WHY RIC EDELMAN IS GOING PRIVATE

Originally Published By **Dan Jamieson**

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Last week, when he announced that The Edelman Financial Group Inc. will be acquired by private-equity firm Lee Equity Partners LLC., Mr. Edelman said that his firm isn't big enough to develop the liquidity and attention of analysts needed for institutional investors to trade the stock.

“I wasn't dissatisfied with being a public company, per se,” he said. “Our dissatisfaction was that the stock price [did] not accurately reflect the value of the firm.” If there is a lesson in Ric Edelman's decision to take his advisory and planning firm private, it may be that the RIA business is still too much of a cottage industry to merit public ownership.

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SEEING VALUE

By contrast, Lee Equity Partners' interest in buying the firm reflects a positive view of the registered investment advisory industry among private-equity investors “that the public markets haven't embraced,” Mr. Edelman said. Lee Equity Partners will pay $8.85 a share in cash for the company, a premium of 43% over the closing price of $6.18 last Monday when the deal was announced.

The Edelman Financial Group has 43 offices in the United States and manages about $17 billion in client assets.Thirty of those locations are Edelman Financial Services offices, run by employees who follow a standardized planning and investment process. The rest are affiliated independent registered investment advisers.

Last year, the firm ended its independent-contractor broker-dealer business. In 2005, Mr. Edelman's firm became a public entity after he sold it to Sanders Morris Harris Group Inc., a publicly traded holding company. Last year, the Sanders Morris name was dropped in favor of The Edelman Financial Group.

“I was the first person in our industry to become public,” Mr. Edelman said. “Now I'm the first person to delist.” Mr. Edelman declined to comment on whether he might go public again, saying that he would rather focus on one transaction at a time. A number of other RIA firms and consolidators are owned in part by private-equity firms, which, according to their business model, will be looking for ways to exit. Going public is one option for the advisory firms if they are large enough.

Joe Duran, chief executive of United Capital Financial Advisers LLC, a consolidator that has acquired nearly 40 advisory firms, figures that a publicly traded wealth manager requires a market capitalization of $500 million to $1 billion to be viable. “That would imply $200 million to $250 million in revenue, with a reasonable margin,” he said. That translates to about $30 billion in assets.

United Capital manages or oversees about $15 billion and is about “halfway there” in terms of revenue, Mr. Duran said. “Our goal is to monetize existing shareholders, and going public is one of those options, for sure,” Mr. Duran said.

Private-equity firms Bessemer Venture Partners and Grail Partners LLC own about 40% of United Capital, while employees and managers own the rest, Mr. Duran said. According to David DeVoe, managing partner at mergers-and-acquisitions consultant DeVoe & Co. LLC, an RIA firm would need between $15 billion to $30 billion in assets to get to the critical size of about $300 million in market cap.

He noted that few RIA firms are that size. The market cap of The Edelman Financial Group stood at about $200 million prior to news of its sale, and about 35,000 of its shares traded per day. Last year, the firm generated $169 million in revenue, according to the Form 10K it filed with the Securities and Exchange Commission.

By contrast, independent broker-dealer LPL Investment Holdings Inc., which went public in November 2010, has $3.5 billion in annual revenue and a market cap of about $4 billion. Large RIA operations mentioned as potential public enterprises are Focus Financial Partners LLC, whose affiliated firms manage about $45 billion; Fisher Investments, which runs $39 billion; HighTower Advisors LLC, with more than $20 billion; and The Mutual Fund Store, with $6.5 billion in assets.

Focus Financial, which recently secured a $220 million credit line from a group of major banks, has no need to go public, said Rudy Adolf, its founder and chief executive. “We have plenty of capital, and the business is growing,” he said. Dave Eckerly, a spokesman for Fisher Asset Management LLC, said the company has no plans to go public. Representatives for HighTower and The Mutual Fund Store declined to comment.

AVOIDING SCRUTINY

A desire to avoid scrutiny is a major reason large wealth management firms are reluctant to go public and instead seek private financing as a first option, said **Dan Seivert**, chief executive of **Echelon Partners**, an M&A consultant.

"You go public because it's a means of gaining liquidity for yourself or your shareholders," he said. "But if you can gain that liquidity by not going public, and avoid the cost and the quarterly management of earnings, you will."

Mr. Edelman warned that small public financial companies will have a tough time getting investor attention."Will analysts in the financial sector pay attention to Citigroup [Inc.] or to Edelman Financial Group?" he asked. "Being a microcap in the financial services sector is not an ideal situation. In a different industry, it might not be an issue," Mr. Edelman said.

His deal with Lee Equity Partners, which is expected to close in the third quarter, is subject to approval by shareholders and assumes that no other bidders will come knocking in the next month and a half. Assuming that the transaction is completed, Mr. Edelman will walk away with about $15 million in cash, based on his publicly reported holdings of 3.4 million shares in The Edelman Financial Group.

He is converting half his shareholdings into equity in the new venture, which will give him a 30% ownership stake, up from his 11% stake.

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