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Banks Scour An Altered Wealth Landscape for Opportunity

The list of banks that divested themselves of asset managers last year includes some of the largest and best-known institutions in the world, from **Barclays** in Europe to **Bank of America** and **Citigroup** in the U.S. But those sales and others tell only part of the story, reflecting a strategic recalibration of the banking industry's money management operations rather than a wholesale retreat.

In particular, many well-capitalized banks remain committed to either expanding existing wealth management operations or adding that capability to their menu of financial services. As those banks emerge from the financial crisis with sturdier balance sheets, many will necessarily consider acquisitions as a component in that strategy.

To be sure, the wealth management sector was hardly spared during the financial meltdown. The sector's reputation suffered serious damage as furious clients watched trillions of dollars disappear without warning and as they pondered the due diligence implications of the Bernard Madoff scandal. In explaining the mood among some clients last year to *Barron's*, one wealth manager at **Wilmington Trust** said, "I've had clients walk in and say, look, I got a statement from Bernie Madoff that said I owned such and such, but it turns out that I didn't own anything — so prove to me you're not Madoff." The bottom line at Wilmington Trust and other wealth managers was also hammered as assets dropped and investors retreated to less profitable safe havens such as money markets and bond funds. In Wilmington's Wealth Advisory Services business, revenues declined 15% in 2009.

But the convulsion of 2007-09 also created opportunity, as clients in the traditionally staid sector responded by aggressively moving assets in whole or part to new managers. Simultaneously, governments in Europe and the U.S. are generating additional opportunities as they press offshore banking centers such as Switzerland and Lichtenstein for greater transparency — and force citizens to repatriate assets in those havens — thereby putting a portion of that money up for play. *Wealth Bulletin* figures more than $500 billion in assets has fled offshore havens in Europe since 2008. "A lot of consumers are disenfranchised and there is a big wide-open door right now," Tiburon Strategic Advisors managing principal Charles Roame told the American Bankers Association Wealth Management and Trust Conference in March. "This is as good as it gets for client acquisition."

For banks, wealth management provides a range of benefits that, in the post-crisis environment, may appear even more attractive. Capital requirements, for one, are lower than in traditional banking operations and profitability and return on investment can be higher. Wealth management can also improve a bank's bottom line and its appeal to investors by diversifying its sources of income away from traditional interest-rate-driven businesses, with some banks aiming to generate 20% of revenues in non-interest-rate-sensitive operations. Although the supermarket banking model has fallen into disfavor, a wealth management operation can constitute a core diversification, since it makes client relationships "stickier," with opportunities for cross-selling between traditional commercial and retail banking and wealth management units.

Many independent wealth managers have also been reviewing the post-crisis landscape and mulling whether the industry can continue sustaining thousands of players, particularly those with subscale operations that face more costly and

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Berkshire Capital Securities LLC is a privately-owned investment bank that provides merger, acquisition, valuation and strategic advisory services to clients focused in the investment management and securities industries. Since 1983, Berkshire Capital has completed almost 240 transactions (with AUM transfer of over $450 billion and an aggregate value of over $10 billion) and over 200 valuations, strategic reviews and fairness opinions.

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time-consuming compliance and regulatory rules — and more demands from clients. As Boston Consulting Group notes in a recent report on the global wealth industry: "The industry is being pulled in opposite directions. Revenues and profitability are sliding at a time when clients want more intensive service. As a result, wealth managers will have to do more with less."

By wrapping themselves into a bank's operations, independent owners can gain easy access to new clients and avail themselves of the benefits of a range of corporate services, including technology, legal, human resources and marketing, as well as new sources of in-house financial expertise that can be of help to wealthy clients. In the post-Madoff world, the link to a brand name bank can also add the cachet required to ease client concerns. This reassessment by independent firms is coinciding with more generalized succession and estate planning issues that are creeping up on baby boom owners throughout the asset management industry.

At the moment, players on both sides are largely in the courting stage, with several deals expected to consummate this year and momentum likely to pick up in 2011-12. For many banks in the early stages of recovery, a drag on acquisitions this year involves the tight scrutiny they face from regulators. Weaker banks are being forced to rebuild capital ratios and stronger ones are under pressure to stay focused on their core business. Where possible, the winners in the banking industry are being prodded to use available capital to purchase their weaker competitors, as opposed to enhancing secondary businesses like wealth management through acquisitions. In this environment, the sort of "non-material" purchase of a small, independent wealth manager that might be overlooked in normal times may be frowned upon by regulators.

The deals that do take place invariably involve three goals: geographic expansion; the addition of a particular capability; or the kickoff of a wealth management operation built around a target. For example, the acquisition last September by Chicago-based **Harris Financial Corp.** of Arizona's **Stoker Ostler Wealth Advisors** helped expand the reach of **Harris Private Bank** in a key growth market where it has been operating for 34 years. For Stoker Ostler, the decision involved scale and fit. In a video posted on the company's Website, co-founder and managing partner Phil Stoker touts Harris as a large, established institution, "and that, combined with their resources, their open architecture, was attractive to us and, frankly, to our clients." In a clear nod to the concerns of those clients, the video employs key buzz words in describing Harris such as "sound" and "stable," while emphasizing the bank's commitment to service. Harris is part of Toronto-based **BMO Financial Group**.

Through its subsidiary, **GenSpring Family Offices** of Florida, **SunTrust Banks** also expanded its wealth management business last year via acquisition. In this case, the target — multi-family office **Epic Advisors** — provided the benefit of geography and improved capabilities. Based in Denver, Epic serves clients in 11 Western states, a part of the country where GenSpring had a limited footprint. In addition, Epic offered bill-paying capabilities that GenSpring can extend to its entire portfolio of offices. In explaining the benefit for smaller firms in tying up with GenSpring, senior partner John Elmes told *Financial Advisor*: "Multifamily offices today — their assets are declining but their expenses are staying the same unless they reduce their staff. A lot of them [have] not. That means expenses as a percentage of assets have gone up and that helps us [pitch GenSpring as a buyer]. Our advantage is that we've created a resource center that allows them to create scale."

Bryn Mawr Bank Corp.'s acquisition of **Lau Associates** in 2008 is an example of how small regional banks are building wealth management capabilities via acquisition. In Bryn Mawr's case, this deal met two strategic requirements: expanding Bryn Mawr's footprint beyond its base in the Philadelphia area to Lau's Delaware home; and bolstering its assets under management by one-quarter, in line with its aggressive plan to more than double AUM over a five-year period to $5 billion. "The acquisition was a significant step in our strategic plan to grow our wealth management services," the company said in its 2008 annual report. Subsequently, Bryn Mawr set up a trust company in Delaware. Another publicly traded Pennsylvania bank, **Susquehanna Bancshares**, bought two local wealth managers in 2007-08 (**Widmann, Siff & Co.** and **Stratton Holding Co.**) as part of a strategy "to diversify our company's revenues, in addition to benefiting customers."

As executives at banks of all sizes and ambitions review potential targets, they need to bear in mind a number of considerations:

- **Strategic and Cultural Fit.** Are you selecting the appropriate wealth management firm for your bank? This involves a review of such areas as corporate culture, clientele and capabilities to ensure the target complements your business. It also involves developing a relationship with a target prior to any union.
- **Structure.** Are you structuring the transaction properly? What is your expected rate of return? These questions involve considerations such equity, compensation and long-term incentives for management at the targeted firm, as well as post-acquisition management responsibility and autonomy.
- **Cost.** Does the deal make sense financially? Ensure an appropriate analysis of investment and return, including a model that incorporates a realistic appraisal of the target's prospects, the likely synergies, and how those synergies will benefit both firms.
- **Planning.** How do we proceed after the deal? Develop a post-transaction plan that your management and the target can both embrace, thereby ensuring a successful merger and business.