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RIA M&A Defies the Odds in 2020

Bouncing back from COVID, another blockbuster year

RIA M&A activity rocketed higher in the second half of 2020, racking up another record year in the process. The 159 transactions established the seventh consecutive year of record activity, as the industry rebounded from (or perhaps reacted to) a global crisis. The number of transactions is 20% higher than the prior year's 132 deals, but that number obscures the recent momentum.

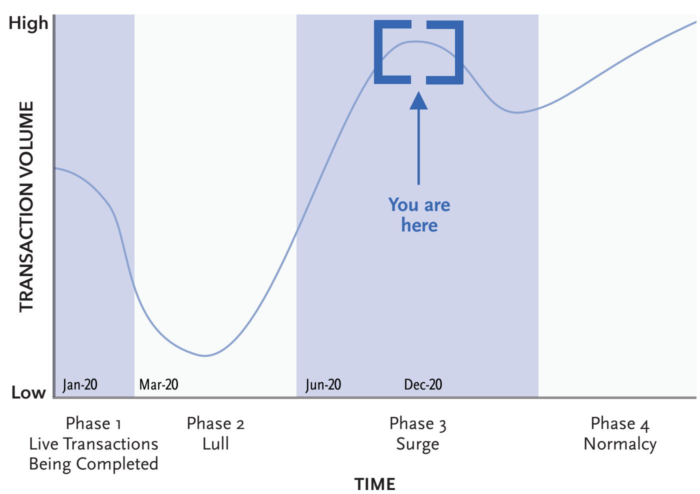
Additional results are being written into the record books: The 48 transactions posted in Q4 create a new high-water mark for quarterly volume. This milestone comes on the heels of the Q3 record of 44 transactions, when the industry crossed 40 transactions in a quarter for the first time. And with 92 transactions, the activity in this six-month period is well above any two quarters in the industry.

This six-month spike is the anticipated result of COVID's impact on RIA M&A. The industry is in the midst of the *Surge*, the third of four stages of M&A activity following the start of the pandemic as outlined in the Q1 2020 Deal Book. We anticipate the *Surge* will likely evolve and continue into early 2021.

To date, the arc of the four phases has largely occurred as expected. Despite the significant impact of the pandemic, the wealth management industry bounced back quickly and has been an area of strength in the U.S. economy. After a compressed *Lull*, RIA M&A has been experiencing an accelerating *Surge*, month after month and quarter after quarter.

The surge in activity has largely been driven by professionally managed firms with over $1B in AUM. DeVoe & Company expects a steady increase of small and mid-sized firms to sell externally over the next several quarters, which will extend the surge. Following a clearing of delayed sales during the *Lull* period and a stimulus of external sales stimulated by the implications of COVID, a new normal trajectory will emerge.

Four Phases of Post-COVID RIA M&A

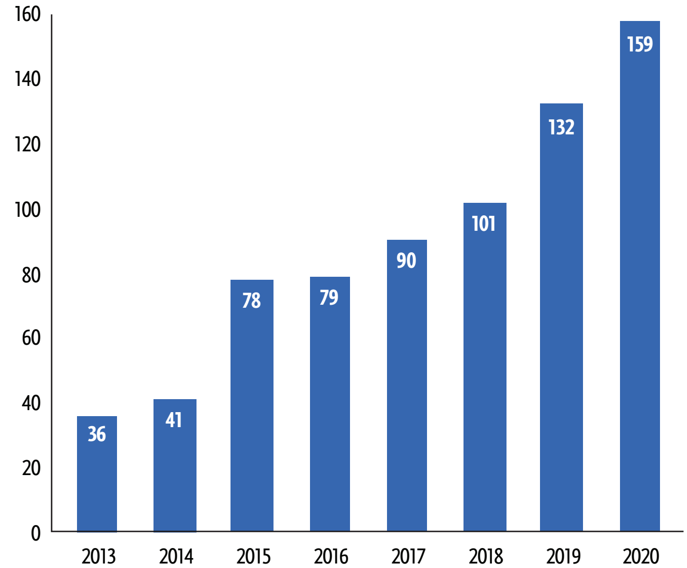


Investments are not FDIC-insured, nor are they deposits of or guaranteed by a bank or any other entity, so they may lose value.

Putting it in perspective, activity was up nearly 60% from just two years ago and was four times the number of transactions in 2014. These are big jumps. This extreme amount of activity is beginning to test the limits of 'healthy M&A.' As DeVoe & Company discussed in the Q1 2020 RIA Deal Book, healthy M&A occurs within a zone of equilibrium between seller interest and buyer capacity (the industry catchphrase of 20 buyers for every seller is and has been a gross misrepresentation and flawed concept). During the last several months, acquirers have been at full capacity; their M&A executives are working around the clock. The strain is prompting them to be more selective and even step away from certain opportunities. RIA M&A remains healthy, but we have entered a red zone of potential disequilibrium.

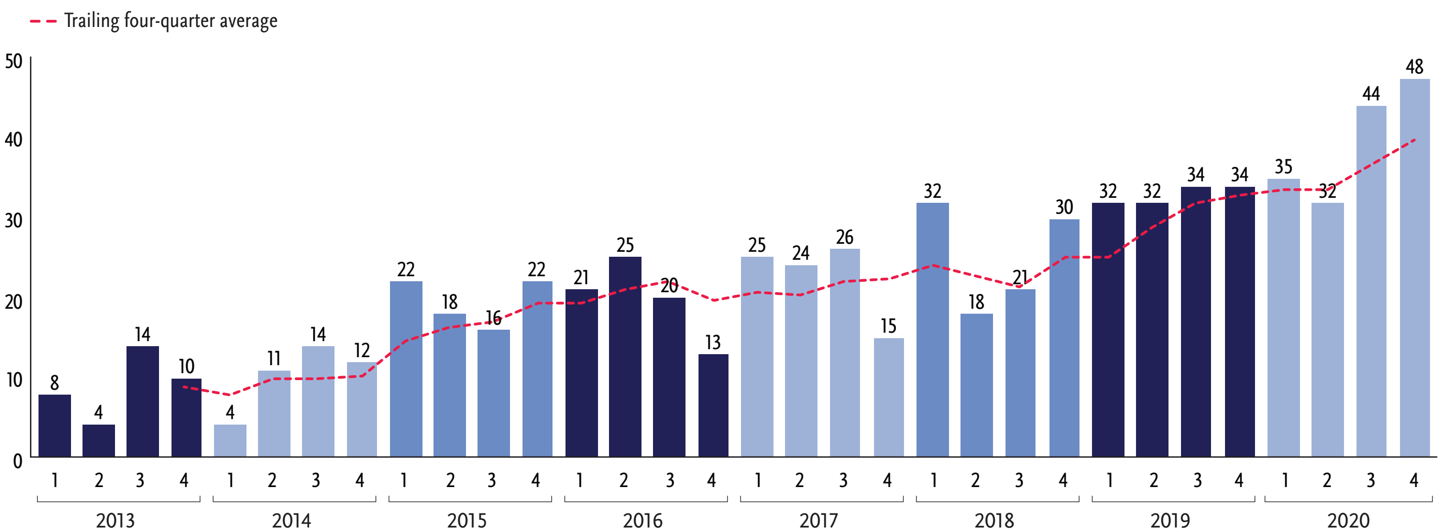
M&A Activity Sets Record for 7th Year in Row

Annual M&A activity



Giant Last Quarter of 2020 Caps the Year

Number of transactions executed per quarter



The Rise of the *META-Firm*

A newly defined category of RIAs has become a dominant force in RIA M&A. DeVoe & Company recently coined the term *META-Firms* to describe a group of companies that will shape the wealth management industry over the next decade. The majority of these roughly two dozen wealth management organizations have M&A as a core plank in their business strategy and have become leading acquirers.

META-Firms are a small number of large RIAs that share a unique set of characteristics:

- **Scale:** They are large — all have over $10B in AUM and several have over $100B.
- **Resources:** Their massive scale enhances their value proposition, and their high profits provide them with capital to make aggressive, strategic investments; many are backed by private equity, providing nearly limitless incremental capital.
- **Management:** They are run by sophisticated management teams who understand this industry, and have boards of seasoned executives who can contribute perspectives and winning strategies from other industries.
- **Conviction:** They are committed to enhancing their positions of leadership in the space and willing to make bold moves.

We borrowed the acronym META from the online gaming community, which stands for the *Most Effective Tactics Available* to win the game. The word "meta" itself also fits the description: The Greek prefix *meta-* includes words such as "beyond," "transcending" and "changed/altered." *META-Firms* passionately seek to win the wealth management game and will often do so by changing longstanding rules; they have both the desire and resources to implement game-changing strategies.

M Most
E Effective
T Tactics
A Available

How will all these abstract descriptions play out in the real world? These firms will grow faster, operate more efficiently and — dare we say it — serve clients better than non-*META-Firms*. A few examples help demonstrate how these firms are changing the game:

The creation of Edelman Financial Engines (EFE) itself is an example of the power of *META-Firms*. Private equity architected and financed the creation of the industry's largest RIA. This megamerger of two leading firms yielded multiple strategic benefits. The most evident is Edelman's national footprint of advisors now serving the individual needs of executives at the hundreds of corporations using Financial Engines' retirement plan services.

EFE's and Wealth Enhancement Group's uses of technology to grow faster are also examples of *META-Firm* activity. The companies' use of data mining, marketing infrastructure, digital message mapping and personalized experiences creates powerful engines of growth. The results speak for themselves: EFE generated 200,000 prospects in 2020.

Mercer Advisors' approach to client service is yet another example. Tearing pages from the playbooks of leaders like Disney, McDonald's and the Ritz Carlton, they are creating consistent, optimal client experiences across their platform of 47 offices. The result is arguably the most scalable, repeatable and institutionalized client experience in the industry.

Many *META-Firms* also are also key players in RIA M&A. Focus Financial Partners, Hightower, CAPTRUST, Creative Planning and many other *META-Firms* are growing aggressively through acquisition and improving their organizations in the process. Their differentiated business models and unrivaled scale make them attractive buyers. Given their momentum and characteristics, *META-Firms* acquired over half of the sellers in 2020. Their share will likely increase over the next several years.

The Importance of Culture in M&A

With valuations at record highs and acquirers getting better at accelerating seller decisions, it is important to keep culture at the forefront of an evaluation process. Merging a company into another is also blending people, norms and values. "It's beyond the analogy of getting married," Matt Cooper, President, Beacon Pointe Advisors, recently stated. "It's more like you are blending families that include four kids, two dogs and a cat."

Given its importance, culture was a recurring theme at DeVoe & Company's recent M&A+ Succession Summit. In the midst of technical discussions on valuation, deal structure and capital solutions, the topic of culture permeated nearly every session.

"A transaction is a little bit like Hotel California," said Bob Oros, CEO, Hightower. Given the implied reality that 'you can never leave,' parties should ensure that the organizations will merge harmoniously. "Culture and fit are critical determinants of whether a transaction is going to be successful," he concluded.

As a seller assesses a buyer's fit on investment philosophy and client service model, they should keep an antenna tuned to cultural cues. Of course, it's critical to immerse in the details of valuation and deal structure. But at the same time, sellers can maintain an anchored focus on company culture.

Some firms are taking an increasingly proactive approach when it comes to these softer elements. "We screen folks out from a cultural alignment perspective first," said Adam Birenbaum, Chairman and CEO, Buckingham Wealth Partners. He and others noted that the softer elements of a transaction (i.e., culture, mission and strategy) should become more balanced with or even eclipse the economics.

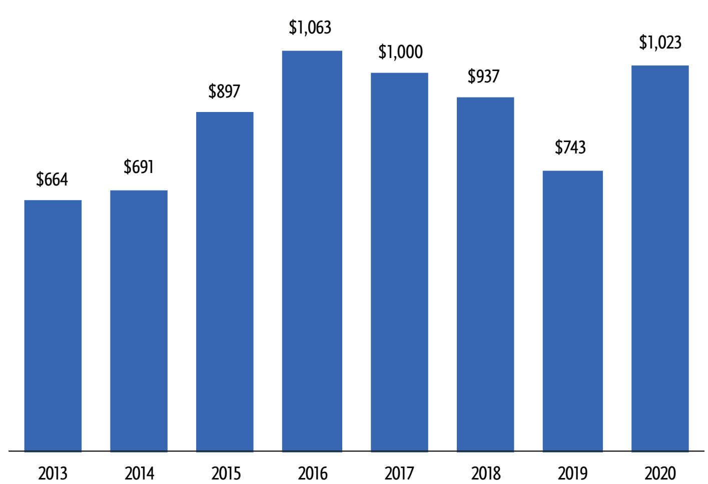
The decision to merge firms is not just a business decision; it's a life decision. One is embarking on a journey where people will spend 40+ hours a week for (ideally) the remainder of their career. The economics are critical, but culture will ultimately be a more important factor for a successful long-term outcome.

Large Firm Sales Drive Up Average AUM

Following a steadily down-sloping line for the last three years, the average size of sellers shot back up to $1B. The 2020 average of $1.02B is nearly 40% above the 2019 average of $743MM. (DeVoe & Company's calculation of average sellers methodology excludes sellers greater than $5B in AUM to eliminate the impact of outliers and maintain statistical consistency.)

Spike in Average AUM of Sellers

Average AUM of sellers – in $MM (over $100MM and less than $5B)



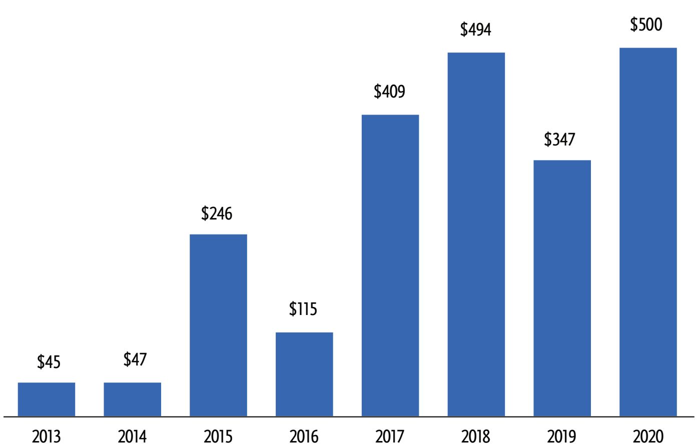
The spike in deal size — an unprecedented increase of $300MM from the previous year — was driven by the post-COVID surge of $1B+ transactions. In 2020, 46 RIAs in the $1B to $5B range sold, nearly doubling the 25 of the previous year. Meanwhile, smaller transactions were flat, at 70 transactions each year. Historically, the number of smaller sellers has increased year over year.

During the initial months of COVID, larger firms with full-time executives who were fully dedicated to running the business were able to continue executing strategic initiatives — including M&A. By contrast, smaller firms whose leaders also oversee client relationships had to focus on what was most important: serving clients. Consequently, their M&A activities were slowed by COVID, during a period when larger firms took M&A action because of COVID.

The combination of record numbers and larger average seller size led the industry to the highest total AUM transacted in a single year. The $499.6B in 2020 AUM was a 44% increase above 2019's $347B and just eclipsed the prior all-time high set in 2018.

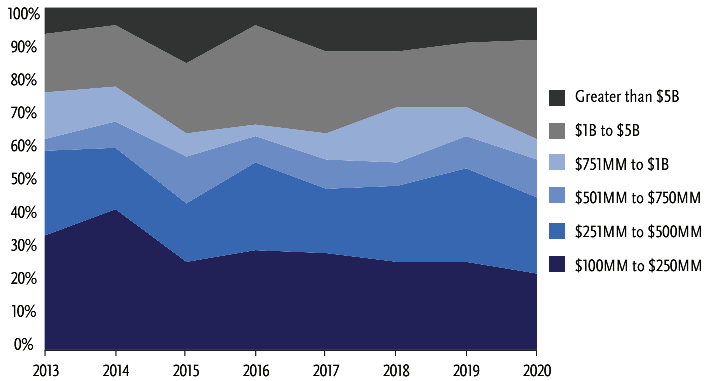
Highest Ever Annual AUM Transaction Volume

Total assets transacted by year (in $B)



Increase in Larger Transactions

Annual transactions by seller size as a percentage of total transactions



(Nearly) All Boats Rose with the M&A Tidal Wave

All buyer categories increased their number of transactions in 2020 vs 2019, with the negligible exception of *Banks*. Overall, there were few significant shifts in market share. Aside from a bump in activity among the *Other* category players, all other buyer categories moved just a few percentage points in one direction or another.

Consolidators executed 42% of transactions, a slight decrease from their 43% share in 2019. *Consolidators* offer attractive options for sellers seeking scale. Their diverse business models provide RIAs with a wide array of options. This relatively small group of acquirers executed the lion's share of transactions — and, consequently, most of the firms in the Top Acquirers list are *Consolidators* (see next page).

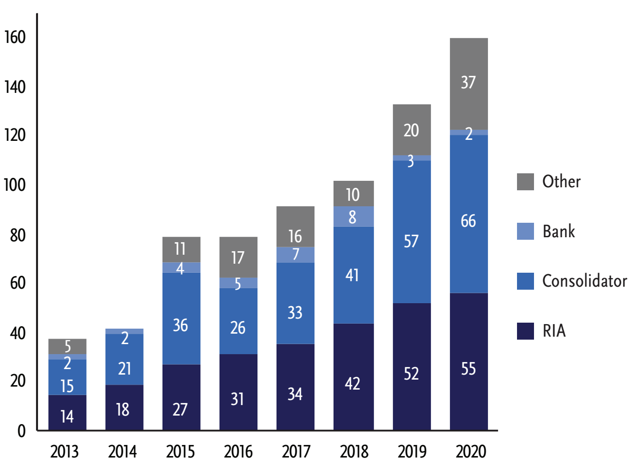
RIAs as a buyer category executed more transactions in 2020 than 2019, but their slower pace yielded a smaller market share. They dipped from 39% in 2019 to 35% in 2020. We anticipate a potential uptick next year if smaller and mid-sized firms come to market in greater numbers.

The *Other* category — which is comprised of buyers that are not *RIAs, Consolidators* or *Banks* — significantly increased its share from 15% last year to 23% this year. Private equity (PE) was particularly active and made headlines with high-profile deals. A total of eight PE investments were made, including GTCR's investment in CAPTRUST, General Atlantic's investment in Creative Planning, Abry Partners' investment in Beacon Pointe, Lightyear Capital's investment in Allworth Financial, and Berkshire Partners' investment in EP Wealth. (DeVoe & Company was honored to be involved in several PE transactions in 2020.) With a slew of international transactions from CI Financial (see right), an increase in revenue share model financing and non-traditional activity, the *Other* category nearly doubled its volume.

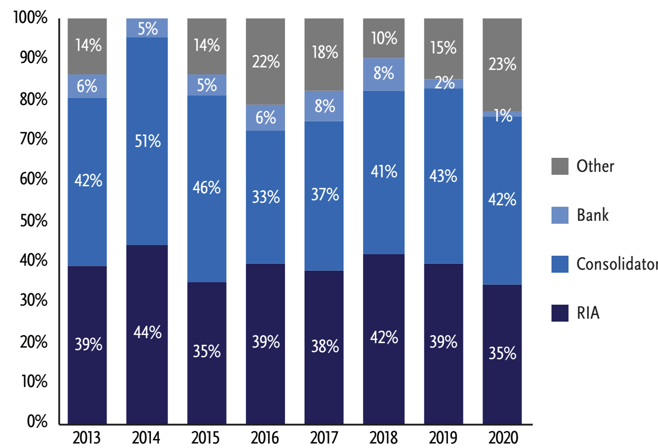
With only two transactions, *Banks* have a minimal presence in the industry during the year.

Consolidators Top Buyer Categories; *Other* Makes Inroads

Number of acquisitions by buyer category



Percentage of acquisitions by buyer category



Top 12 Acquirers Absorb Over 40% of Annual Transactions

Top 12 acquirers of 2020

Firm	Number of transactions
CI Financial	8
Hightower Advisors	8
Creative Planning	8
Mercer Advisors	7
Buckingham Wealth Partners	5
EP Wealth	5
CAPTRUST	5
Wealth Enhancement Group	5
Emigrant Partners	4
Allworth Financial	4
MAI Capital Management	4
Cerity Partners	4

Last year at this time, we wrote a section titled *The Canadians Are Coming*. Well, they came, alright. Specifically, CI Financial emerged as the standard-bearer and arrived with conviction. Executing eight transactions during 2020 (in addition to two more in late 2019), Toronto-based CI jumped to the top of the Top 12 Acquirers list, sharing the spot with Hightower and Creative Planning.

Hightower demonstrated its ability to integrate multiple billion-dollar firms in a year. Among the firm's eight acquisitions were those of Stearns Financial ($1.3B) — a DeVoe & Company client — and Osborn Williams & Donohue ($1.4B). Creative Planning showed its scope with acquisitions ranging in size from $126MM to $1.7B in AUM, and in locations from Georgia to Texas to the Midwest.

Sub-Acquisitions Accelerate

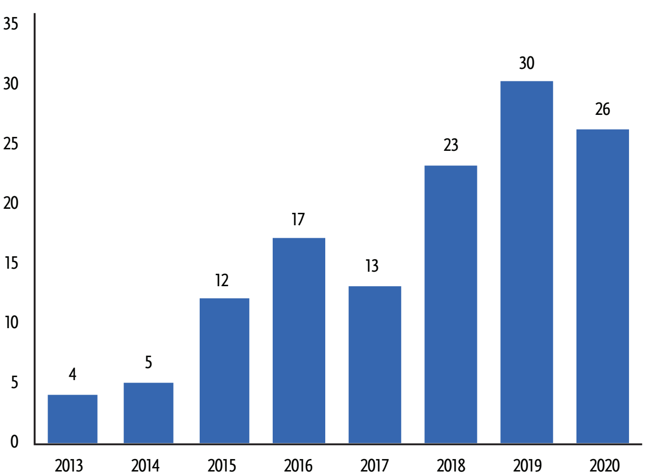
The last quarter of 2020 was an all-time high for sub-acquisitions. Sub-acquisitions — acquisitions made by firms that have themselves been acquired — increased to 12 during the period, nearly double the quarterly average of the last two years.

Despite the strong finish, this type of acquisition dipped slightly in 2020. The 26 transactions in 2020 hit a midpoint between the peak of 30 in 2019 and 23 in 2018.

The surge in recent activity is part of the broader increase of mid-size firm sales that DeVoe & Company anticipates in the near term. A resurgence in sub-acquisitions, potentially exceeding their peak in 2019, is a scenario that may likely play out in 2021. With the average size of sub-acquisitions roughly half of other deals, their increasing number would drag down the overall average seller size.

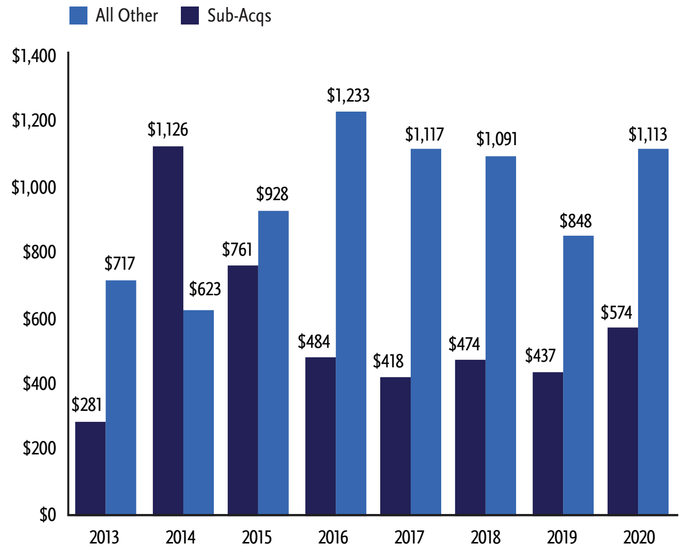
Sub-Acquisitions Dip Slightly, but Accelerate Late in Year

Number of sub-acquisitions by year



Sub-Acquisitions Remain Smaller in Size

Average AUM of sub-acquisitions vs all other transactions in $MM (greater than $100MM, less than $5B)



Looking Forward

Heightened M&A activity to continue: What goes up must come down. At least, that is the old adage. After seven consecutive record years and M&A volume at twice the volume of four years ago, is it now time for the RIA M&A volume to come down?

No.

At least, not according to our analysis. RIA M&A is likely to continue increasing for the foreseeable future. We may see a lull later in 2021 following the recent frenzy. However, we expect that a surge in small and mid-sized deals will more likely contribute to around 45 transactions per quarter for the near term.

DeVoe & Company is less concerned about a lull than an accelerating trajectory. Ideally, 2021 yields fewer than 240 transactions. This volume is in a zone where experienced buyers can increase their staff to meet the supply. Beyond this increase, buyers will likely become strained and more selective about acquisitions, and valuations will likely decrease. The unsettling implication is that some RIAs may leave the dance without their favorite partner — or any partner at all.

Several other key trends that intersect with future M&A activity have emerged from DeVoe & Company's industry analysis:

Organic growth accelerates: 2021 will likely see the silver lining of a crisis for the wealth management industry. RIAs are great at taking care of clients during a crisis. And when the dust settles, happy clients tell their friends, who become new RIA clients.

Divergence in business performance: Crisis and post-crisis periods typically create divergence in business performance. Those firms that managed themselves optimally through COVID and have since proactively focused on growth will start to separate themselves from their peers.

The growing power of *META-Firms*: *META-Firms* are reshaping the top of the RIA ecosystem. The separation between Mega-RIAs (i.e., RIAs with $10B in AUM) and *META-Firms* (the subset of ~25 mega RIAs that have differentiated business strategies) will become increasingly apparent. Over the next few years, the broader industry will evolve more quickly as these organizations grow and have greater influence. Still, we expect smaller and mid-sized firms to continue to exist and thrive.

Succession/demographics: COVID was a shot across the bow for every firm without a clearly defined, written succession plan. As a result, a new wave of succession planning and equity migration is occurring industry wide. And in many cases, principals are determining that an external sale is the optimal path forward. This positive consequence of COVID will help close the industry's succession planning exposure point, while driving incremental M&A activity.

Overall, the structural underpinnings of the RIA industry are solid. The industry not only demonstrated resilience through the global pandemic, but also helped Americans through an unprecedented crisis. The industry is likely to experience accelerated evolution over the next several years as technology, private equity and the growing power of major players shape its future. These emerging trends are more positive than negative and will contribute to a stronger value proposition for U.S. households. After such a challenging 2020, a new year has never been such a welcome change.

Our Methodology and the Focus of the RIA Deal Book™

The DeVoe RIA M&A Deal Book seeks to track and analyze the trends of RIA mergers and acquisitions. Leveraging our founder's experience tracking RIA M&A for over 17 years — longer than anyone in the industry — DeVoe & Company reports on activities and analyzes the trends to bring you deeper insight.

The RIA Deal Book's purview is to focus primarily on the acquisitions and mergers of true RIAs, and only on transactions of $100 million or more in AUM. Our reporting limits our tracking to $100MM+ RIAs to optimize the statistical accuracy of our reporting. We seek to screen out the SEC-registered hedge funds, IBDs, mutual fund companies and other companies that aren't operating as traditional RIA firms. We also exclude the "advisors joining RIAs" category, unless there are important developments.

Our goal is to provide the RIA community with the very best M&A data on the 5,000+ SEC-registered RIAs so that advisors like you can make more informed strategic decisions.

About DeVoe & Company:

DeVoe & Company is a goal-based consulting firm and investment bank focused exclusively on guiding wealth management and investment management companies to a higher level of success. We provide consulting, M&A, and valuation services to help you accelerate the achievement of your business goals. Leveraging our team's 300 years of combined experience in RIA business consulting and management, we develop solutions tailored to your unique goals, needs, and situation.

The wealth and investment management industries are highly dynamic and evolving at a fast pace. DeVoe & Company can help you better understand your options, determine your optimal path, and craft an implementable plan for you to capitalize on the opportunities.

What We Do

Our mission is to help you achieve success on an accelerated basis. Our services fall into three broad categories:

- **Business Consulting**
- **Investment Banking**
- **Valuations**

Who We Are

Founded and led by RIA thought-leader David DeVoe, our team has grown to ten professionals with 300 years of combined experience. Our consulting approach is a reflection of the team's background: An ideal balance of analytically rigorous theory and real world experience. Our team includes a McKinsey-trained management consultant and several former CEOs/COOs of $1B to $10B RIAs. As a result, we are positioned like no other consulting firm to provide you advice on any strategic challenge you may face. Our breadth of experience enables us to be your complete partner.

How We Do It

DeVoe & Company executed more than 500 engagements in the last several years, supporting firms managing $50MM to over $80B in AUM

DeVoe & Company creates transformational change for our clients through a unique, highly focused approach. Most engagements begin with our proprietary strategic planning process: StrategicContext™. During the StrategicContext™ stage we gain a detailed understanding of your business, professional, and personal goals. Through this methodical approach a strategic "North Star" for the engagement emerges. This North Star provides the management team with a consistent point of alignment for the myriad decisions throughout the process. As a result, the outcome will be deeply rooted in the company's core goals and integrated into a cohesive plan.

Our Insights

We regularly publish white papers, are quoted in financial publications and create other thought leadership pieces that we make available on our website at www.devoeandcompany.com.

A few of our most recent articles / white papers include:

- *It's Time for a Human Capital Revolution*
- *DeVoe RIA M&A Outlook Study*
- *Succession Planning: Planning Your Future*
- *Putting Strategic Context Around Your Succession Plan*
- *Tailor-Made Successor*
- *True Value: Learn to Focus on the Things that Drive Up the Value of Your Practice*

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