Wealth Management M&A To Pick Up in 2010

Originally Published By Halah Touryalai, Registered Rep.

Mergers and acquisitions in the wealth management business will bounce back in 2010 as valuations and cash flows pick up with the improving market and economy, experts predict. But buyers and sellers will be more selective than they were during the last M&A boom in the business between 2004 and 2007, according to **Echelon Partners**, a Los Angeles-based M&A consulting firm.

Still, this year's dealmaking could yield substantial payoffs for wealth managers who are willing to roll up their sleeves a bit, the group says in its 2010 outlook report.

Low valuation multiples (triggered mostly by lagging cash flows) over the last two years kept many advisors from selling their firms, says **Daniel Seivert**, CEO and managing partner of Echelon Partners. But with multiples creeping back, many of those same advisors are now ready to make deals, he says. Advisors that wouldn't even entertain the idea of selling their firm during the downturn are now at entertaining the idea. However, they are being cautious in how they do deals.

Seivert says a firm with $2 million in revenue and $1 million in profit was selling at 6 times cash flow, or $6 million, between 2004 and 2007. In 2008 and 2009, that same firm saw valuation multiples slip to around 4 to 5 times cash flows. In 2010, the valuation multiples should be off 10 percent to 20 percent from their peak.

The magnitude of this year's bounce back will depend greatly on the market's performance. If the equity market rises 10 percent or more, the supply of wealth management sellers will increase significantly over 2009 levels but will likely remain below the peak numbers recorded between 2004 and 2007. Seivert expects deals to number around 450 this year, up from 300 a year in 2008 and 2009. By comparison, the number of deals done a year between 2004 and 2007 ranged from 600 to 750, Seivert says.

Charles Schwab's M&A data contradict these numbers, showing that the number of deals done between RIAs in any year between 2002 and 2009 did not exceed 100. But Echelon says that many firms do not report their transactions and that what constitutes a deal varies; some equity transactions among insiders or partners in the business are often either not announced or not counted. That said, even Schwab agrees that 2010 will be a better year for RIA M&A.

Echelon says that it may take partners longer to negotiate deal structures, and that sellers will demand more upfront cash and guarantees instead of equity. A deal that might have taken five months to complete could take nine months, he says, and a deal that would have been done in nine months could take up to 13 months. The time it takes for these deals to close will take longer because sellers will be doing more due diligence and more shopping around instead of selling to the highest bidder, Seivert says.

Another potential shift in M&A deals in 2010 is that retiring advisors will look to phase out of the business, selling pieces to internal partners over time rather than selling to third parties all in one go. As this trend takes hold, it will create downward pressure on the number of true outright sales to external third parties, unless those third parties are tolerant of longer-term equity hold times by the selling advisors, the report says.

Sales to third parties like RIA roll-ups are already lagging. In 2004 and 2005, bank acquisitions of RIAs represented between 40 and 50 percent of all RIA assets acquired. But through the third quarter of 2009, national banks acquired almost no RIA assets while regional banks accounted for less than 5 percent of RIA assets acquired, according to Schwab Advisor Services Strategic Business Development. Meanwhile, private-equity backed consolidators like Focus Financial and WealthTrust, which offer back-office support and consulting to networks of RIAs, are also being less aggressive about acquisitions. In 2003, consolidators accounted for just eight percent of all RIA assets acquired. In 2007, they accounted for 45 percent. Through the third quarter of 2009, it was 35 percent. (See Registered Rep.'s December 2009 cover story for more about RIA roll-up problems.)

Echelon Partners says 2010 will be a mixed year for aggregators. On the positive side, there will be more deals to chase. On the negative side, the deal process may slow down as would-be partners or acquisitions will likely be asking more questions and conducting more due diligence along the way. This is a natural by-product of the economic downturn we experienced, but there is also an increasing amount of skepticism about rollup firms.

ABOUT ECHELON PARTNERS

Daniel Seivert

Managing Director

dseivert@echelon-group.com