

ARBITRAGE AND MOMENTUM IN ADVISORY CONSOLIDATION

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The pace of wealth-firm aggregations seems to be picking up. Adding to recent purchases by comparative newcomers **Focus Financial Partners** and **United Capital Financial**, veteran advisory acquirers wealthtrust.com WealthTrust and **Boston Private Financial Holdings** have moved to expand and solidify their respective affiliate networks. For all the activity so far, however, industry participants say it's just a foretaste of deal-flow to come as savvy buyers wave wads of cash and parent-company stock under the noses of liquidity-strapped firm owners in need of viable growth-and-exit strategies.

"You're going to continue to see this kind of activity for a while," says **Elizabeth Nesvold**, managing partner of New York-based M&A consultancy **Silver Lane Advisors**, referring to recent acquisitions in the RIA space. "The firms doing the roll-ups take different approaches but [they are showing] that they know how to structure and execute these kinds of deals."

Dan Seivert, CEO of Los Angeles-based investment banking and consulting firm **Echelon Partners**, agrees that move toward integration among independent wealth firms is still in its infancy. "Some of the early players are making themselves known," he says. "And there are 15 or 20 others right behind them."

Deals

Late this past summer Boston Private, which started buying private banks and investment advisories a decade ago, established a private-banking and trust presence in New York when one of its affiliates, Coral Gables, Fla.-based **Gibraltar Private Bank & Trust**, opened an office in Manhattan. This gives Boston Private a wealth-management "cluster" in the Big Apple to match similar groupings of private-banking and high-net-worth advisory affiliates in or around Boston, San Francisco and Seattle.

Nashville-based WealthTrust, which also did its first deals in the late 1990s, last week completed its first acquisitions in a year by taking stakes in Cleveland, Ohio-based **Fairport Asset Management** and Radnor, Pa.-based **Axiom Asset Management**. These transactions extend WealthTrust's presence into Ohio and the Northeast, increase its total assets under management to around \$9 billion and -- through Fairport -- gives it a shot at sharpening its network-wide financial-planning capabilities.

New York-based Focus, which made its first acquisitions late in 2005, brought in five more fee-based affiliates over the last three or four months, giving it a total of 14 "partner" firms and around \$25 billion in client assets. Newport Beach, Calif.-based United, another two year old, recently acquired four firms to give it a network of more than a dozen offices and approximately \$8 billion in client assets.

The simple view of the aggregation phenomenon has buyers wanting in on an anticipated bonanza in wealth management as hordes of baby boomers -- flush with assets from inheritances, business sales and pension-plan nest eggs -- look for help sorting out their finances and investments to prepare for retirement or, where there's enough money on hand, to get their estates in order.

Cycles

In addition, market research indicates that the high-net-worth clients prefer the fee-based, fiduciary, and product-neutral RIA business model over the traditional service offerings of big banks and brokerages -- many of which have responded by re-molding their approaches to wealth management, says Fairport's CEO **Scott Roulston**.

Independent RIAs are the fastest-growing asset gatherers in the financial-service industry, says Tiburon, Calif.-based market-research firm **Tiburon Strategic Advisors**. Boston-based **Cerulli Associates**, another research firm, says that the RIA space has grown from about \$950 billion and 11,745 firms in 2005 to \$1.4 trillion and 14,451 firms in 2007.

Though this paints a tantalizing picture, the image is still blurry until you realize that most independent RIA owners are themselves boomers -- and they're just as keen as their clients to see themselves rewarded for decades of hard work. Unfortunately their principal assets -- their businesses -- aren't, in most cases, especially fungible. And this makes buying such firms a neat arbitrage play for the early-in aggregators.

Wealth-firm owners "are suffering from illiquidity," says Seivert. But as more buyers come into the market, the arbitrage aspect of acquiring such firms -- that a network of affiliates, suitably managed, is worth a lot more in re-sale or IPO than the same firms would be as standalones -- is likely to be diluted as competition among buyers inflates initial asking prices.

This makes speed in establishing a viable network of affiliates and parlaying it into a significant liquidity event a vital consideration for wealth-firm consolidators.

Haves

It also means that firms looking for buyers need a realistic understanding of their place in the market.

In a 2005 report called **Back to the Future, JPMorgan Asset Management's Undiscovered Managers** points to a growing gulf between "have" and "have not" firms. The have-nots may compensate their owners pretty well, but they lack the resources to fund expansion or react nimbly to changes in the marketplace by, for instance, investing in new technologies and coping with more stringent compliance.

"[The have-not] group includes about 94% of all industry participants and all of those firms [with] less than \$25 million [in] assets under management," says the Undiscovered Managers study. The have-not category also includes "firms that generate between \$1 million and \$3 million in annual revenues but have unattractive client bases or are inefficient."

The haves meanwhile are "mid-sized firms with annual revenues of \$1 million to \$3 million, and a small percentage of organizations that have less than \$1 million in annual revenue but more than \$25 million of assets under management," says Back to the Future. "Although not yet large companies, these mid-sized firms have robust client bases, are profitable and have the resources to grow their organizations over time."

Aggregation, however nascent, is widening the gulf between have and have-not firms as the haves, pressured by large competitors, coalesce into groups of 40 or 50 "highly profitable" organizations.

Momentum

WealthTrust, Focus, United and Dallas-based **Fiduciary Network**, run by Undiscovered Managers founder **Mark Hurley** are -- the odd 401(k) administrator aside -- fairly pure-play aggregators of fee-based, client-facing wealth-management firms. Boston Private, with considerable holdings in institutionally oriented asset management, straddles the pure-play set and a group of asset-manager aggregators with private-client sidelines like **Affiliated Managers Group, Asset Management Finance** and **Convergent Capital Management**. (Boston Private stands apart from other firm-wide aggregators in having already gone public.) Another half-way participant is insurance-brokerage network **National Financial Partners**.

Meanwhile momentum is becoming as important to attracting new affiliates -- a key ingredient to reaching the critical mass necessary to the arbitrage that underlies many aggregation plays in the wealth-management space.

WealthTrust's acquisitions of Fairport and Axiom were its first since it bought Scottsdale, Ariz.-based **DeGreen Wealth Management** (now **WealthTrust Arizona**) in the fall of 2006. That followed hard on a private-equity infusion that let WealthTrust get back on the acquisition trail after a two-year hiatus imposed by regional brokerage **Morgan Keegan**, its erstwhile owner.

"It feels good to have closed a couple more," says WealthTrust's CEO **Rusty Benton**. "But we never went away: we had to spend time pulling functions out of Morgan Keegan, and on re-integrating our systems, but that's done and we expect to do a couple [of acquisitions] a quarter next year."

United's CEO **Joe Duran** agrees that it's helpful to be seen as an active acquirer. "People look and say, 'Those people are doing things' -- it's very important."

ABOUT ECHELON PARTNERS

ECHELON Partners (ECHELON) was formed in 2001 to offer investment banking and consulting to a subset of the financial services industry known as "investment product developers and distributors" (IPDADs). Since that time, ECHELON's professionals have helped hundreds of senior executives envision, initiate, and execute a multitude of complex business strategies and transactions. ECHELON's business is making companies more valuable through delivering advice and orchestrating transactions. Accordingly, ECHELON measures its success in the enterprise value it creates for its clients. Companies that strive to outperform their peers choose to work with ECHELON because we are as passionate about their results as they are.

Daniel Seivert

Managing Director

dseivert@echelon-group.com