DEVOE & COMPANY

2021 RIA M&A Starts with a Bang

The Surge continued, driven by mid-sized firms entering the market

RIA M&A clocked another record lap in Q1 and is in position for another record year. On the heels of a record-breaking 2020 — which saw 159 transactions, including 48 in Q4 alone — the industry tallied an unprecedented 58 transactions in the first three months of 2021.

To put the first-quarter transaction volume in perspective, this was the first time RIA M&A crossed the 50-deal milestone in any quarter. And yet, the 40-deal milestone was exceeded for the first time in Q3 2020. It is even more remarkable considering that quarterly volume hovered in the 20s from mid-2015 to 2017 and in the 30s from late 2018 through mid-2020. For perhaps a fleeting moment, the industry's M&A chart actually resembles a hockey stick.

This historic quarter opened with a spike of 33 transactions in January, far outpacing the previous single-month record of 18 transactions exactly a year earlier. January is typically a strong month, but this was far above the norm.

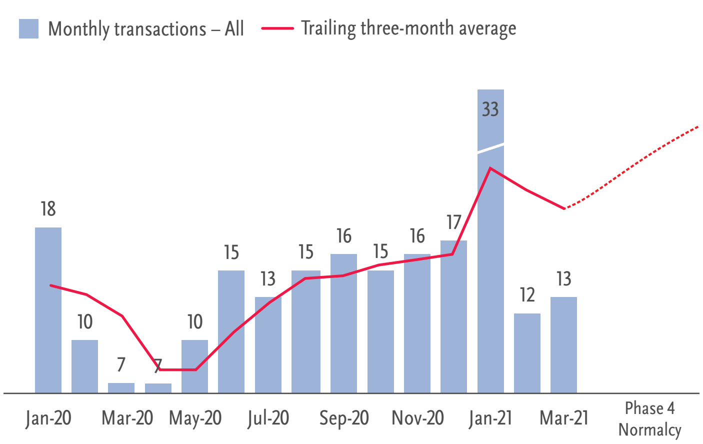
So, the quarter took off like a rocket, but on a month-to-month basis was a mixed bag. The pace cooled rapidly in February and March, with 12 and 13 transactions, respectively. After redlining for eight straight months, the engine was out of gas. The industry had burned through the excess fuel created by the impact of COVID, and RIA M&A has now coasted for two months.

These results indicate that the industry is moving out of the *Surge* — the third of *Four Phases of Post-COVID RIA M&A* DeVoe & Company forecasted in our Q1 2020 Deal Book. The shock of COVID created a lull of activity, before sellers sold in progressively higher numbers through the balance of 2020. The *Surge* crested in January as dozens of sellers raced to close transactions either before the end of 2020 or early 2021 — at least in part to insulate themselves from potential tax increases under the Biden administration. The industry is now catching its breath.

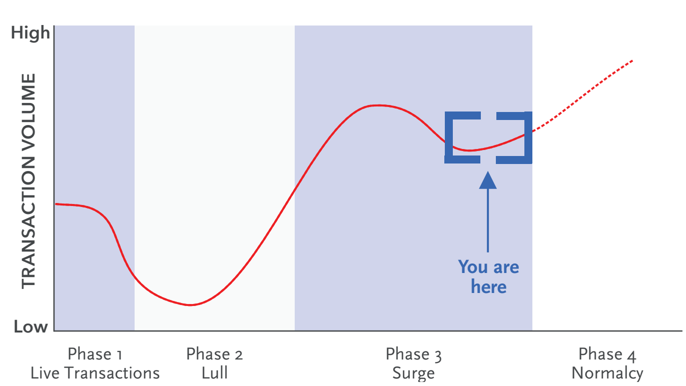
DeVoe & Company anticipates M&A activity will soon recalibrate to the *Normalcy* of Stage 4: a milder, though sustained, upward curve lasting for at least another five to seven years.

12 Months of Activity Follows DeVoe's Forecasted Four Phases of Post-COVID RIA M&A

Actual transactions executed

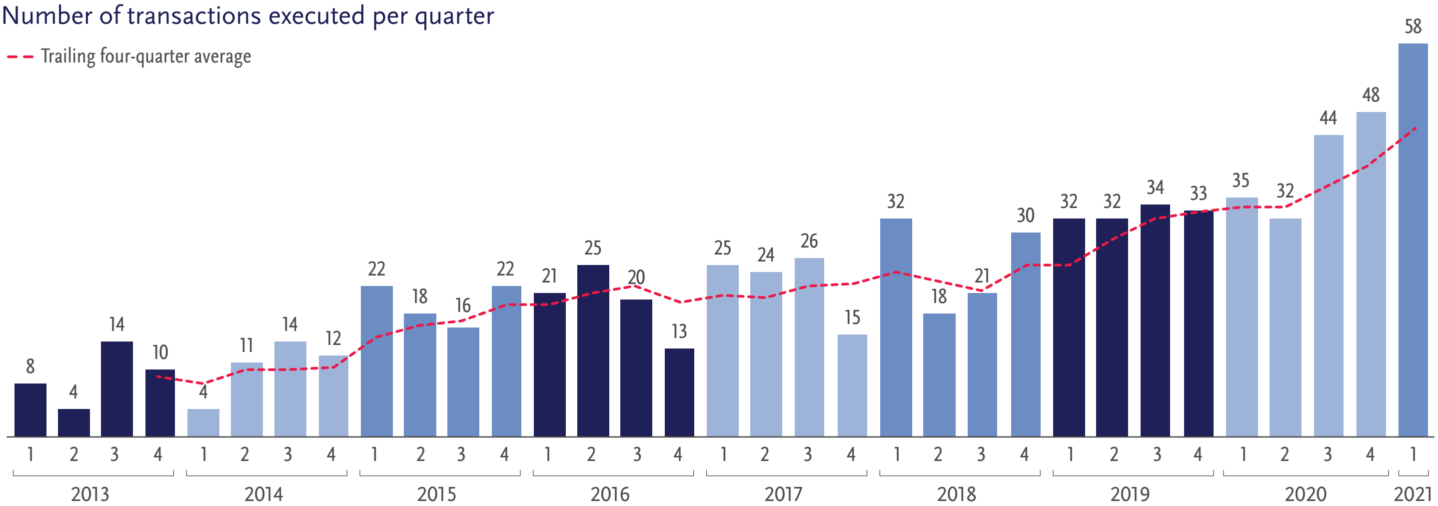


DeVoe Four Phases of Post-COVID RIA M&A



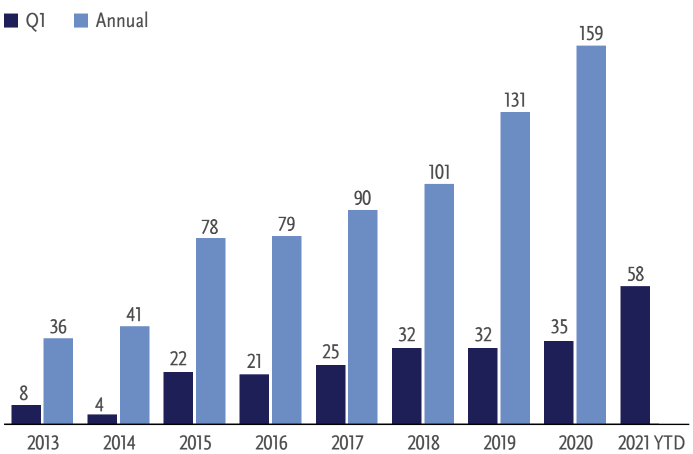
M&A Activity Takes Off in Q1

Number of transactions executed per quarter



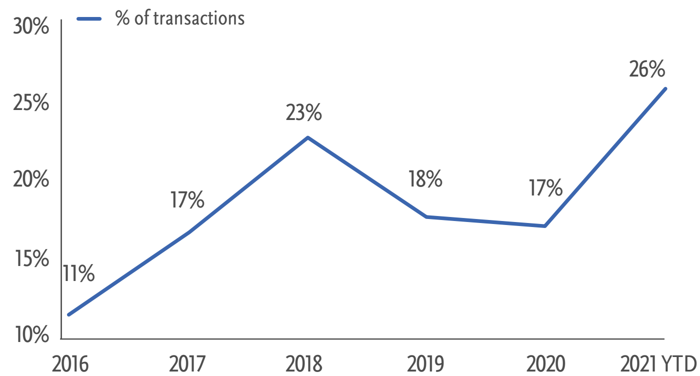
2021 Starts Strong

Annual vs Q1 M&A activity



Uptick in Activity Among Mid-Sized Sellers

Percentage of transactions – $500MM–$1B



Mid-Sized Seller Activity Surges

Mid-sized RIAs joined the M&A party over the last several months and were a primary driver of the extended surge. Selling at twice their usual volume, firms between $500MM to $1B of AUM contributed heavily to the record Q1 and drove the vast majority of the January spike.

In the first quarter, mid-sized sellers shot up to 26% of all transactions — a steep uptick from the 17–18% over the last few years. For comparison, the 15 mid-sized sellers in Q1 2021 were more than double the seven in Q1 2020 and equivalent to all the mid-sized transactions during the entire year of 2017.

The heightened mid-sized seller activity followed a wave of activity by $1B+ RIAs — or a more important distinction, professionally managed organizations. Professionally managed firms did not pause their plans to sell during COVID. Their full-time management teams were able to focus their attention on strategic issues; by definition, these executives do not oversee clients.

By contrast, firms that have yet to put full-time CEOs, COOs and other senior executives in place (i.e., typically firms under $1B in AUM) are run by advisors who split their time between managing client relationships and running the business. So, following the start of the crisis, they spent *all* their time tending to the impact of COVID. And rightly so — they were focused on taking care of clients and staff through this tumultuous period.

Once the COVID dust settled, the leaders of these mid-sized firms were able to shift their focus back to strategic issues, and after the typical six to 10 month M&A gestation period, the new vintage of sellers announced completed transactions, hence, the two waves of seller categories that contributed to a sustained surge.

This domino effect of mega/large/medium/small RIAs selling in sequential waves is not an uncommon occurrence in the industry. After observing this phenomenon in the past, we have concluded that seller psychology likely plays a role. As principals of firms who are contemplating a sale see their larger peers take action to sell, it reinforces the decision and provides proof of concept. With the leaders of their admired colleagues taking action, this can be the tipping point to move forward with conviction.

Although succession planning is a common goal in many transactions, the primary decision driver for mid-sized firms to sell is to gain the benefits of scale. Matt Hall from $687MM Hill Investment Group put it eloquently when he hired DeVoe & Company to explore their options: “We want a launch pad, not a landing pad.” Mid-sized firms are usually seeking a partner to help them achieve a new set of stretch goals, as opposed to an exit. And, firms this size are often in a position to sell only if they find their perfect buyer. If Focus Financial Partners had not created a clear path for Hill to achieve a new level of greatness, Matt and the team would likely still be running a very successful, fully independent firm.

Average AUM of Sellers Holds Steady in Q1

The average AUM of sellers held steady at the $1B level in the first quarter. The Q1 $1.03B average AUM of sellers is on par with the 2020 average ($1.02B), which jumped significantly over 2019’s average of $747MM.

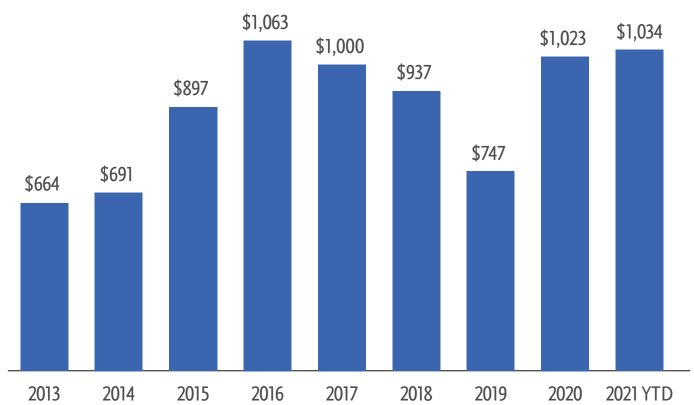
Average AUM remains strong as sellers in the $1B+ category maintained their higher activity levels from 2020. Overall, $1B+ sellers comprised 39% of transactions during the period, compared with 38% in 2020 and 30% in the two prior years. In addition, the number of sellers with $500MM to $1B of AUM nearly doubled vs each of the last two quarters.

At the same time, the share of transactions among firms in the $251MM to $500MM range continued to decline, from 27% in 2019 to 22% in 2020 to a mere 12% in Q1 2021. However, the compression in this segment is likely to be short lived. DeVoe & Company expects the number of sellers in this range to grow over the next several quarters as outlined earlier.

Notably, though, several mega-transactions took place in the quarter. Prominent examples include CI Financial’s acquisition of Segall Bryant & Hamill ($23B), Silicon Valley Bank’s acquisition of Boston Private ($13.3B) and Hightower’s purchase of Bel Air Advisors ($8B). A reminder that these and other mega-deals don’t affect the average seller size, as DeVoe & Company excludes sellers greater than $5B in AUM to eliminate the impact of outliers and maintain statistical consistency.

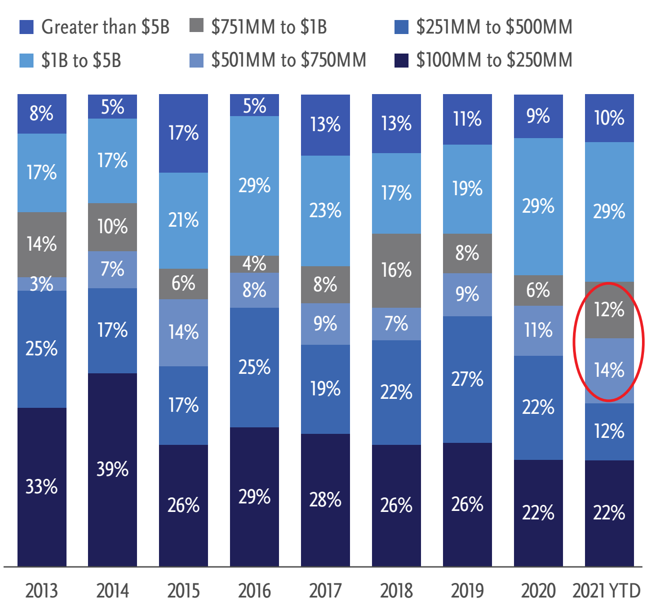
Seller Size Stays High, Reflects Larger Sellers

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



Growth in $500MM to $1B Sellers; $1B+ Stays Strong

Percentage of total transactions by seller AUM



Buyer Categories Remain Consistent

Contrasting sharply with recent swings in M&A transaction volume, buyer categories maintained the relative stability that we have observed for several years in a row.

Consolidators represented 40% of the acquisition volume in Q1, a slight dip from their 42% share for 2020. Their models continue to resonate with advisors seeking to sell, largely because *consolidators* tend to offer a broad spectrum of options with varying characteristics.

Several firms in this category made multiple acquisitions in Q1:

- Mercer Advisors completed a whopping eight transactions
- Focus Financial finished the quarter with three transactions and two sub-acquisitions by its partner firms
- Beacon Pointe also made three acquisitions
- Several other *consolidators* — including Hightower, Wealth Enhancement Group, and CAPTRUST — each made two acquisitions

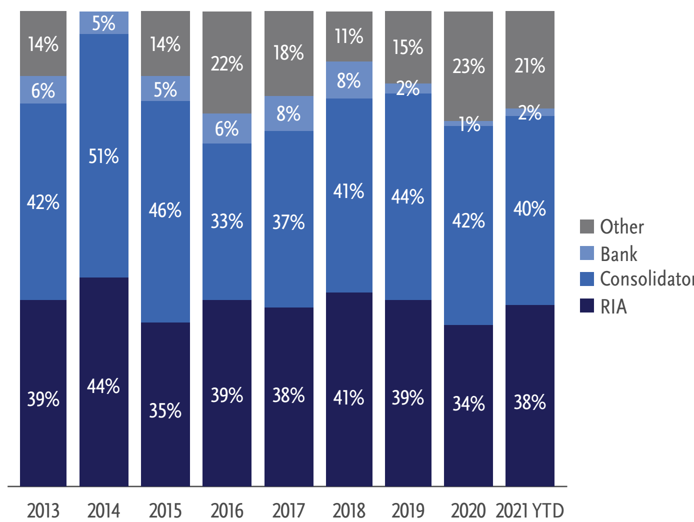
Transactions in the *RIA* buyer category grew slightly, representing 38% of all transactions in the period, compared with 34% in Q4 2020. *RIA* buyers' share of transactions remains above the 2020 full-year average of 35% and is near the historical average of around 40% that we've seen since 2016.

Buyers in the *Other* category — composed of private equity firms, asset managers and other non-RIAs — represented 21% of transactions in the first quarter. This group's activity is down just slightly compared with its 23% share of transactions for all of 2020.

Meanwhile, *Banks* continued to barely register any buying activity, with just one transaction in the quarter, albeit a large one (the aforementioned Silicon Valley Bank acquisition of Boston Private).

RIAs, Consolidators Still Active in Buyer Ranks

Percentage of acquisitions by buyer category



Newsflash: More Sellers Than Buyers in the RIA Marketplace

Clearly, it is a great time to be a seller. With a strong pool of buyers, high valuations and a favorable economic growth environment, conditions for sellers probably could not be better.

However, it is also a great time to be a buyer. By many metrics, there has never been a better time to be a buyer of RIAs.

That might seem like a bold statement, when many observers wax on about a *seller's market* and state misleading statistics like "50 buyers to every seller." But the facts make a strong case that adding inorganic growth to your strategic plans could be a sound decision.

At no point in history have RIA principals been so willing to sell their firms. The record number of external sales represents empirical evidence and should be music to any aspirational buyer's ears. Similarly, the openness among principals to meet with buyers and explore the concept of selling their firm has never been so high. The anecdotal evidence is clearly apparent in DeVoe & Company's buy-side engagements. In parallel, we have experienced a steady uptick in sell-side engagements, as more advisors proactively engage with finding their very best partner.

Overall, during the last five years the industry has made a psychological shift: RIA principals have steadily moved toward giving up degrees of control and ownership in exchange for the benefits of scale. They are willing to give up certain decisions, and equity, to focus more energy on what they enjoy doing most.

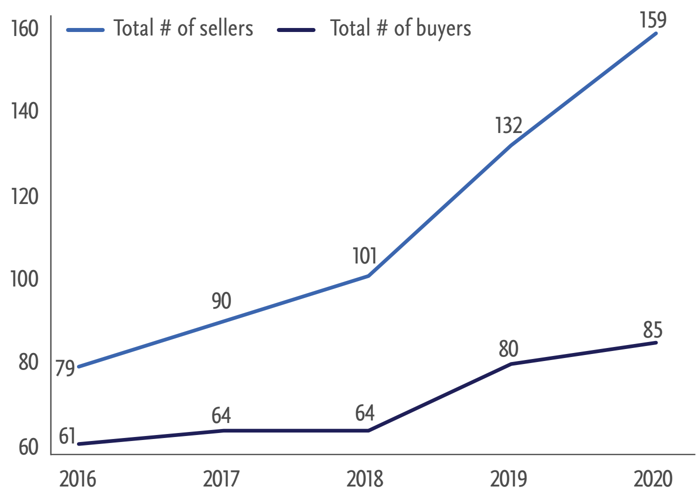
Perhaps the most compelling data is the evolving ratio between actual buyers and sellers over time. During the last five years, the number of sellers has doubled (159 in 2020 compared with 79 in 2016), while the number of active buyers has ticked up only 40% (from 61 in 2016 to 85 in 2020). Successful buyers have consequently benefited from a greater selection of potential targets and been in a position to execute more deals.

Buyers have not hesitated to execute more deals. Four years ago, for every buyer that closed a deal, there were 1.3 sellers that did the same. Today, that ratio has expanded to two sellers for every one buyer. You read that correctly: The average successful buyer in today's marketplace is closing two deals a year.

As a result, active buyers are having watershed years. Some are even executing seven or eight transactions in a year. And this pool of heavily active buyers is increasing. In 2020, 14 firms each acquired four or more RIAs — compared with seven acquirers meeting that rate in 2019, and only two acquirers doing so in 2016.

Sellers Growing Faster Than Buyers

Total number of sellers vs buyers 2016–2020



So, the ratio of buyers to sellers in the RIA marketplace is actually 1:2. Not 50:1. (The 50:1 ratio is actually an impossibility based on the size and composition of the RIA industry; 160 sellers times 50 is 8,000 buyers — there are only roughly 5,000 total firms over $100MM.)

Even if there were 50 *aspirational buyers* per seller, wanting to buy another firm is not the same as being a qualified buyer that is truly prepared and committed to going on the arduous journey of closing a deal.

Conclusion

After a roller coaster 2020, the new year started with a bang. We believe the January peak of M&A activity and the following compression in February and March mark the completion of the third phase of the post-COVID RIA M&A lifecycle. Just over a year after the pandemic began, we are now moving into the *new normal* of RIA M&A activity — timing that seems to coincide with the glimmer of a *new normal* for parts of daily life as well.

The softened activity of February and March is unlikely to be sustained through the year. The continued high valuations, attractive value propositions of strong acquirers, and heightened propensity of RIAs to sell externally set the stage for another strong year. We expect that the mid-sized and smaller firms will sell in greater numbers over the next several quarters and contribute to what will likely be another record level of activity for 2021.

The *new normal* of RIA M&A activity is anticipated to bend upward over time and continue to be strong for another five to seven years. The owner demographics, continued lack of succession planning and a continually increasing interest in joining forces with bigger players will yield a steadily increasing stream of sellers.

Valuations for sellers will also expand in range, as RIAs experience a divergence of performance. Those firms that reacted quickly to the pandemic and even flourished through the last year will command high valuations, while those that struggled through this challenging time may find their offers disappointing.

A small group of leading buyers will continue to acquire multiple firms per year (and likely pay the highest valuations). 2021 may be the first year that some of these *Consolidators* consolidate — and merge into one another. And the META-RIAs will continue to separate from the rest of the pack across many dimensions.

However, the industry may see more traditional RIA buyers enter the space, such as the 'RIA next door' acquiring its neighbors. The psychological comfort of *selling to one of us* — a buyer run by advisors — has always garnered strong interest in the industry. And today, many sellers are increasingly curious about exploring options beyond the mega firms.

Ideally, 2021 yields 200 or so transactions. For this to happen, the post-COVID breather of February/March would be short lived, and the numbers would creep back toward 15–20 transactions per month. The industry just has too many future sellers embedded in its ranks to have M&A burn at a slow rate.

Each month/quarter/year the transaction volume is low simply increases the supply of future sellers that have to eventually come into the market. Scenarios where too many sellers hit the market at once have unsettling implications. A *healthy but not extreme* continued acceleration of transactions will help ensure the industry itself remains healthy.

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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