As M&A activity ramps back up, RIAs need to bone up on the details

Independent advisers want to do deals, but many confess they aren't really prepared to do so

By Jeff Benjamin for InvestmentNews

As the pace of merger and acquisition activity in the RIA space ramps up following a three-month pandemic-related lull, the latest concern is around a gap in understanding the nitty-gritty details of what business consolidation is all about.

"Deal structures are rapidly evolving, and the industry is too dynamic to just say, 'I want to do M&A,'" said Brandon Kawal, principal of Advisor Growth Strategies.

Kawal, who surveyed a cross section of RIA buyers and sellers during the first few months of 2020, found that while owners generally had a realistic grasp of valuations, the increasingly complex nature of deal structures put most firms behind the curve when it comes to approaching a merger or acquisition.

Of the 96 firms surveyed, 51% said they are unprepared to engage in M&A opportunities, and 16% said they are only somewhat prepared. Almost a quarter of respondents admitted to having no idea how a deal would be financed.

Kawal said the findings are important because, looking past the slowdown in activity from March through May, consolidation is seen as a theme that will only gain momentum as more of the aging financial adviser population searches for succession planning solutions.

While the M&A activity is dominated by large aggregator firms that have dedicated acquisition teams, Kawal said not all buyers are at that level of sophistication.

"On the buyer side, there's a need for education around what it takes to compete, which boils down to people, platform and process," he said. "The most established buyers have established platforms you can plug into, so it's important to know who you're competing against."

Sellers, which are often smaller and with less resources dedicated to M&A, can be especially vulnerable to the nuances of consolidation, Kawal said.

"On the seller's side, you need to know what the market is valuing," he said. "Before you go to the market you need to know how to best prepare yourself to command what you want by knowing what buyers will value in your business."

David DeVoe, chief executive of DeVoe & Co., discounted the relatively small sample size of the research, but acknowledged the general premise that RIA owners haven't always given M&A the attention it deserves.

“It is true that most advisers are not prepared for M&A, and rightly so,” DeVoe said. “Their core focus is supporting their clients; M&A for any seller is a once-in-a-lifetime transaction.”

He recalled presentations to a couple of hundred people at conferences where 95% of the audience would identify themselves as RIA buyers.

“Everyone thinks they’re a buyer, but very few fall into the category of qualified buyer,” DeVoe said. “Qualified buyers have sourced capital, have a target profile, have a detailed integration plan, can articulate strategic value, and the list goes on. The devil is in the details. It takes expertise. It takes practice. Most sellers today are looking for a partner who has made one or more acquisitions before. They don’t want to be a test case.”

Mark Bruno, managing director at Echelon Partners, also warned against generalizing with such a small sample size.

“The motivation for engaging in a merger or acquisition can have a direct correlation with the level of preparedness,” he said. “If a firm is strictly looking to be opportunistic, either as a buyer or a seller, in this market and has not given much previous consideration to M&A, they will naturally feel less prepared. There are, however, a number of firms that have been strategically planning for a merger, acquisition, sale or transition for years. They’ve effectively laid the groundwork by conducting a real valuation, developing G2 leadership, and building infrastructure and operations that can help them absorb or integrate with another firm.”