | 384                | 226     |   |
| Realized losses <sup>2</sup>         |                    |         |   |
| Trading securities                   | (122               | ) (200  | ) |
| Derivatives <sup>1</sup>             | 0                  | (167    | ) |
| Gain on securities, net <sup>3</sup> | \$2,893            | \$2,050 |   |

<sup>1</sup> Amounts related to economic derivatives held by certain consolidated investment companies.

<sup>2</sup> Realized gains and losses are computed on a specific-identification basis.

<sup>3</sup> Amounts related to consolidated investment companies totaled \$0.4 million and \$1.4 million for the three months ended March 31, 2013 and 2012, respectively.

## (7) Fair Value Measurements

Fair value is the price that would be received to sell an asset or the price paid to transfer a liability as of the measurement date. A three-tier, fair-value reporting hierarchy exists for disclosure of fair value measurements based on the observability of the inputs to the valuation of financial assets and liabilities. The three levels are:

Level 1 – Quoted prices for identical instruments in active markets. Level 1 assets may include equity and debt securities that are traded in an active exchange market, including shares of mutual funds.

Level 2 – Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations in which all significant inputs and significant value drivers are observable in active markets. Level 2 assets and liabilities may include debt and equity securities, purchased loans and over-the-counter derivative contracts whose fair value is determined using a pricing model without significant unobservable market data inputs.

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Level 3 – Valuations derived from valuation techniques in which one or more significant inputs or significant value drivers are unobservable in active exchange markets.

## (a) Fair Value Measurements on a Recurring Basis

The following table presents fair value measurements for classes of Federated's financial assets and liabilities measured at fair value on a recurring basis:

| (in thousands)                                       | March 31, 2013                |                  |                 |                  | December 31, 2012             |                 |                 |                  |
|--|-------------------------------|------------------|-----------------|------------------|-------------------------------|-----------------|-----------------|------------------|
|  | Fair Value Measurements Using |                  |                 |                  | Fair Value Measurements Using |                 |                 |                  |
|  | Level 1                       | Level 2          | Level 3         | Total            | Level 1                       | Level 2         | Level 3         | Total            |
| <b>Financial Assets</b>                              |                               |                  |                 |                  |                               |                 |                 |                  |
| Cash and cash equivalents                            | \$56,427                      | \$0              | \$0             | \$56,427         | \$67,585                      | \$0             | \$0             | \$67,585         |
| Available-for-sale equity securities                 | 95,571                        | 34,131           | 0               | 129,702          | 102,493                       | 33,530          | 0               | 136,023          |
| Trading securities—equity                            | 17,188                        | 14,132           | 0               | 31,320           | 9,808                         | 16,776          | 0               | 26,584           |
| Trading securities—debt                              | 0                             | 89,408           | 0               | 89,408           | 0                             | 28,436          | 0               | 28,436           |
| Foreign currency forward contract                    | 0                             | 23               | 0               | 23               | 0                             | 158             | 0               | 158              |
| <b>Total financial assets</b>                        | <b>\$169,186</b>              | <b>\$137,694</b> | <b>\$0</b>      | <b>\$306,880</b> | <b>\$179,886</b>              | <b>\$78,900</b> | <b>\$0</b>      | <b>\$258,786</b> |
| <b>Financial Liabilities</b>                         |                               |                  |                 |                  |                               |                 |                 |                  |
| Interest rate swap                                   | \$0                           | \$9,520          | \$0             | \$9,520          | \$0                           | \$11,178        | \$0             | \$11,178         |
| Acquisition-related future consideration liabilities | 0                             | 0                | 11,711          | 11,711           | 0                             | 0               | 11,759          | 11,759           |
| Other <sup>1</sup>                                   | 976                           | 465              | 0               | 1,441            | 1,015                         | 0               | 0               | 1,015            |
| <b>Total financial liabilities</b>                   | <b>\$976</b>                  | <b>\$9,985</b>   | <b>\$11,711</b> | <b>\$22,672</b>  | <b>\$1,015</b>                | <b>\$11,178</b> | <b>\$11,759</b> | <b>\$23,952</b>  |

<sup>1</sup> Amounts include investments sold short within one of the consolidated investment companies and/or foreign currency forward contracts recorded within Other current liabilities on the Consolidated Balance Sheets.

The following is a description of the valuation methodologies used for financial assets and liabilities measured at fair value on a recurring basis. Federated did not hold any nonfinancial assets or liabilities measured at fair value on a recurring basis at March 31, 2013 or December 31, 2012.

**Cash and cash equivalents**

Cash and cash equivalents include investments in money market funds and deposits with banks. Cash and cash equivalents invested in Federated money market funds totaled \$41.9 million and \$60.2 million at March 31, 2013 and December 31, 2012, respectively. Cash investments in money market funds are valued under the market approach through the use of quoted market prices in an active market, which is the NAV of the underlying funds, and are classified within Level 1 of the valuation hierarchy.

**Available-for-sale equity securities**

Available-for-sale equity securities include investments in sponsored fluctuating-value mutual funds and are included in Investments—affiliates on the Consolidated Balance Sheets. For investments in mutual funds that are publicly available, the securities are valued under the market approach through the use of quoted market prices available in an active market, which is the NAV of the underlying funds, and are classified within Level 1 of the valuation hierarchy. For one investment in a mutual fund that is not publicly available but for which the NAV is calculated daily and for

which there are no redemption restrictions, the security is valued using NAV as a practical expedient and is classified as Level 2. There is no modeling or additional information needed to arrive at the fair values of any of these investments.

Trading securities—equity

These trading securities represented primarily the equity securities held by consolidated investment companies and included in Investments—consolidated investment companies as well as certain equity investments held in separate accounts for which Federated is the beneficiary and included in Investments—other on the Consolidated Balance Sheets. For the publicly traded equity securities available in an active market, whether domestic or foreign, the fair value of these securities is often classified as Level 1 and is based on unadjusted quoted market prices. From time to time, however, the fair value of certain equity

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securities traded principally in foreign markets may be determined by third-party pricing services when it has been determined that there has been a significant trend in the U.S. equity markets or in index futures trading. The determination to use the third-party pricing service versus the unadjusted quoted market price is the cause for transfers between Level 1 and Level 2 for these securities. For the period between December 31, 2012 and March 31, 2013, there were no investments transferred between Level 1 and Level 2. For the period between December 31, 2011 and March 31, 2012, \$2.7 million of investments transferred from Level 1 to Level 2 as a result of a determination by management at the end of the first quarter 2012 to use adjusted quoted market prices because there had been a significant trend to do so in the U.S. equity markets or in index futures trading after the foreign markets closed, as compared to, at the end 2011, using unadjusted quoted market prices to determine fair values of these equity securities. Transfers into and out of Levels 1 and 2 of the fair value hierarchy are reported at fair values as of the beginning of the period in which the transfers occur.

At March 31, 2013 and December 31, 2012, equity trading securities also included shares of certain non-publicly traded mutual funds that were valued using NAV as a practical expedient (Level 2). Most significantly, Federated held shares of an offshore master investment fund as a result of consolidating one of its feeder funds as of March 31, 2013 and December 31, 2012. The offshore master investment fund, which is not publicly available, makes investments in global project and trade finance transactions. The \$8.7 million and \$12.1 million fair value at March 31, 2013 and December 31, 2012, respectively, of the feeder fund's investment in the master fund was determined using the NAV of the master fund, as a practical expedient, and was classified as Level 2 in the valuation hierarchy at March 31, 2013 and December 31, 2012. At Federated's request, this investment is being redeemed primarily as portfolio investments mature. Federated expects that the investment will be fully redeemed in the latter half of 2013.

#### Trading securities—debt

At March 31, 2013, trading debt securities primarily represented high-quality short-term debt securities held by a consolidated, non-U.S. dollar, sponsored money market fund (\$56.7 million). The remaining trading debt securities held at March 31, 2013 and the balance at December 31, 2012 primarily represented U.S. and foreign bonds held by consolidated Federated-sponsored investment companies. The fair value of these securities may include observable market data such as valuations provided by independent pricing services after considering factors such as the yields or prices of investments of comparable quality, coupon, maturity, call rights and other potential prepayments, terms and type, reported transactions, indications as to values from dealers and general market conditions. The entire amount of these securities is included in Investments—consolidated investment companies or Investments—other on the Consolidated Balance Sheets.

#### Foreign currency forward contracts

The fair value of foreign currency forward contracts is primarily included in Receivables, net or Other current liabilities on the Consolidated Balance Sheets. These contracts represented contracts held by certain consolidated Federated-sponsored investment companies as part of their investment strategy. Pricing is determined by interpolating a value by utilizing the spot foreign exchange rate and forward points (based on the spot rate and currency interest rate differentials), which are all inputs that are observable in active markets (Level 2).

#### Interest rate swap

The fair value of Federated's interest rate swap (the Swap) at March 31, 2013 is included in Other current liabilities (\$6.0 million) and Other long-term liabilities (\$3.5 million) on the Consolidated Balance Sheets. Pricing is determined based on a third-party, model-derived valuation in which all significant inputs are observable in active markets including the Eurodollar future rate and yields for three- and thirty-year Treasury securities. See Note (8) for more information regarding the Swap.

#### Acquisition-related future consideration liabilities

From time to time, pursuant to purchase and sale agreements entered into in connection with certain business combinations, Federated may be required to make future consideration payments if certain contingencies are met. See Note (12)(a) for additional information regarding the nature and timing of these payments. In connection with these arrangements entered into after January 1, 2009, Federated records a liability representing the estimated fair value of future consideration payments as of the acquisition date. The liability is subsequently remeasured at fair value on a recurring basis with changes in fair value recorded in earnings. As of March 31, 2013, acquisition-related future consideration liabilities were recorded in Other current liabilities (\$4.3 million) and Other long-term liabilities (\$7.4 million) on the Consolidated Balance Sheets. Management estimated the fair value of future consideration payments based primarily upon expected future cash flows using an income approach valuation methodology with unobservable data inputs (Level 3). As of March 31, 2013, significant inputs involving unobservable market data included (1) an estimated rate of change for underlying AUM ranging from (15)% - 28% per year (weighted average of 4%); (2) an estimate ranging from 0.01% - 0.02% per year of the impact of fee waivers to maintain positive or zero net yields on the contractually-derived net revenue per managed asset assumptions (weighted average of

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0.02%); and (3) an estimated discount rate ranging from 15% - 18% based on the current estimated market rate of return (weighted average of 16%). Assuming no other changes in model inputs, the fair value of the future consideration liability will increase, resulting in additional Intangible asset related expense in the period of change if: (1) the underlying AUM grow at a rate that is greater than the assumed rate, (2) the actual impact of fee waivers to maintain positive or zero net yields on the net revenue is less than the assumed amount or (3) the discount rate decreases. Conversely, the fair value of the future consideration liability will decrease if the inverse occurs for any of these inputs, assuming no other changes.

The following table presents a reconciliation of the beginning and ending fair value measurements of Federated's liability for future consideration payments related to these acquisitions for each period presented:

| (in thousands)                     | Three Months Ended<br>March 31, |          |
|------------------------------------|---------------------------------|----------|
|                                    | 2013                            | 2012     |
| Beginning balance                  | \$11,759                        | \$13,404 |
| Changes in fair value <sup>1</sup> | (48 )                           | (1,000 ) |
| Ending balance                     | \$11,711                        | \$12,404 |

For the quarter ended March 31, 2013, the amount was primarily included as Other expense on the Consolidated Statements of Income and primarily represented a foreign currency loss. For the quarter ended March 31, 2012, the amount was primarily included as a decrease to Intangible asset related expense on the Consolidated Statements of Income.

#### Investments sold short

The fair value of investments sold short within a consolidated investment company is included in Other current liabilities on the Consolidated Balance Sheets. The investments primarily relate to domestic equity securities that are available in an active exchange market. The fair value of these investments is classified as Level 1 and is based on unadjusted quoted market prices.

#### (b) Fair Value Measurements on a Nonrecurring Basis

Federated holds a 12% non-voting, noncontrolling interest in a privately-held investment management firm that is registered as an investment adviser and a commodity trading adviser. This investment is accounted for using the equity-method of accounting. The excess carrying value of Federated's equity-method investment as compared to its proportionate share of the investee's underlying net assets reflects goodwill. During 2012, due to declines in the investee's AUM, their performance relative to indices and the uncertainty regarding each in the future, Federated evaluated the carrying value of its investment for other-than-temporary impairment under the equity-method of accounting. Management estimated the fair value of its investment at December 31, 2012 and determined that it was other-than-temporarily impaired. Accordingly, Federated recorded a \$3.0 million impairment charge in Nonoperating Income (Expenses) – Other, net to write down the equity-method investment to a fair value of \$3.8 million as of December 31, 2012. The estimate of fair value was based primarily upon the present value of expected future cash flows using an income approach valuation methodology with unobservable data inputs (Level 3). Significant unobservable model inputs included: (1) projected AUM across product lines with a 10-year compounded annual growth rate of 15% and a terminal growth rate of 3%; and (2) a 17% discount rate based upon the current estimated market rate of return. No new indicators of impairment existed as of March 31, 2013. Given uncertainties regarding the success of future sales efforts and possible prolonged periods of over/underperformance compared to indices and the significance of these factors to AUM, management cannot be certain of the outcome of future cash flow analyses for this investment with a remaining carrying value and maximum exposure to loss of \$3.8 million at March 31, 2013.

(c) Fair Value Measurements of Other Financial Instruments

The fair value of Federated's debt is estimated by management based upon expected future cash flows utilizing a discounted cash flow methodology under the income approach. The fair value of the liability is estimated using observable market data (Level 2) in estimating inputs including the discount rate. Based on this fair value estimate, the carrying value of debt appearing on the Consolidated Balance Sheets approximates fair value.

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## (8) Debt and Interest Rate Swap

Debt consisted of the following:

| (dollars in thousands) | Weighted-Average Interest<br>Rate <sup>1</sup> | March 31, 2013 | December 31, 2012 |
|------------------------|--|----------------|-------------------|
| Term Loan              | 3.646%   | \$ 308,125     | \$ 318,750        |
| Less: Short-term debt  |  | 42,500         | 42,500            |
| Long-term debt         |  | \$ 265,625     | \$ 276,250        |

<sup>1</sup> See additional information below regarding the interest rate fixed at 3.646% in connection with the Swap.

In 2011, Federated entered into an Amended and Restated Credit Agreement with a syndicate of banks that included a \$382.5 million term loan (Term Loan) and \$200 million revolving credit facility (collectively, Credit Agreement). The Credit Agreement expires on June 10, 2016. The Term Loan, a variable-rate note, requires principal payments of \$10.6 million per quarter for the first three years and \$28.3 million per quarter for the fourth and fifth years and a final payment of \$28.3 million due upon its expiration. Certain subsidiaries entered into an Amended and Restated Continuing Agreement of Guaranty and Suretyship whereby these subsidiaries guarantee payment of all obligations incurred through the Credit Agreement.

The borrowings under the Term Loan bear interest at a spread over the London Interbank Offering Rate (LIBOR). Federated is a party to an interest rate swap (the Swap) with PNC Bank, National Association and certain other banks to hedge its interest rate risk on the Term Loan. Under the Swap, which expires on April 1, 2015, Federated receives payments based on LIBOR plus a spread and makes payments based on an annual fixed rate of 3.646%. The Swap requires monthly cash settlements of interest paid or received. The differential between the interest paid or interest received from the monthly settlements is recorded as adjustments to Debt expense on the Consolidated Statements of Income. The Swap is accounted for as a cash flow hedge and has been determined to be highly effective. Federated evaluates effectiveness using the long-haul method. Changes in the fair value of the Swap will likely be offset by an equal and opposite change in the fair value of the hedged item, therefore very little, if any, net impact on reported earnings is expected. The fair value of the Swap agreement at March 31, 2013 was a liability of \$9.5 million which was recorded in Other current liabilities (\$6.0 million) and Other long-term liabilities (\$3.5 million) on the Consolidated Balance Sheets. The entire amount of this loss in fair value was recorded in Accumulated other comprehensive loss, net of tax on the Consolidated Balance Sheets at March 31, 2013. During the next twelve months management expects to charge \$6.0 million of this loss to Debt expense on the Consolidated Statements of Income as a component of Federated's fixed interest rate of 3.646%. This amount could differ from amounts actually recognized due to changes in interest rates subsequent to March 31, 2013 and will not affect the amount of interest expense recognized in total on the Term Loan for any period presented. During the three-month periods ended March 31, 2013 and 2012, \$1.7 million and \$1.9 million, respectively, were charged to Debt expense on the Consolidated Statements of Income as a component of Federated's fixed interest rate associated with the Swap.

As of March 31, 2013, the entire \$200 million revolving credit facility was available for borrowings.

The Credit Agreement includes representations, warranties and other covenants, including an interest coverage ratio covenant and a leverage ratio covenant. Federated was in compliance with all covenants at and during the three months ended March 31, 2013. The Credit Agreement and the Swap also have certain stated events of default and cross default provisions which would permit the lenders/counterparties to accelerate the repayment of the debt or to terminate the Swap if not cured within the applicable grace periods. The events of default generally include breaches of contract, failure to make required loan payments, insolvency, cessation of business, deterioration in credit rating to below investment grade, notice of lien or assessment and other proceedings, whether voluntary or involuntary, that would require the repayment of amounts borrowed.

## (9) Share-Based Compensation Plans

(a) Restricted Stock

During the first three months of 2013, Federated awarded 474,050 shares of restricted Federated Class B common stock, all of which was awarded in connection with a bonus program in which certain key employees received a portion of their bonus in the form of restricted stock under Federated's Stock Incentive Plan. This restricted stock, which was granted on the bonus payment date and issued out of treasury, will generally vest over a three-year period.

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Federated awarded 1,015,273 shares of restricted Federated Class B common stock under its Stock Incentive Plan during 2012. Of this amount, 480,773 shares of restricted Federated Class B common stock were awarded in connection with the aforementioned bonus program. The remaining shares were awarded to certain key employees and generally vest over a ten-year period.

## (b) Stock Options

During the quarter ended March 31, 2013 and year ended December 31, 2012, there were no stock options issued or exercised.

## (10) Equity

During 2008, the board of directors authorized a share repurchase program that allows Federated to buy back as many as 5 million shares of Class B common stock. The program has no stated expiration date and no other programs existed as of March 31, 2013. The program authorizes executive management to determine the timing and the amount of shares for each purchase. The repurchased stock is held in treasury for employee share-based compensation plans, potential acquisitions and other corporate activities. During the first three months of 2013, Federated repurchased 0.1 million shares of common stock for \$2.7 million, nearly all of which were repurchased in the open market. The remaining shares were repurchased in connection with employee separations and are not counted against the board-approved share repurchase program. At March 31, 2013, approximately 1.7 million shares remained available to be purchased under the current buyback program.

## (11) Earnings Per Share Attributable to Federated Investors, Inc. Shareholders

The following table sets forth the computation of basic and diluted earnings per share for amounts attributable to Federated Investors, Inc. using the two-class method:

| (in thousands, except per share data)   | Three Months Ended |          |
|---|--------------------|----------|
|   | March 31,<br>2013  | 2012     |
| Numerator – Basic and Diluted   |                    |          |
| Net income attributable to Federated Investors, Inc.  | \$42,994           | \$42,325 |
| Less: Total income available to participating unvested restricted shareholders <sup>1</sup> | (1,657             | ) (1,540 |
| Total net income attributable to Federated Common Stock <sup>2</sup>                        | \$41,337           | \$40,785 |
| Denominator   |                    |          |
| Basic and Diluted weighted-average common shares outstanding                                | 100,518            | 100,112  |
| Earnings per Share  |                    |          |
| Net income attributable to Federated Common Stock – Basic and Diluted                       | \$0.41             | \$0.41   |

<sup>1</sup> Income available to participating restricted shareholders includes dividends paid on unvested restricted shares and their proportionate share of undistributed earnings.

<sup>2</sup> Federated Common Stock excludes unvested restricted stock which are deemed participating securities in accordance with the two-class method of computing earnings per share.

For the three-month periods ended March 31, 2013 and 2012, 0.1 million and 0.3 million stock option awards, respectively, were not included in the computation of diluted earnings per share for each period because the exercise price was greater than the average market price of Federated Class B common stock for each respective period. In the event the awards become in-the-money, these shares would be included in the calculation of diluted earnings per share and would result in dilution.

(12) Commitments and Contingencies

(a) Contractual

In 2010, Federated acquired the money market management business of SunTrust Banks, Inc. (SunTrust Acquisition). As part of the SunTrust Acquisition, Federated is required to make annual contingent purchase price payments in the fourth quarters of each of the five years following the acquisition date. The contingent purchase price payments are calculated as a percentage of revenue less distribution expenses directly attributed to certain eligible assets. The first two contingent purchase price payments of \$5.0 million and \$4.2 million were paid in the fourth quarters of 2011 and 2012, respectively. At March 31, 2013,

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Notes to the Consolidated Financial Statements (continued)  
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management estimated remaining contingent payments could total \$11 million over the three years that remain; however, the actual amount of the contingent payments will vary based on asset levels and related net revenues and is not limited by any maximum amount. A wide range of outcomes for actual payments is possible due to the extent of reasonably possible flow-rate volatility for the respective AUM. As of March 31, 2013, a liability of \$8.2 million representing the estimated fair value of future consideration payments was recorded in Other current liabilities (\$3.5 million) and Other long-term liabilities (\$4.7 million) (see Note (7)(a) for a discussion regarding the valuation methodology). This liability is remeasured at each reporting date with changes in the fair value recognized in Intangible asset related expense on the Consolidated Statements of Income.

In 2008, Federated completed the acquisition of certain assets of Clover Capital Management, Inc., a Rochester, New York-based investment manager that specializes in value investing (Clover Capital Acquisition). As part of the Clover Capital Acquisition, Federated is required to make contingent purchase price payments based upon growth in revenues over the five-year period following the acquisition date. The contingent purchase price payments, which could total as much as \$56 million, will be recorded as additional goodwill at the time the contingency is resolved. The applicable growth targets were not met for the first two anniversary years and as such, no related payments were made. In the first quarter 2012 and 2013, \$5.9 million and \$3.4 million were paid with regard to the third and fourth anniversary years, respectively. As of March 31, 2013, no amounts were accrued for the fifth anniversary year ending in December 2013.

Pursuant to other acquisition agreements, Federated may be required to make additional purchase price payments based on a percentage of revenue less certain direct expenses attributable to eligible AUM. The payments could occur annually through 2017. As of March 31, 2013, liabilities totaling \$3.5 million and representing the estimated fair value of future consideration payments were recorded in Other current liabilities (\$0.8 million) and Other long-term liabilities (\$2.7 million) (see Note (7)(a) for a discussion regarding the valuation methodology). The liabilities are remeasured at each reporting date with changes in the fair value recognized in Intangible asset related expense and/or Other expense on the Consolidated Statements of Income.

Pursuant to various significant employment arrangements, Federated may be required to make certain incentive compensation-related payments. The employment contracts expire on various dates through the year 2014 with payments possible through 2018. As of March 31, 2013, the maximum bonus payable over the remaining terms of the contracts approximates \$43 million, none of which would be payable in the remainder of 2013. In addition, certain employees have incentive compensation opportunities related to the Federated Kaufmann Large Cap Fund (the Fund Bonus). Assuming asset levels and other variable inputs at March 31, 2013 remain constant throughout the year, the Fund Bonus payment in 2014 may approximate \$1 million. Management is unable to reasonably estimate a range of possible bonus payments for the Fund Bonus for subsequent years due to the wide range of possible growth-rate scenarios.

(b) Guarantees and Indemnifications

On an intercompany basis, various wholly owned subsidiaries of Federated guarantee certain financial obligations of Federated Investors, Inc., and Federated Investors, Inc. guarantees certain financial and performance-related obligations of various wholly owned subsidiaries. In addition, in the normal course of business, Federated has entered into contracts that provide a variety of indemnifications. Typically, obligations to indemnify third parties arise in the context of contracts entered into by Federated, under which Federated agrees to hold the other party harmless against losses arising out of the contract, provided the other party's actions are not deemed to have breached an agreed upon standard of care. In each of these circumstances, payment by Federated is contingent on the other party making a claim for indemnity, subject to Federated's right to challenge the other party's claim. Further, Federated's obligations

under these agreements may be limited in terms of time and/or amount. It is not possible to predict the maximum potential amount of future payments under these or similar agreements due to the conditional nature of Federated's obligations and the unique facts and circumstances involved in each particular agreement. Management believes that if Federated were to incur a loss in any of these matters, such loss should not have a material effect on its business, financial position or results of operations.

(c) Other Legal Proceedings

Federated has claims asserted and threatened against it in the ordinary course of business. As of March 31, 2013, Federated does not believe that a material loss related to these claims is reasonably possible.

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## (13) Accumulated Other Comprehensive Loss attributable to Federated Shareholders

The components of Accumulated other comprehensive loss, net of tax attributable to Federated shareholders are as follows:

| (in thousands)   | Unrealized Loss<br>on Interest<br>Rate Swap <sup>1</sup> | Unrealized Gain<br>on Securities<br>Available for Sale <sup>2</sup> | Unrealized<br>Loss on<br>Foreign<br>Currency<br>Hedge | Foreign<br>Currency<br>Translation<br>Gain<br>(Loss) | Total      |
|--|--|---|---|--|------------|
| Balance at December 31, 2011                                       | \$ (9,634 )  | \$ 325  | \$368   | \$329  | \$(8,612 ) |
| Other comprehensive income (loss) before reclassifications and tax | (1,180 )   | 7,389   | (2,367 )  | 2,595  | 6,437      |
| Tax impact   | 400  | (3,091 )  | 697   | (908 )   | (2,902 )   |
| Reclassification adjustments, before tax                           | 1,883  | (503 )  | 0   | 0  | 1,380      |
| Tax impact   | (659 )   | 176   | 0   | 0  | (483 )     |
| Net current-period other comprehensive income (loss)               | 444  | 3,971   | (1,670 )  | 1,687  | 4,432      |
| Balance at March 31, 2012  | \$ (9,190 )  | \$ 4,296  | \$(1,302 )  | \$2,016  | \$(4,180 ) |
| Balance at December 31, 2012                                       | \$ (7,071 )  | \$ 3,644  | \$0   | \$490  | \$(2,937 ) |
| Other comprehensive income (loss) before reclassifications and tax | (26 )  | 4,604   | 0   | (48 )  | 4,530      |
| Tax impact   | 9  | (1,611 )  | 0   | 17   | (1,585 )   |
| Reclassification adjustments, before tax                           | 1,684  | (2,322 )  | 0   | 0  | (638 )     |
| Tax impact   | (618 )   | 812   | 0   | 0  | 194        |
| Net current-period other comprehensive income (loss)               | 1,049  | 1,483   | 0   | (31 )  | 2,501      |
| Balance at March 31, 2013  | \$ (6,022 )  | \$ 5,127  | \$0   | \$459  | \$(436 )   |

<sup>1</sup> Amounts reclassified from Accumulated other comprehensive loss, net of tax were recorded in Debt expense on the Consolidated Statements of Income.

<sup>2</sup> Amounts reclassified from Accumulated other comprehensive loss, net of tax were recorded in Gain on securities, net on the Consolidated Statements of Income.

## (14) Subsequent Events

On April 25, 2013, the board of directors declared a \$0.24 per share dividend to shareholders of record as of May 8, 2013 to be paid on May 15, 2013.

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Part I, Item 2. Management's Discussion and Analysis  
of Financial Condition and Results of Operations (unaudited)

The discussion and analysis below should be read in conjunction with the consolidated financial statements appearing elsewhere in this report. Management has presumed that the readers of this interim financial information have read or have access to Management's Discussion and Analysis of Financial Condition and Results of Operations appearing in Federated's Annual Report on Form 10-K for the year ended December 31, 2012.

General

Federated Investors, Inc. (together with its subsidiaries, Federated) is one of the largest investment managers in the United States with \$377.3 billion in managed assets as of March 31, 2013. The majority of Federated's revenue is derived from advising Federated-sponsored mutual funds and Separate Accounts (which include separately managed accounts, institutional accounts, sub-advised funds and other managed products) in both domestic and international markets. Federated also derives revenue from providing administrative and other mutual fund-related services, including distribution, shareholder servicing and retirement plan recordkeeping services.

Federated's investment products are primarily distributed in four markets. These markets and the relative percentage of managed assets at March 31, 2013 attributable to such markets are as follows: wealth management and trust (46%), broker/dealer (31%), institutional (14%) and international (6%).

Investment advisory fees, administrative service fees and certain fees for other services, such as distribution and shareholder service fees, are contract-based fees that are generally calculated as a percentage of the net assets of the investment portfolios that are managed by Federated. Federated's revenue is primarily dependent upon factors that affect the value of managed assets including market conditions and the ability to attract and retain assets. Nearly all assets under management (AUM or managed assets) in Federated's investment products can be redeemed at any time with no advance notice requirement. Fee rates for Federated's services generally vary by asset and service type and may vary based on changes in asset levels. Generally, management-fee rates charged for advisory services provided to equity products are higher than management-fee rates charged on money market and fixed-income products. Likewise, mutual funds typically have a higher management-fee rate than Separate Accounts. Similarly, traditional separate accounts typically have a higher management-fee rate than liquidation portfolios. Accordingly, revenue is also dependent upon the relative composition of average AUM across both asset and product types. Federated may waive certain fees for competitive reasons such as to maintain positive or zero net yields, to meet regulatory requirements or to meet contractual requirements. Since Federated's products are largely distributed and serviced through financial intermediaries, Federated pays a portion of fees earned from sponsored products to the financial intermediaries that sell these products. These payments are generally calculated as a percentage of net assets attributable to the financial intermediary selling the product and comprise the vast majority of Distribution expense on the Consolidated Statements of Income. Certain components of distribution expense can vary depending upon the asset type, distribution channel and/or the size of the customer relationship. Federated generally pays out a larger portion of revenue earned from managed assets in money market funds than revenue earned from managed assets in equity or fixed-income funds.

Federated's most significant operating expenses are compensation and related expense and Distribution expense as described above. Compensation and related expense includes base salary and wages, incentive compensation and other employee expenses including payroll taxes and benefits. Incentive compensation, which includes stock-based compensation, can vary dependent on various factors including, but not limited to, overall results of operations for Federated, investment management performance and sales performance.

The discussion and analysis of Federated's financial condition and results of operations are based on Federated's Consolidated Financial Statements. Federated operates in a single operating segment, the investment management business. Management evaluates Federated's performance at the consolidated level. Management analyzes all expected revenue and expenses and considers market demands in determining an overall fee structure for services provided and in evaluating the addition of new business. Federated's growth and profitability are dependent upon its ability to attract and retain AUM and upon the profitability of those assets, which is impacted, in part, by management's decisions regarding fee waivers in order for certain money market funds to maintain positive or zero net yields. Fees for fund-related services are ultimately subject to the approval of the independent directors or trustees of the mutual funds. Management believes the most meaningful indicators of Federated's performance are AUM, total revenue and net income, both in total and per diluted share.

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Management's Discussion and Analysis (continued)  
of Financial Condition and Results of Operations (unaudited)

Business Developments

Money Market Fund Matters

For the three-month period ended March 31, 2013, approximately 43% of Federated's total revenue was attributable to money market assets as compared to 46% for the same period in 2012. A significant change in Federated's money market business or a significant reduction in money market assets due to regulatory changes, changes in the financial markets including significant and rapid increases in interest rates over a short period of time causing certain investors to prefer direct investments in interest-bearing securities, significant deterioration in investor confidence, further persistent declines in or additional prolonged periods of historically low short-term interest rates and resulting fee waivers or other circumstances, could have a material adverse effect on Federated's results of operations.

(a) Current Regulatory Environment

Domestic

In January 2010, the Securities and Exchange Commission (SEC) adopted extensive amendments to Rule 2a-7 of the Investment Company Act of 1940 (Rule 2a-7) aimed at enhancing the resiliency of money market funds. These amendments included a series of enhancements including rules that require all money market funds to meet specific portfolio liquidity standards and rules that significantly enhance the public disclosure and regulatory reporting obligations of these funds. In 2010 and 2011, Federated dedicated internal resources to comply with these amendments including efforts to enhance its information systems and improve related reporting capabilities. These efforts were internally sourced and not material to Federated's financial position, results of operations or cash flows for those years. In Federated's view, the amendments of 2010 meaningfully and sufficiently strengthen money market funds. Recent experience demonstrated that the amendments of 2010 were effective in meeting heightened requests for redemptions occurring in connection with the U.S. credit rating downgrade in 2011 and the ongoing European debt crisis.

More recently, the SEC undertook a project to develop a proposal for additional reforms related to money market funds. In August 2012, then SEC Chairman Mary Schapiro issued a public statement announcing that she did not have sufficient votes from the other SEC commissioners to pursue certain proposed reforms relating to money market funds. In her statement, Ms. Schapiro stated that the SEC had been considering two alternative reform proposals, one which would have required a floating net asset value (NAV) and the other which would have imposed capital requirements coupled with some form of redemption restriction. In her statement, she invited other policymakers to take up the issue of reform. On September 27, 2012, then Treasury Secretary Timothy Geithner sent a letter to the members of the Financial Stability Oversight Council (FSOC) announcing his intent to pursue money market fund reform. His letter urged FSOC to use its authority under Section 120 of the Dodd-Frank Act to recommend that the SEC proceed with money market reform. Mr. Geithner outlined three potential options for reform in his letter and stated that he had asked his staff to begin drafting a formal recommendation for FSOC to consider at its November 2012 meeting.

In November 2012, FSOC issued Proposed Recommendations Regarding Mutual Fund Reform citing its authority under Section 120 of the Dodd-Frank Act (Proposed Recommendations). The Proposed Recommendations are in draft form and were subject to a public comment period which ended on February 15, 2013. The Proposed Recommendations include three main alternatives: a floating NAV for money market funds; an NAV capital buffer and minimum balance at risk (or 30-day hold back of up to 3% on certain redemptions); and an NAV capital buffer combined with other measures. In response to the Proposed Recommendations, Federated has filed multiple comment letters on the Proposed Recommendations pointing out, among other things, that: (1) FSOC exceeded its authority in how it used the Section 120 process; (2) FSOC has not provided justification for further reform efforts; (3) a floating NAV would not prevent "runs" on money market funds; (4) an NAV capital buffer of the kind proposed is impractical and not economically attainable in the current interest rate environment; and (5) the minimum-balance-at-risk concept would impair the utility of money market funds to investors and would be prohibitively costly for both fund groups

and intermediaries to implement.

On November 30, 2012, the SEC Staff issued a study entitled Response to Questions Posed by Commissioners Aguilar, Parades and Gallagher. This study responded to questions posed by the Commissioners in response to potential reform measures being advanced by then SEC Chairman Mary Shapiro. The study addressed certain misconceptions about the role of money market funds in the financial crisis of 2008 and confirmed the effectiveness of the 2010 amendments to Rule 2a-7. Federated also filed a comment letter on the study commending the SEC Staff for its work while raising questions on some aspects of the study and recommending further analysis.

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Management's Discussion and Analysis (continued)  
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It has been reported that the SEC Staff is working on its own rule proposal and that proposal could include a floating NAV for certain money market funds, in particular prime funds. It could also include a floating NAV proposal for all money market funds as well as other reform measures. In April 2013, Commissioner Daniel Gallagher stated that the SEC Staff is actively working on the proposal and that he expects the SEC to issue the proposal in the "near term." Federated believes the potential changes summarized above, if enacted, would significantly reduce the utility and attractiveness of money market funds for investors who, in Federated's view, value money market funds in their current form as an efficient and effective cash management investment product offering daily liquidity at par. If ultimately enacted, some or all of these changes would be detrimental to Federated's money market fund business and could materially and adversely affect Federated's operations. The very proposal of such amendments could have an adverse impact on Federated's money market fund business and operations and could also negatively impact the short-term credit markets.

Management is carefully monitoring developments in this area and plans to actively participate both individually and with industry groups in the public comment process that would accompany any rule change proposal. Federated is unable to assess the degree of any potential impact such additional reforms may have on its business and operations until such proposals are issued. Even when issued, the final version of any rule amendment could vary significantly from the form in which it is proposed.

International

The European Union (EU) recently agreed to allow certain of its members to move forward in drafting a proposal that would establish a financial transactions tax (FTT) in those countries. Preliminary details of the FTT include a 0.1 percent tax on trades in certain financial instruments, and a 0.01 percent tax on the notional value of derivatives trades, subject to certain limited exemptions. The imposition of the FTT and the potential breadth of its application could adversely impact the operations of a wide array of Federated products, including Federated's Irish- and U.K.-domiciled Undertakings for Collective Investment in Transferable Securities products, as well as Federated's domestic money market and fixed-income funds. Final terms of the proposed FTT will be subject to additional government approval prior to enactment.

In addition, European-based money market funds face regulatory reform pressure in Europe similar to that faced in the U.S. The European Commission has reportedly prepared a draft reform proposal which could include a floating NAV for money market funds and/or capital requirements.

Federated is unable to assess the degree of any potential impact such proposals may have on its business and operations until such proposals are issued. Even when issued, the final version of any rule amendment could vary significantly from the form in which it is proposed.

(b) Historically Low Short-Term Interest Rates

For several years, the Federal Reserve has kept the near-zero federal funds rate unchanged and short-term interest rates continued at all-time low levels. In certain money market funds, the gross yield earned by the fund is not sufficient to cover all of the fund's operating expenses due to these historically low short-term interest rates. Since the fourth quarter 2008, Federated has voluntarily waived fees in order for certain money market funds to maintain positive or zero net yields. These fee waivers have been partially offset by related reductions in distribution expense and net income attributable to noncontrolling interests as a result of Federated's mutual understanding and agreement with third-party intermediaries to share the impact of the waivers.

These voluntary fee waivers are calculated as a percent of AUM in certain money market funds and thus will vary dependent upon the asset levels in such funds. In addition, the level of waivers are dependent on several other factors including, but not limited to, available yields on instruments held by the money market funds, changes in expenses of the money market funds and changes in the mix of money market assets. In any given period, a combination of these factors drives the amount of fee waivers necessary in order for certain funds to maintain positive or zero net yields. As

an isolated variable, an increase in yields on instruments held by the money market funds will cause the pre-tax impact of fee waivers to decrease. Conversely, as an isolated variable, an increase in expenses of the money market fund would cause the pre-tax impact of fee waivers to increase.

With regard to asset mix, changes in the relative amount of money market fund assets in prime and government money market funds as well as the distribution among certain share classes that vary in pricing structure will impact the level of fee waivers. Generally, prime money market funds waive less than government money market funds as a result of higher gross yields on the underlying investments. As such, as an isolated variable, an increase in the relative proportion of average managed assets

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invested in prime money market funds as compared to total average money market fund assets should typically result in lower waivers to maintain positive or zero net yields. Conversely, the opposite would also be true.

The impact of such fee waivers on various components of Federated's Consolidated Statements of Income was as follows for the periods presented:

| (in millions)                              | Three Months Ended |                      |                       |                  |                   |
|--|--------------------|----------------------|-----------------------|------------------|-------------------|
|  | March 31,<br>2013  | December 31,<br>2012 | September 30,<br>2012 | June 30,<br>2012 | March 31,<br>2012 |
| Investment advisory fees                   | \$ (54.9 )         | \$ (40.0 )           | \$ (41.2 )            | \$ (43.0 )       | \$ (52.9 )        |
| Other service fees                         | (32.4 )            | (30.7 )              | (28.3 )               | (27.3 )          | (27.5 )           |
| Total Revenue                              | (87.3 )            | (70.7 )              | (69.5 )               | (70.3 )          | (80.4 )           |
| Less: Reduction in Distribution expense    | 64.8               | 54.9                 | 52.9                  | 53.1             | 57.5              |
| Operating income                           | (22.5 )            | (15.8 )              | (16.6 )               | (17.2 )          | (22.9 )           |
| Less: Reduction in Noncontrolling interest | 0.8                | 0.3                  | 0.3                   | 0.0              | 0.6               |
| Pre-tax impact                             | \$ (21.7 )         | \$ (15.5 )           | \$ (16.3 )            | \$ (17.2 )       | \$ (22.3 )        |

The negative pre-tax impact of fee waivers to maintain positive or zero net yields on certain money market funds decreased for the first quarter 2013 as compared to the same quarter of 2012 primarily as a result of a change in the mix of average money market assets in addition to the impact of the leap year in 2012 compared to 2013.

Based on recent commentary from the Federal Reserve Bank in its March 20, 2013 press release, "the current highly accommodative stance of monetary policy will remain appropriate for a considerable time..." Federated is unable to predict when the Federal Reserve will increase its target for the federal funds rate. As such, fee waivers to maintain positive or zero net yields on certain money market funds and the related reduction in distribution expense and net income attributable to noncontrolling interests could continue for the foreseeable future. Assuming asset levels and mix remain constant and based on recent market conditions, fee waivers for the second quarter 2013 may result in a negative pre-tax impact on income of a similar amount as the first quarter 2013. While the level of fee waivers are impacted by various factors, increases in short-term interest rates that result in higher yields on securities purchased in money market fund portfolios would reduce the negative pre-tax impact of these waivers. Management estimates that an increase of 10 basis points in gross yields on securities purchased in money market fund portfolios will likely reduce the negative pre-tax impact of these waivers by approximately forty percent from the current levels and an increase of 25 basis points would reduce the impact by approximately seventy percent from the current levels. The actual amount of future fee waivers could vary significantly from management's estimates as they are contingent on a number of variables including, but not limited to, changes in assets within the money market funds, available yields on instruments held by the money market funds, actions by the Federal Reserve, the U.S. Department of the Treasury, the SEC, FSOC and other governmental entities, changes in expenses of the money market funds, changes in the mix of money market customer assets, Federated's willingness to continue the fee waivers and changes in the extent to which the impact of the waivers is shared by third parties.

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## Asset Highlights

## Managed Assets at Period End

| (in millions)                      | March 31,<br>2013 | 2012      | Percent Change |    |
|------------------------------------|-------------------|-----------|----------------|----|
| By Asset Class                     |                   |           |                |    |
| Money market                       | \$279,668         | \$274,704 | 2              | %  |
| Fixed-income                       | 52,770            | 46,221    | 14             | %  |
| Equity                             | 37,852            | 34,117    | 11             | %  |
| Liquidation portfolio <sup>1</sup> | 7,019             | 8,583     | (18)           | )% |
| Total managed assets               | \$377,309         | \$363,625 | 4              | %  |
| By Product Type                    |                   |           |                |    |
| Mutual Funds:                      |                   |           |                |    |
| Money market                       | \$242,734         | \$245,232 | (1)            | )% |
| Fixed-income                       | 42,612            | 38,526    | 11             | %  |
| Equity                             | 24,491            | 23,612    | 4              | %  |
| Total mutual fund assets           | \$309,837         | \$307,370 | 1              | %  |
| Separate Accounts:                 |                   |           |                |    |
| Money market                       | \$36,934          | \$29,472  | 25             | %  |
| Fixed-income                       | 10,158            | 7,695     | 32             | %  |
| Equity                             | 13,361            | 10,505    | 27             | %  |
| Total separate account assets      | \$60,453          | \$47,672  | 27             | %  |
| Liquidation Portfolio <sup>1</sup> | \$7,019           | \$8,583   | (18)           | )% |
| Total managed assets               | \$377,309         | \$363,625 | 4              | %  |

## Average Managed Assets

| (in millions)                         | Three Months Ended<br>March 31,<br>2013 | 2012      | Percent Change |    |
|---------------------------------------|---|-----------|----------------|----|
| By Asset Class                        |   |           |                |    |
| Money market                          | \$284,588                               | \$282,801 | 1              | %  |
| Fixed-income                          | 52,732                                  | 45,792    | 15             | %  |
| Equity                                | 36,685                                  | 32,827    | 12             | %  |
| Liquidation portfolio <sup>1</sup>    | 7,215                                   | 8,703     | (17)           | )% |
| Total average managed assets          | \$381,220                               | \$370,123 | 3              | %  |
| By Product Type                       |   |           |                |    |
| Mutual Funds:                         |   |           |                |    |
| Money market                          | \$250,652                               | \$251,825 | 0              | %  |
| Fixed-income                          | 42,581                                  | 38,128    | 12             | %  |
| Equity                                | 24,037                                  | 23,075    | 4              | %  |
| Total average mutual fund assets      | \$317,270                               | \$313,028 | 1              | %  |
| Separate Accounts:                    |   |           |                |    |
| Money market                          | \$33,936                                | \$30,976  | 10             | %  |
| Fixed-income                          | 10,151                                  | 7,664     | 32             | %  |
| Equity                                | 12,648                                  | 9,752     | 30             | %  |
| Total average separate account assets | \$56,735                                | \$48,392  | 17             | %  |

|                                    |           |           |     |    |
|------------------------------------|-----------|-----------|-----|----|
| Liquidation Portfolio <sup>1</sup> | \$7,215   | \$8,703   | (17 | )% |
| Total average managed assets       | \$381,220 | \$370,123 | 3   | %  |

<sup>1</sup> Liquidation portfolio represents a portfolio of distressed bonds. Federated has been retained by a third party to manage these assets through an orderly liquidation process that will generally occur over a multi-year period.

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## Changes in Fixed-Income and Equity Fund and Separate Account Assets

| (in millions)                                      | Three Months Ended |          |
|--|--------------------|----------|
|  | March 31,<br>2013  | 2012     |
| <b>Fixed-Income Funds</b>                          |                    |          |
| Beginning assets                                   | \$42,478           | \$37,241 |
| Sales  | 5,148              | 4,822    |
| Redemptions  | (5,009)            | (3,987)  |
| Net sales  | 139                | 835      |
| Net exchanges                                      | (42)               | (59)     |
| Market gains and losses/reinvestments <sup>1</sup> | 37                 | 509      |
| Ending assets                                      | \$42,612           | \$38,526 |
| <b>Fixed-Income Separate Accounts</b>              |                    |          |
| Beginning assets                                   | \$10,233           | \$7,573  |
| Sales <sup>2</sup>                                 | 531                | 220      |
| Redemptions <sup>2</sup>                           | (645)              | (280)    |
| Net redemptions <sup>2</sup>                       | (114)              | (60)     |
| Market gains and losses/reinvestments <sup>1</sup> | 39                 | 182      |
| Ending assets                                      | \$10,158           | \$7,695  |
| <b>Total Fixed-Income</b>                          |                    |          |
| Beginning assets                                   | \$52,711           | \$44,814 |
| Sales <sup>2</sup>                                 | 5,679              | 5,042    |
| Redemptions <sup>2</sup>                           | (5,654)            | (4,267)  |
| Net sales <sup>2</sup>                             | 25                 | 775      |
| Net exchanges                                      | (42)               | (59)     |
| Market gains and losses/reinvestments <sup>1</sup> | 76                 | 691      |
| Ending assets                                      | \$52,770           | \$46,221 |
| <b>Equity Funds</b>                                |                    |          |
| Beginning assets                                   | \$23,152           | \$21,930 |
| Sales  | 1,752              | 1,823    |
| Redemptions  | (2,388)            | (2,187)  |
| Net redemptions                                    | (636)              | (364)    |
| Net exchanges                                      | 47                 | (12)     |
| Market gains and losses/reinvestments <sup>1</sup> | 1,928              | 2,058    |
| Ending assets                                      | \$24,491           | \$23,612 |
| <b>Equity Separate Accounts</b>                    |                    |          |
| Beginning assets                                   | \$11,858           | \$8,957  |
| Sales <sup>2</sup>                                 | 1,106              | 1,461    |
| Redemptions <sup>2</sup>                           | (568)              | (486)    |
| Net sales <sup>2</sup>                             | 538                | 975      |
| Market gains and losses/reinvestments <sup>1</sup> | 965                | 573      |
| Ending assets                                      | \$13,361           | \$10,505 |

|  |          |          |   |
|--|----------|----------|---|
| Total Equity                                       |          |          |   |
| Beginning assets                                   | \$35,010 | \$30,887 |   |
| Sales <sup>2</sup>                                 | 2,858    | 3,284    |   |
| Redemptions <sup>2</sup>                           | (2,956   | ) (2,673 | ) |
| Net (redemptions) sales <sup>2</sup>               | (98      | ) 611    |   |
| Net exchanges                                      | 47       | (12      | ) |
| Market gains and losses/reinvestments <sup>1</sup> | 2,893    | 2,631    |   |
| Ending assets                                      | \$37,852 | \$34,117 |   |

<sup>1</sup> Reflects approximate changes in the fair value of the securities held by the portfolios, and, to a lesser extent, reinvested dividends, distributions, net investment income and the impact of changes in foreign exchange rates.

<sup>2</sup> For certain accounts, Sales and Redemptions are calculated as the remaining difference between beginning and ending assets after the calculation of Market gains and losses/reinvestments.

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## Changes in Liquidation Portfolio

| (in millions)         | Three Months Ended |         |
|-----------------------|--------------------|---------|
|                       | March 31,<br>2013  | 2012    |
| Liquidation Portfolio |                    |         |
| Beginning assets      | \$7,346            | \$8,856 |
| Net redemptions       | (327)              | (273)   |
| Ending assets         | \$7,019            | \$8,583 |

Changes in Federated's average asset mix period-over-period across both asset class and product types have a direct impact on Federated's operating income. As described above, asset mix impacts Federated's total revenue due to the difference in the fee rates earned on each asset class and product type per invested dollar and certain components of distribution expense can vary depending upon the asset class, distribution channel and/or the size of the customer relationship. The following table presents the relative composition of average managed assets and the percent of total revenue derived from each asset class and product type for the periods presented:

| By Asset Class        | Percent of Total Average Managed Assets |      | Percent of Total Revenue     |      |   |
|-----------------------|---|------|------------------------------|------|---|
|                       | Three Months Ended March 31,            |      | Three Months Ended March 31, |      |   |
|                       | 2013                                    | 2012 | 2013                         | 2012 |   |
| Money market assets   | 75                                      | % 77 | % 43                         | % 46 | % |
| Fixed-income assets   | 14                                      | % 12 | % 23                         | % 21 | % |
| Equity assets         | 9                                       | % 9  | % 33                         | % 32 | % |
| Liquidation portfolio | 2                                       | % 2  | % 0                          | % 0  | % |
| Other activities      | --                                      | --   | 1                            | % 1  | % |
| By Product Type       |   |      |                              |      |   |
| Funds:                |   |      |                              |      |   |
| Money market assets   | 66                                      | % 68 | % 42                         | % 45 | % |
| Fixed-income assets   | 11                                      | % 10 | % 21                         | % 20 | % |
| Equity assets         | 6                                       | % 6  | % 27                         | % 27 | % |
| Separate Accounts:    |   |      |                              |      |   |
| Money market assets   | 9                                       | % 9  | % 1                          | % 1  | % |
| Fixed-income assets   | 3                                       | % 2  | % 2                          | % 1  | % |
| Equity assets         | 3                                       | % 3  | % 6                          | % 5  | % |
| Liquidation Portfolio | 2                                       | % 2  | % 0                          | % 0  | % |
| Other activities      | --                                      | --   | 1                            | % 1  | % |

Total managed assets represent the balance of AUM at a point in time. By contrast, average managed assets represent the average balance of AUM during a period of time. Because substantially all revenue and certain components of distribution expense are generally calculated daily based on AUM, changes in average managed assets are typically a key indicator of changes in revenue earned and asset-based expenses incurred during the same period.

March 31, 2013 period-end managed assets increased 4% over period-end managed assets at March 31, 2012 due primarily to increases in period-end fixed-income, money market and equity assets. Average managed assets for the three-month period ended March 31, 2013 increased 3% over average managed assets for the same period in 2012 primarily as a result of increases in average fixed-income and equity assets. Period-end money market assets at March 31, 2013 increased 2% as compared to March 31, 2012. Average money market assets for the three-month period ended March 31, 2013 increased 1% as compared to the same period in 2012. The financial markets posted a

strong performance in the first quarter 2013 despite the continued pressure of global macroeconomic events. Short-term interest rates remained low in the first quarter 2013. Period-end fixed-income assets at March 31, 2013 increased 14% as compared to March 31, 2012 primarily due to positive net sales and market appreciation. Average fixed-income assets for the three-month period ended March 31, 2013 increased 15% as compared to the same period in 2012. Period-end equity assets at March 31, 2013 increased 11% as compared to March 31, 2012 primarily due to market appreciation. Average equity assets for the three-month period ended March 31, 2013 increased 12% as compared to the same period in 2012. As expected, the liquidation portfolio at March 31, 2013 decreased 18% as compared to March 31,

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2012 and average assets in the liquidation portfolio for the three-month period ended March 31, 2013 decreased 17% as compared to the same period in 2012 due to the gradual liquidation of the portfolio.

## Results of Operations

Revenue. The following table sets forth components of total revenue for the periods presented:

| (in millions)                                  | Three Months Ended<br>March 31, |         |          |                   |
|--|---------------------------------|---------|----------|-------------------|
|  | 2013                            | 2012    | Change   | Percent<br>Change |
| Revenue from managed assets                    | \$225.8                         | \$228.4 | \$(2.6 ) | (1 )%             |
| Revenue from sources other than managed assets | 2.2                             | 1.9     | 0.3      | 16 %              |
| Total revenue                                  | \$228.0                         | \$230.3 | \$(2.3 ) | (1 )%             |

Revenue from managed assets decreased \$2.6 million for the three-month period ended March 31, 2013 as compared to the same period in 2012 primarily due to an increase of \$6.9 million in voluntary fee waivers related to certain money market funds in order for these funds to maintain positive or zero net yields and a decrease of \$2.8 million due to the impact of the leap year in 2012 compared to 2013. The decrease in revenue was partially offset by an increase of \$4.1 million resulting from higher average fixed-income assets and an increase of \$3.2 million resulting from higher average equity assets.

See Business Developments – Historically Low Short-Term Interest Rates for additional information on voluntary fee waivers related to certain money market funds in order for these funds to maintain positive or zero net yields, including the offsetting decreases in expense and net income attributable to noncontrolling interests, the net pre-tax impact on income and a discussion of management's expectation regarding the pre-tax impact on income from fee waivers for the second quarter of 2013.

For the three-month period ended March 31, 2013, Federated's ratio of revenue from managed assets to average managed assets was 0.24% as compared to 0.25% for the same period of 2012. The decrease in the rate was primarily due to the increase in voluntary fee waivers to maintain positive or zero net yields on certain money market funds for the three-month period ended March 31, 2013 as compared to the same period of 2012.

Operating Expenses. The following table sets forth significant fluctuations in operating expenses for the periods presented:

| (in millions)            | Three Months Ended<br>March 31, |         |          |                   |
|--------------------------|---------------------------------|---------|----------|-------------------|
|                          | 2013                            | 2012    | Change   | Percent<br>Change |
| Compensation and related | \$66.9                          | \$64.1  | \$2.8    | 4 %               |
| Distribution             | 58.2                            | 61.7    | (3.5 )   | (6 )%             |
| All other                | 34.7                            | 34.1    | 0.6      | 2 %               |
| Total operating expenses | \$159.8                         | \$159.9 | \$(0.1 ) | 0 %               |

Total operating expenses for the three-month period ended March 31, 2013 decreased \$0.1 million compared to the same period in 2012. Distribution expense decreased \$3.5 million in the first quarter 2013 as compared to the same period in 2012 primarily due to a \$7.3 million decrease resulting from higher fee waivers associated with maintaining positive or zero net yields on certain money market funds, partially offset by a \$4.2 million increase primarily related

to a change in the mix of average money market assets. Compensation and related expense increased \$2.8 million in the first quarter 2013 as compared to the same period in 2012 reflecting a \$1.8 million increase in base compensation primarily due to increased headcount and a \$0.8 million increase in incentive compensation.

Income Taxes. The income tax provision decreased \$0.9 million for the three months ended March 31, 2013 as compared to the same period in 2012 primarily due to a reduction to the capital loss deferred tax asset valuation allowance partially offset by increased state taxes. The effective tax rate was 35.5% for the three-month period ended March 31, 2013 as compared to 36.5% for the same period in 2012. The decrease in the effective tax rate primarily related to a reduction to the capital loss deferred tax asset valuation allowance (1.4%) partially offset by increased state taxes (0.4%).

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Liquidity and Capital Resources

**Liquid Assets.** At March 31, 2013, liquid assets, net of noncontrolling interests, consisting of cash and cash equivalents, investments and receivables, totaled \$248.4 million as compared to \$271.9 million at December 31, 2012. The decrease of \$23.5 million primarily reflects a decrease of \$15.5 million in Cash and cash equivalents, which is summarized in the discussion below and a decrease of \$6.3 million in Investments—affiliates due primarily to net redemptions of available-for-sale securities in the first three months of 2013.

At March 31, 2013, Federated's liquid assets included investments in certain Federated-sponsored money market and fluctuating-value funds that may have direct and/or indirect exposures to international sovereign debt and currency risks. Federated has been actively monitoring its money market, fixed-income and equity portfolios to manage sovereign debt and currency risks with respect to recent events in certain euro-zone countries. Federated's experienced portfolio managers and analysts work to evaluate credit risk through quantitative and fundamental analysis. Further, for cash invested in certain money market funds (approximately \$34 million), only indirect short-term exposures exist primarily to high-quality international bank names that are subject to Federated's credit analysis process and meet the requirements of Rule 2a-7.

**Cash Provided by Operating Activities.** Net cash provided by operating activities totaled \$19.8 million for the three months ended March 31, 2013 as compared to \$30.3 million for the same period in 2012. The decrease of \$10.5 million was primarily due to a \$6.4 million increase in cash paid for taxes for the three months ended March 31, 2013 as compared to the same period in 2012 due to a \$5.0 million federal extension payment in the first quarter 2013 while none was required in the first quarter 2012. The remaining difference is primarily related to cash paid to vendors for operating activities.

**Cash Provided by Investing Activities.** During the three-month period ended March 31, 2013, cash provided by investing activities was \$4.5 million and was primarily related to \$11.8 million in redemptions of available-for-sale securities, partially offset by \$3.4 million in cash paid in connection with acquisitions and \$3.1 million in cash paid for property and equipment.

**Cash Used by Financing Activities.** During the three-month period ended March 31, 2013, cash used by financing activities was \$35.4 million. During the first three months of 2013, Federated paid \$25.1 million or \$0.24 per share in dividends to holders of its common shares and repaid \$10.6 million in connection with its long-term debt obligations (see Note (8) to the Consolidated Financial Statements for additional information).

**Borrowings.** In 2011, Federated entered into an Amended and Restated Credit Agreement with a syndicate of banks that included a \$382.5 million term loan (Term Loan) and \$200 million revolving credit facility (collectively, Credit Agreement). Proceeds have been used for general corporate purposes including cash payments related to acquisitions, dividends, investments and share repurchases. During each of the three months ended March 31, 2013 and 2012, Federated made principal payments of \$10.6 million on the Term Loan. As of March 31, 2013, the entire \$200 million revolving credit facility was available for borrowings. The interest rate swap (the Swap) that Federated entered into during 2010 to hedge its interest rate risk associated with the term loan remains in effect. The Swap converts the variable interest rate on the Term Loan to a fixed rate of 3.646%. See Note (8) to the Consolidated Financial Statements for additional information.

The Credit Agreement has an interest coverage ratio covenant (consolidated earnings before interest, taxes, depreciation and amortization (EBITDA) to consolidated interest expense) and a leverage ratio covenant (consolidated

debt to consolidated EBITDA) as well as other customary terms and conditions. Federated was in compliance with its interest coverage and leverage ratios at and during the three months ended March 31, 2013. An interest coverage ratio of at least 4 to 1 is required and as of March 31, 2013, the interest coverage ratio was 28 to 1. A leverage ratio of no more than 2.5 to 1 is required and as of March 31, 2013, the leverage ratio was 0.88 to 1. The Credit Agreement and the Swap also have certain stated events of default and cross default provisions which would permit the lenders/counterparties to accelerate the repayment of the debt or the Swap if not cured within the applicable grace periods. The events of default generally include breaches of contract, failure to make required loan payments, insolvency, cessation of business, deterioration in credit rating to below investment grade, notice of lien or assessment and other proceedings, whether voluntary or involuntary, that would require the repayment of amounts borrowed.

Future Cash Needs. In addition to the contractual obligations and contingent liabilities described below, management expects that principal uses of cash will include paying incentive and base compensation, funding distribution expenditures, paying shareholder dividends, repaying debt obligations, funding business acquisitions and global expansion, paying taxes, repurchasing company stock, advancing sales commissions, seeding new products and funding property and equipment

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acquisitions, including computer-related software and hardware. As a result of the highly regulated nature of the investment management business, management anticipates that expenditures for compliance and investment management personnel, compliance systems and related professional and consulting fees may continue to increase.

On April 25, 2013, the board of directors declared a \$0.24 per share dividend to shareholders of record as of May 8, 2013 to be paid on May 15, 2013.

After evaluating Federated's existing liquid assets, expected continuing cash flow from operations, its remaining borrowing capacity under the revolving credit facility of the Credit Agreement and its ability to obtain additional financing arrangements and issue debt or stock, management believes it will have sufficient liquidity to meet its present and reasonably foreseeable cash needs. Although management currently is not projecting to draw on the availability under the revolving credit facility for the next 12 months, management may choose to borrow additional amounts up to the maximum available under the revolving credit facility which could cause total outstanding borrowings to total as much as \$498 million.

Financial Position

The following discussion summarizes significant changes in assets and liabilities that are not discussed elsewhere in Management's Discussion and Analysis of Financial Condition and Results of Operations and the status of Federated's goodwill and equity-method investment as of March 31, 2013.

Accrued compensation and benefits at March 31, 2013 decreased \$44.7 million from December 31, 2012 primarily due to the annual 2012 accrued incentive compensation being paid in the first quarter 2013 (\$55.2 million), partially offset by the accrual of 2013 incentive compensation earned in the first quarter of 2013 (\$20.8 million).

Long-term deferred tax liability, net at March 31, 2013 increased \$11.4 million from December 31, 2012 primarily as a result of tax amortization in excess of book amortization of intangible assets (\$5.6 million), a decrease in long-term incentive compensation (\$2.0 million) and a decrease in share-based compensation (\$1.4 million).

Investments—consolidated investment companies at March 31, 2013 increased \$65.4 million from December 31, 2012 primarily as a result of the consolidation of an investment company in the first quarter 2013. Redeemable noncontrolling interest in subsidiaries at March 31, 2013 increased \$71.7 million from December 31, 2012. This increase primarily reflects non-Federated ownership interests in the investment company consolidated in the first quarter 2013. See Note (5) for additional information.

There were no indicators of goodwill impairment as of March 31, 2013 as Federated's market capitalization exceeded the book value of equity by more than 350%.

Federated holds a 12% non-voting, noncontrolling interest in a privately-held investment management firm that is registered as an investment adviser and a commodity trading adviser. This investment is accounted for using the equity-method of accounting. The excess carrying value of Federated's equity-method investment as compared to its proportionate share of the investee's underlying net assets reflects goodwill. During 2012, due to declines in the investee's AUM, their performance relative to indices and the uncertainty regarding each in the future, Federated evaluated the carrying value of its investment for other-than-temporary impairment under the equity-method of accounting. Management estimated the fair value of its investment at December 31, 2012 and determined that it was other-than-temporarily impaired. Accordingly, Federated recorded a \$3.0 million impairment charge in Nonoperating Income (Expenses) – Other, net to write down the equity-method investment to a fair value of \$3.8 million as of

December 31, 2012. The estimate of fair value was based primarily upon the present value of expected future cash flows using an income approach valuation methodology with unobservable data inputs (Level 3). Significant unobservable model inputs included: (1) projected AUM across product lines with a 10-year compounded annual growth rate of 15% and a terminal growth rate of 3%; and (2) a 17% discount rate based upon the current estimated market rate of return. No new indicators of impairment existed as of March 31, 2013. Given uncertainties regarding the success of future sales efforts and possible prolonged periods of over/underperformance compared to indices and the significance of these factors to AUM, management cannot be certain of the outcome of future cash flow analyses for this investment with a remaining carrying value and maximum exposure to loss of \$3.8 million at March 31, 2013.

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Contractual Obligations and Contingent Liabilities

Contingent Payments. Pursuant to various acquisition- and employee-related agreements, Federated is required to make certain periodic contingent payments. Details regarding these commitments are as follows:

In 2010, Federated acquired the money market management business of SunTrust Banks, Inc. (SunTrust Acquisition). As part of the SunTrust Acquisition, Federated is required to make annual contingent purchase price payments in the fourth quarters of each of the five years following the acquisition date. The contingent purchase price payments are calculated as a percentage of revenue less distribution expenses directly attributed to certain eligible assets. The first two contingent purchase price payments of \$5.0 million and \$4.2 million were paid in the fourth quarters of 2011 and 2012, respectively. At March 31, 2013, management estimated remaining contingent payments could total \$11 million over the three years that remain; however, the actual amount of the contingent payments will vary based on asset levels and related net revenues and is not limited by any maximum amount. A wide range of outcomes for actual payments is possible due to the extent of reasonably possible flow-rate volatility for the respective AUM. As of March 31, 2013, a liability of \$8.2 million representing the estimated fair value of future consideration payments was recorded in Other current liabilities (\$3.5 million) and Other long-term liabilities (\$4.7 million) (see Note (7)(a) to the Consolidated Financial Statements for a discussion regarding the valuation methodology). This liability is remeasured at each reporting date with changes in the fair value recognized in Intangible asset related expense on the Consolidated Statements of Income.

In 2008, Federated completed the acquisition of certain assets of Clover Capital Management, Inc., a Rochester, New York-based investment manager that specializes in value investing (Clover Capital Acquisition). As part of the Clover Capital Acquisition, Federated is required to make contingent purchase price payments based upon growth in revenues over the five-year period following the acquisition date. The contingent purchase price payments, which could total as much as \$56 million, will be recorded as additional goodwill at the time the contingency is resolved. The applicable growth targets were not met for the first two anniversary years and as such, no related payments were made. In the first quarter 2012 and 2013, \$5.9 million and \$3.4 million were paid with regard to the third and fourth anniversary years, respectively. As of March 31, 2013, no amounts were accrued for the fifth anniversary year ending in December 2013.

Pursuant to other acquisition agreements, Federated may be required to make additional purchase price payments based on a percentage of revenue less certain direct expenses attributable to eligible AUM. The payments could occur annually through 2017. As of March 31, 2013, liabilities totaling \$3.5 million and representing the estimated fair value of future consideration payments were recorded in Other current liabilities (\$0.8 million) and Other long-term liabilities (\$2.7 million) (see Note (7)(a) for a discussion regarding the valuation methodology). The liabilities are remeasured at each reporting date with changes in the fair value recognized in Intangible asset related expense and/or Other expense on the Consolidated Statements of Income.

Pursuant to various significant employment arrangements, Federated may be required to make certain incentive compensation-related payments. The employment contracts expire on various dates through the year 2014 with payments possible through 2018. As of March 31, 2013, the maximum bonus payable over the remaining terms of the contracts approximates \$43 million, none of which would be payable in the remainder of 2013. In addition, certain employees have incentive compensation opportunities related to the Federated Kaufmann Large Cap Fund (the Fund Bonus). Assuming asset levels and other variable inputs at March 31, 2013 remain constant throughout the year, the Fund Bonus payment in 2014 may approximate \$1 million. Management is unable to reasonably estimate a range of possible bonus payments for the Fund Bonus for subsequent years due to the wide range of possible growth-rate scenarios.

Legal Proceedings. Federated has claims asserted and threatened against it in the ordinary course of business. As of March 31, 2013, Federated does not believe that a material loss related to these claims is reasonably possible.

#### Recent Accounting Pronouncements

For a complete list of new accounting standards recently adopted by Federated, see Note (3) to the Consolidated Financial Statements.

#### Critical Accounting Policies

Federated's Consolidated Financial Statements have been prepared in accordance with U.S. generally accepted accounting principles (GAAP). In preparing the financial statements, management is required to make estimates and assumptions that

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Management's Discussion and Analysis (continued)  
of Financial Condition and Results of Operations (unaudited)

affect the amounts reported in the Consolidated Financial Statements and accompanying notes. Management continually evaluates the accounting policies and estimates it uses to prepare the Consolidated Financial Statements. In general, management's estimates are based on historical experience, information from third-party professionals and various other assumptions that are believed to be reasonable under the facts and circumstances. Actual results may differ from those estimates made by management and those differences may be material.

Of the significant accounting policies described in Federated's Annual Report on Form 10-K for the year ended December 31, 2012, management believes that its policies regarding accounting for intangible assets, acquisition-related future consideration liabilities and income taxes involve a higher degree of judgment and complexity. See Note (1) of the Consolidated Financial Statements and the section entitled Critical Accounting Policies in Management's Discussion and Analysis of Financial Condition and Results of Operations included in Federated's Annual Report on Form 10-K for the year ended December 31, 2012 for a complete discussion of these policies.

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Part I, Item 3. Quantitative and Qualitative Disclosures About Market Risk  
(unaudited)

There have not been any material changes to Federated's exposures to market risk during the three months ended March 31, 2013 that would require an update to the disclosures provided in Federated's Annual Report on Form 10-K for the year ended December 31, 2012.

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Part I, Item 4. Controls and Procedures  
(unaudited)

Federated carried out an evaluation, under the supervision and with the participation of management, including Federated's President and Chief Executive Officer and Chief Financial Officer, of the effectiveness of Federated's (a) disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of March 31, 2013. Based upon that evaluation, the President and Chief Executive Officer and the Chief Financial Officer concluded that Federated's disclosure controls and procedures were effective at March 31, 2013.

There has been no change in Federated's internal control over financial reporting that occurred during the quarter (b) ended March 31, 2013 that has materially affected, or is reasonably likely to materially affect, Federated's internal control over financial reporting.

Table of ContentsPart II. Other Information  
(unaudited)

## Item 1A. Risk Factors

There are no material changes to the risk factors included in Federated's Annual Report on Form 10-K for the fiscal year ended December 31, 2012.

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

(c) The following table summarizes stock repurchases under Federated's share repurchase program during the first quarter 2013.

|                      | Total Number<br>of Shares<br>Purchased | Average<br>Price Paid<br>per Share | Total Number of Shares<br>Purchased as Part of<br>Publicly Announced<br>Plans or Programs <sup>1</sup> | Maximum Number of Shares that<br>May Yet Be Purchased Under<br>the<br>Plans or Programs <sup>1</sup> |
|----------------------|--|------------------------------------|--|--|
| January <sup>2</sup> | 21,472                                 | \$2.93                             | 0  | 1,859,834  |
| February             | 20,000                                 | 23.28                              | 20,000   | 1,839,834  |
| March                | 90,000                                 | 24.24                              | 90,000   | 1,749,834  |
| Total                | 131,472                                | \$20.62                            | 110,000  | 1,749,834  |

Federated's share repurchase program was authorized in August 2008 by the board of directors and permits the purchase of up to 5.0 million shares of Federated Class B common stock with no stated expiration date. No other plans existed as of March 31, 2013.

<sup>2</sup> In January 2013, 21,472 shares of restricted stock with a weighted-average price of \$2.93 per share were repurchased in connection with employee separations.

Part II, Item 5. Other Information  
(unaudited)

SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.

At the Annual Meeting of Shareholders of Federated Investors, Inc. (Federated) held on Thursday, April 25, 2013 in Pittsburgh, Pennsylvania, the holder of Federated's Class A Common Stock, which constituted all of the shares entitled to vote at the meeting, approved the following proposal which is described in more detail in Federated's Information Statement to shareholders dated March 13, 2013 (Information Statement).

The holder of Federated's Class A Common Stock elected six individuals to the Board of Directors as set forth below:

| Director               | Shares Voted For | Shares Withheld |
|------------------------|------------------|-----------------|
| John F. Donahue        | 9,000            | —               |
| J. Christopher Donahue | 9,000            | —               |
| Michael J. Farrell     | 9,000            | —               |
| David M. Kelly         | 9,000            | —               |
| John W. McGonigle      | 9,000            | —               |
| Edward G. O'Connor     | 9,000            | —               |

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Part II, Item 6. Exhibits  
(unaudited)

The following exhibits required to be filed or furnished by Item 601 of Regulation S-K are filed or furnished herewith and incorporated by reference herein:

Exhibit 31.1 – Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith)

Exhibit 31.2 – Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith)

Exhibit 32 – Certification pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (furnished herewith)

The following XBRL documents are filed herewith:

Exhibit 101.INS – XBRL Instance Document

Exhibit 101.SCH – XBRL Taxonomy Extension Schema Document

Exhibit 101.CAL – XBRL Taxonomy Extension Calculation Linkbase Document

Exhibit 101.DEF – XBRL Taxonomy Extension Definition Linkbase Document

Exhibit 101.LAB – XBRL Taxonomy Extension Label Linkbase Document

Exhibit 101.PRE – XBRL Taxonomy Extension Presentation Linkbase Document

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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.

Federated Investors, Inc.  
(Registrant)

Date April 26, 2013

By: /s/ J. Christopher Donahue  
J. Christopher Donahue  
President and  
Chief Executive Officer

Date April 26, 2013

By: /s/ Thomas R. Donahue  
Thomas R. Donahue  
Chief Financial Officer