Why Supercharged RIA Mergers, Acquisitions Market May Accelerate

By Charles Paikert for Family Wealth Report

There have been a great deal of wealth sector M&A transactions, but if anything, the pace is going to get hotter, a conference exploring this trend recently heard.

The red hot RIA M&A market shows no signs of cooling down, according to one of the industry's leading buyers.

"The market is not slowing down anytime soon and actually might even accelerate," said David Barton, vice chairman of Mercer Advisors, speaking at a virtual M&A panel presented by Advisor Growth Strategies. "2021 might even be more frothy than last year."

Both M&A deal volume and valuation multiples set records in 2020. The median adjusted EBITDA multiple increased 21 per cent from 2019 to 2020, according to *Advisor Growth's RIA Deal Room* report.

As long as deal activity flourishes, valuations will remain high, said Rush Benton, senior director and a top M&A executive for Captrust, also one of the industry's most active buyers. "There's just too much demand on the buy side," Benton said at the Deal Room roundtable.

Soaring multiples may "price out" some buyers, said Marty Bicknell, CEO of Mariner Wealth Advisors, who also spoke at the Deal Room Virtual Roundtable.

Multiples are now averaging around eight times cash flow for firms under $1 billion in AuM, over 10 times EBITDA for RIAs with more than $1 billion in assets and in the mid-teens for wealth managers with over $5 billion in AuM, according to the Deal Room report and other industry sources.

Nonetheless, there will be "plenty of firms who aren't going to be priced out," Bicknell said. Around ten firms backed by deep-pocketed capital providers "won't need to take a break," he added.

"Gold rush" caveat and criticism of CI Financial
However Barton, Mercer's chief M&A executive, added a caveat to the blue-sky forecasts.

"The gold rush won't last forever, although when [it will stop] is hard to say," Barton said. "The pricing will continue to go up but there will be a point at which that arbitrage will narrow to an extent that it will slow the buying rate."

Barton and other roundtable panelists also took shots at CI Financial, the Canadian asset manager which has upended the RIA mergers and acquisitions market by going on an unprecedented buying spree and acquiring 14 US RIAs in the past 19 months, paying premium prices for most.

CI has been able to buy so many firms so quickly by paying “unheard of multiples in the business,” Barton said. But, citing CI’s 50 per cent decline in stock price over the past seven years, sellers who take equity and are looking for growth may be disappointed, he cautioned.

And some of the large RIAs CI Financial acquired appeared to be “trying to solve for succession and liquidity” rather than looking for scale and growth within a larger organization, according to Benton.

What’s more, Benton implied, for all of its deal activity, CI has yet to demonstrate any proven track record of building scale or integration.

Trends in seller’s market

The current seller’s market has resulted in increased "reverse due diligence" of buyers by advisory owners considering a sale, according to the roundtable panelists.

Even vendors such as asset managers are getting “a lot of questions” about RIA buyers, said Michael Guirguis, director of RIA national accounts for BlackRock. “Sellers are doing their due diligence and really do want to know what it’s like to work with certain firms,” Guirguis said.

The strong demand among buyers for a limited supply of firms has also meant fewer contingency provisions and "earn-outs" in deals.

Instead, more deals are being structured to offer sellers increased incentives for reaching various metrics. Mariner’s “management incentives” are structured over a three-year period, Bicknell said, measuring a firm’s growth beyond the cash flow at the time Mariner bought it.

While cash still accounts for nearly three-fourths of the average deal structure, the number of transactions that included some equity increased 13 per cent in 2020, according to Advisor Growth’s Deal Room report, a trend that appears to be continuing. Mariner is seeing “a relatively high demand for equity” so far this year, according to Bicknell.

And all panelists agreed that big buyers would continue to seek funding from private equity capital providers.

Mercer now receives funding from its third capital provider and equity stake holder, Oak Hill Capital. Captrust sold a 25 per cent stake to private equity firm GTCR last year at a $1.25 billion valuation. In April, Mariner took outside capital for the first time, selling a minority stake to Leonard Green & Partners.

Advice for sellers

Benton: “Don’t over-promise to employees about what they can expect from a transaction.”

Bicknell: “Ask yourself ‘what is my ideal situation and what is non-negotiable’ for a sale.”

Barton: “Go deep on your own numbers, make sure they’re represented fairly and that there are no crazy adjustments. And make sure your core beliefs are the same as the buyer’s. Remember, it’s not about the honeymoon, it’s about the marriage.”