Industry Update on M&A: Why Buy? Tips for Those with Their Sights Set on Becoming an Acquirer

A conversation with Louis Diamond.

Mindy Diamond:

Welcome to the latest episode of our podcast series for financial advisors. Today's episode is an Industry Update on M&A: Why Buy? Tips for Those with Their Sights Set on Becoming an Acquirer. It's a conversation with my partner, Louis Diamond. I'm Mindy Diamond, and this is Mindy Diamond on Independence.

Mindy Diamond:

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Mindy Diamond:

For Apple Podcast users, I'd be grateful if you'd give the show a review. Your input helps us to make the series better and alerts other advisors like you who may find the content to be relevant. And while you're at it, if you know others who are considering change or simply looking to learn more about the industry landscape, please feel free to share this episode or the series widely.

Mindy Diamond:

M&A has been one of the hottest topics in the wealth management industry in recent years. And even despite choppy markets and rising interest rates, independent firms are getting high watermark valuations and deals are closing at record levels. So what's driving all this activity? Why are independent business owners so eager to sell what they worked long and hard to build and nurture?

Mindy Diamond:

What's the attraction for buyers? And how can a nascent firm or wirehouse advisor, planning for their next chapter, set themselves up to be a successful acquirer? We talked in previous episodes about being on the seller's side. In this episode, we turn the tables for the buy side perspective. Because the truth of the matter is that there's an imbalance in the industry between those who want to sell and those who want to buy.

Mindy Diamond:

There's an incredible appetite amongst buyers and not nearly enough sellers to meet the demand. So to become a credible and attractive acquirer amongst some hefty competition, you need to possess certain attributes, which we will definitely get into. I've asked Louis to join me in answering these questions and more. There's tons to discuss, so let's get to it. Louis, as always, thank you so much for joining me.

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Louis Diamond:

Absolutely. Excited to talk about our topic today.

Mindy Diamond:

You bet. So let's start with level-setting first and foremost before we dive in. What is the current M&A environment in the independent space?

Louis Diamond:

So not surprisingly, it remains a really, really fertile market even with the rising interest rates and the market turbulence. There's more demand than ever before from private equity-backed acquirers, private equity firms in general. And overall, it's still a fractured industry, so still a lot of room to run as far as the number of M&A transactions.

Louis Diamond:

If you look at any industry report, whether through Fidelity or Echelon Partners or DEVO, all of them put out various reports. Seems like every quarter there's a new record being notched as far as number of transactions. And just looking at the median size deals that keeps ticking up. So it's a very active market, with there being a ton of dry powder in the market and a lot of folks looking to do deals and still a lot of folks looking to sell even in spite of the market gyrations.

Mindy Diamond:

And so on the other side of the table, why are independent business owners anxious to sell?

Louis Diamond:

It's probably four or five different things. I think the first one is we've seen a massive run-up in valuations. So the multiples that acquirers are putting on businesses has never been greater. The last couple of years we've probably seen a 30% to 40%, maybe even higher, increase in valuation multiples. And that's because of this imbalance with supply and demand.

Louis Diamond:

The demand for a quality practice, far outweighs the amount of supply. So we're seeing a number of firms come to market because of FOMO, the fear of missing out, wanting to sell their house top of market, seeing what friends have sold for and wanting to make sure they get a piece of the action.

Louis Diamond:

So that's definitely part of it is, opportunistically, looking at the market conditions and thinking it's a good time to sell. Another reason is as the valuation multiples have gone up; it's become prohibitively expensive for next-generation advisors to buy into practices. So more times than not, a firm will want to do an internal succession plan, meaning selling to loyal employees and next-generation folks.

Louis Diamond:

It's easier, it's more seamless and you get to reward those who have helped you build the business over the years. But with the market environment right now, it's become so expensive for these folks to buy into the practice that either the buyer needs to take a ton of debt and really put their financial future in jeopardy, or the seller, meaning the retiring advisor, has to take a big discount with fair market value.

Louis Diamond:

So more times than not, then even if there is a strong next generation, we're seeing it that a business has to be taken to market and to be sold externally or to at least bring in an outside capital source to finance or take a piece of the equity. A third reason is succession. Nothing new here. Advisors looking for succession plans, not being enough younger folks in the business. And usually, a succession event is one of the primary motivations someone has to sell.

Louis Diamond:

And I'll give you just two more real quick. Many firms lack scale, especially as some of these larger firms keep getting larger and larger. The resources and capabilities they have keeps getting better. And firms have to decide whether to reinvest in the business, hire a bunch of folks, build new capabilities et cetera, improve technology. Or do they decide to sell?

Louis Diamond:

And by selling or merging, they can gain some pretty quick scale. And there's some other ones: not wanting to run the business anymore, being burnt out of running it and wanting to hand over those responsibilities to someone else. And maybe even the desire to add on new services: estate planning, or trust services or family office services.

Mindy Diamond:

There's a lot to unpack there. But two questions come to mind: one, is you're talking about the multiples being at high watermarks. Do we expect them to continue?

Louis Diamond:

We don't have the crystal ball, and we're not valuation experts. From what we've seen, it seems like the multiples have stayed relatively consistent, and there isn't really an expectation that they're going to keep going up at the same level that they were before. But I think it is interesting that they've kind of normalized and stayed consistent.

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And I think, especially for higher quality firms, so meaning ones that are larger, can grow organically, have a strong next generation et cetera, there's going to continue to be a lot of demand for those firms. And as we'll get into, there's a lot more buyers than sellers for those types of businesses.

Louis Diamond:

So I think as long as there continues to be all this interest in buying quality businesses, I think there is some potential room to run. But we did see, similar to the housing market, that valuations kept going up and up and up. But now, with the rising interest rates, and some of the stuff that's going on in the stock market, I don't think anyone's expecting them to keep rising at the same level. But also, no one's expecting the market to crater either.

Mindy Diamond:

Well, that's good stuff for sellers, for sure. But the other question is just the other day, I talked to the owner of a billion-dollar firm. And he said he's growing at 30% per year, they're crushing it, loves what he does. Built a successful RIA firm after having come from a traditional brokerage firm many years ago.

Mindy Diamond:

And while he talked about the fact that it is very frustrating that he's unable to add staff and hence, he has a capacity issue, he's really committed to hiring and growing as opposed to selling or merging. And so while there are plenty of sellers that have FOMO and want in on this sort of hoopla of a market, there are many who really want to retain full control. What do you think about that?

Louis Diamond:

I think that's absolutely a business owner's prerogative. And the big thing you give up when you sell the business is control. The good thing is right now, there's so many different acquisition models out there where advisors can keep varying levels of control. So maybe someone looks to sell a minority piece of the business and still keeps their brand and their infrastructure et cetera.

Louis Diamond:

On the other end of the spectrum, would be a full-on acquisition where a large-scale RIA buys a smaller one. And then it's a full integration where brand and investment process and everything is morphed into the buyers. So definitely, that's something that someone has to reconcile with, is how much control am I willing to give up? And how important is it for me to solve for whatever the gap is?

Louis Diamond:

So in the case of the gentleman you spoke with, my guess is either he was more focused on growth, and didn't have any glaring strategic holes to fill. Or said I can be the buyer instead of the seller. And for right now, at least, I think I still have some growth left in me, and I'd rather retain control over taking chips off the table or gaining scale or solving for any of the other reasons that I mentioned that people might look to sell.

Mindy Diamond:

So I think we're going to get to it, but the notion of how likely is he to become a successful buyer at a billion dollars, completely self-funded, not backed by any source of client or institutional capital.

Mindy Diamond:

But the other thing I think is really, what I said to him is, "You have only just decided that you need to add to your infrastructure, that you need to add staff. So give it a couple of years, it's probably not that important. You're not in that much pain. It's not terrible. Right now, you're still growing at 30% per year, so there's no real motivation to sell. But if, after a few years in a very competitive market, you haven't had success in acquiring or buying or recruiting, you may change your tune." Do you agree with that?

Louis Diamond:

Yeah, I completely agree. And look, if he's growing at 30% per year, in the back of his mind, he's thinking, "Why would I sell now when I can be double or triple my size in three to five years?" And I think as long as he can sustain that growth rate, and the client service model doesn't deteriorate, he's still able to have work-life balance and whatever's important to him. I think he's probably right to not sell as long as he can keep up that growth rate responsibly.

Mindy Diamond:

I agree with that totally. And that's what I said to him. I think that we say a lot of times to advisors, you shouldn't move until or unless the pain of staying is great enough. He doesn't have pain. Yeah, he wants to grow. He's beginning to recognize the capacity issue.

Mindy Diamond:

But when you're growing at 30% per year, it's hard to argue with that. Again, I think we're going to get back to it a little later. But let me ask you right now, how likely is it that this gentleman's firm, with the billion under management, becomes the next major acquirer?

Louis Diamond:

To me, if I had to handicap it, I would say it's going to be tough because in this environment, unless you're backed by major institutional capital or have a really strong balance sheet and you've already locked in low borrowing costs, it's hard to compete against these major, major players.

Louis Diamond:

By last count, there's over 30 different private equity firms that have made a platform investment in the wealth management industry, meaning they've backed a firm or a platform that they're then weaponizing to go out and acquire practices.

Louis Diamond:

So you have all those types of firms that are competing on a national basis. You have local ones that may have access to capital et cetera. So his ability to execute on his M&A strategy, to me, the most likely outcome is he hits a couple singles and doubles here and there, maybe he does a deal or two, which might be impactful.

Louis Diamond:

But to say that he's going to automatically become the next major buyer, I think that's hard. Because it takes a lot more than just one firm with an interest in buying to go out and be successful. And I think that's what we're going to spend a lot of talking about is, if you are this type of firm, what can you do to set yourself apart? And what do you need to think about in order to have a shot at competing with the big boys?

Mindy Diamond:

So great pivot points. So, who are firms, whether it be this billion-dollar firm or firms of any size, who are the buyers? Who are they selling to?

Louis Diamond:

So same answer, who are the buyers? Who are the sellers? It could be other RIAs. So it could be a local firm or more of a regional player. Could be really any size. But it would be a firm that shares a common culture, that believes that one plus one equals three. Typically, these firms are not backed by major pools of capital; they're independent and fully owned by the leadership team.

Louis Diamond:

That's definitely a major part of the market. I think as we've seen, the number of non-private equity-backed RIAs that are buying, their share of acquisitions keeps going down and down in favor of these larger private equity-backed firms. But that's still a viable category. Another buyer might be, call them a national acquirer.

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So this would be one of these 30-plus firms that are backed by private equity or family office money or some sort of institutional capital that has scale, has a platform that they figured out growth. And it's one that they believe is attractive enough to lure in multiple firms.

Louis Diamond:

And usually, these practices are spread out across the country, they're agnostic as to the geography. But they're going to be full integration models, meaning someone joining them gives up their brand, gives up full autonomy on the investment side, plugs into their planning process and really, the acquirers' method of doing everything. Other buyers might be a private equity firm or a family office.

Louis Diamond:

These are groups that might buy a majority of the business. They might buy a minority slug of it as well. And usually, there's some sort of strategic benefit outside the capital that these groups bring, whether it's M&A expertise or deal sourcing or strategic guidance. And these are definitely a very popular part of the market. And then we'll say the rest are strategic acquirers. So it could be an insurance company that's looking for distribution or just likes the industry and wants to diversify the revenue stream.

Louis Diamond:

It could be a bank, folks swinging back the other way. Maybe they broke away from a major firm at one point. But now banks definitely want back in the space. We've seen a number of bank deals. And then even asset managers. As asset management is under challenge, a lot of asset managers, they like the fact that fees haven't compressed in the wealth management space, they like the recurring revenue and they like some of the synergies with what they're building. So point is, lots and lots and lots of buyers and a lot of different types of sellers too.

Mindy Diamond:

It seems if you're a seller, it's like drinking from a fire hose. How do you differentiate between them? And again, this is an episode about buyers. But if you are a seller, or thinking about selling or, essentially, a nascent firm or thinking about going independent and thinking about building something with the end in mind, how do you differentiate who you might sell to?

Louis Diamond:

It's hard. So we like to help business owners and advisors bucket these different buyers into categories. And each one has their pros and cons. So it starts with: what are you looking to accomplish? How much control are you looking to keep? What are the major gaps you're looking to solve for?

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And usually, we like to begin with that walk before you run. Before taking meetings or running a full process, you've really got to understand: what's a non-negotiable? What's a redline item for you? And what's the major things you're looking to accomplish?

Louis Diamond:

And then that helps to differentiate. But it is hard. And that's why it's usually advisable that a seller, who's going to sell their business once, works with some sort of professional, whether it's a consultant or investment banker, a business broker or someone who's done this before and can add some institutional credibility to your own process.

Mindy Diamond:

So let's pivot to what people came for, the notion of the buyer. So this may seem like a naive question, but why would a firm even be interested in acquiring?

Louis Diamond:

It's a great question. This is the one where it seems like a no-brainer. Everyone says they want to acquire because it seems like it's a complete no-brainer. But I think there's probably five or six really good reasons. And maybe we'll flip back and forth on what the reasons are.

Louis Diamond:

But I think the first point is it's not really a reason, but it's more a disclaimer that not every firm should be interested in buying. Because being an acquirer is a ridiculous amount of work. The dating process takes forever, you have to kiss a lot of frogs before you find your prince, integration is a massive amount of work, the deal process could be a slog.

Louis Diamond:

So if you're not really committed to being a buyer, I would say be out. It's either be all in or be all out. That's the first disclaimer I'll give is just because it might be attractive, doesn't mean that it's the right thing for you to do. Because you really have to be committed to it and have a strategic plan on how you're going to accomplish it.

Mindy Diamond:

So I would say I'll take the next one, the notion of operating leverage, that the more a firm adds to its bottom line without increasing expenses, the more the firm's expand margins and increase operating leverage. It's why a lot of folks are so interested in going independent in the first place.

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Because if you're an employee advisor of UBS, UBS owns all of your operating leverage as you grow. But when you go independent, you begin to own the operating leverage. So the notion of adding additional advisors or recruiting or acquiring other firms, you are automatically increasing operating leverage without necessarily concomitantly increasing expenses.

Louis Diamond:

Yep, exactly. So your EBOC might be 60% to 65% of revenue before you do a deal. But after you do a deal and you add a million, two million, three million of revenue, to your point, without adding expenses necessarily, maybe your EBOC increases to 65% to 70%. Then all of a sudden, there's more free cash flow and the combined business is worth a lot more than the standalone business.

Louis Diamond:

So I think that's exactly right. That's an elegant way of explaining the financial benefits of M&A. The next one I would give is new talent. A lot of firms look at M&A. Of course, there's financial benefits. But they look at acquisitions as being a talent grab.

Louis Diamond:

It's really hard to find good people. So by acquiring businesses, you're able to bring in next-generation advisors or bring in folks that have a different discipline or different focus, and really help the combined firm be even better. And especially in a tight labor market, this is one of the more appealing aspects of acquiring a company.

Mindy Diamond:

And the next one is actually very similar, the notion of expanding services or areas of focus. So if you're a firm that services mass affluent clients, and you acquire a firm that offers a family office type, or concierge services, or deals with more high-net-worth clients, or that offers insurance services or bringing in someone who does accounting and tax prep, it's the notion of increasing your opportunities for success.

Louis Diamond:

Yeah, exactly right. So looking at each acquisition as being a way to expand capabilities. And there's a number of acquirers in the market who won't even consider a deal unless the target does something differently, and there's areas that they can pick off from the acquired firm that's going to make the combined firm even better.

Mindy Diamond:

But I have to imagine, Louis, that there's a downside to that, that saying, "Stick to your knitting." So if your knitting is serving one type of client, and now you go out and look to only do a deal or acquire a firm that does something completely different than you do, isn't there a high chance for failure?

Louis Diamond:

Yeah, I don't disagree. There has to be a balance. I don't think there would be enough benefits for either firm if they're two completely different businesses. But maybe they're both planning-based firms. One has a focus on working with doctors, the other one comes in, and they have a focus on working with corporate executives.

Louis Diamond:

Maybe there's some cross-synergies between the planning resources and the investment platform. And now it's, "Okay. We're really good at marketing to this one audience. You market to this other audience, and we can use our joint capabilities to go and expand our market share in both markets." So I think it's all about the balance or the give and take of the two.

Mindy Diamond:

And I think that speaks to 100% of what underlies everything we're going to talk about, where acquiring is great, it increases revenue and operating leverage and all that sort of good stuff. But the wrong deal can blow up a firm, and culture matters.

Louis Diamond:

Exactly right. And the last two I'll round us out on, is entering a new geographic market. This one's self-explanatory. So it's, "Okay. We're based in Chicago and we're also in Indiana. We want to acquire a firm that's in New York or that's in Philadelphia and use an acquisition as a way to enter a new market."

Louis Diamond:

And then maybe even extend it further and say, "We're going to enter a new market, and then we're going to do a sub-acquisition strategy in that market as well." So basically, having a beachhead to go out and do more deals in a different geographic area. Much easier to acquire a large share of assets in a new geographic market rather than trying to go and build client by client in a market that you don't have brand credibility and you don't have centers of influence. And the last one, and this one goes hand in hand with operating leverage, is the concept of a rising tide lifting all boats.

Louis Diamond:

So let's say my independent firm is worth nine to 10 times earnings or EBITDA before I do an acquisition. I then go and acquire a firm for six times EBITDA. The combined firm now might be worth 12 times

EBITDA. So very quickly, obviously, you have the work of integrating the firms, the combined entity is worth a whole lot more.

Louis Diamond:

So this might talk to firms that offer equity as part of a deal where it makes sense if I'm at 6X, you're at 10X. Why don't we come together and now be worth 12X? And when the combined firm goes to sell, it's now worth a whole lot more. So lots and lots of financial benefits of acquiring. And we talked about, I think, some of the softer benefits on talent acquisition and expanding services and entering new markets.

Mindy Diamond:

I want to pivot now. So if I'm a team at a traditional brokerage firm, Morgan, Merrill, UBS, name it, any regional firm on the street, how is acquiring in the independent space different than being a successor via a retiring advisor program like Merrill's CTP, or UBS's Alpha or Morgan Stanley's FAP?

Louis Diamond:

I think that's a really, really fair question. When we speak with advisors that are captive at a wirehouse, or really any traditional W2 firm, they do have a big opportunity to serve as the successor to an advisor that's looking to retire. And all of these major firms, and even smaller ones, have come up with buyout mechanisms, where a retiring advisor can monetize their life's work for a relatively fair multiple.

Louis Diamond:

And the next-generation advisor is then able to pay them out from the cash flow of the business, and ultimately, have a much larger pool of assets that they'll manage in the future. So it is a very appealing aspect of being at a big firm in that you do have a captive group of folks to acquire, unlike in the RIA channel where there's a multitude of buyers. And it could be really any firm across the industry could buy. The appealing aspect of being an acquirer in a W2 model is an advisor's likely to sell to someone within their branch office or within their market and certainly within their firm.

Louis Diamond:

So you have less competition, and likely have a clearer path to being a successful acquirer. That said, it's not all positive. Because someone who's "acquiring the business," and I have air quotes up, in a W2 model, is not really acquiring anything. What they're doing is they're using their own sweat equity to transfer economics from the retiring advisor to them after a period of a lower payout.

Louis Diamond:

But in the end, their firm is still legally owning the book of business. So really, it's putting in the blood, sweat and tears to transfer a business, but in the end, you're not owning anything. And this is compared to being independent where advisors own their business, own their equity, own the client relationships. And every firm they acquire, they're legally owning and have the ability to sell it for much higher multiple in the future. So I think that's the first one. Is there anything you would add there?

Mindy Diamond:

No, I think that that's absolutely right. It depends upon what your goal is. If I'm an advisor at Merrill Lynch and I intend to retire, and I am perfectly satisfied that Merrill Lynch is the right legacy for me, it's perfect for my clients, it allows me to do everything I need to do, and either I don't have a next-gen successor or my next-gen successor is equally satisfied as I am, then these retire-in-place programs at the traditional firms are actually a gift.

Mindy Diamond:

The problem is, and I know you and I talk about this all the time, that probably, the number one constituency we hear from are next-gen advisors that call us and say, "A partner advisor who is 60 or 70 wants to retire. It's a gift that I can inherit a billion-dollar book or $500 million book. But what are the downsides?"

Mindy Diamond:

And you and I, we've done episodes, we've written a lot, we've interviewed Tom Lewis, an attorney, talking about the topic. There are plenty of downsides. So I think I don't want to belabor the point, but what you said about the fact that in those retire-in-place programs, the younger advisor is actually buying a business that he or she doesn't own in the end.

Louis Diamond:

Yeah, exactly right.

Mindy Diamond:

But the next thing is the notion of gaining more flexibility and creativity in terms of structure. So maybe you can give us some examples of what we mean by that, Louis?

Louis Diamond:

Sure. So with any of these prepackaged retire-in-place programs, there's sometimes different options that advisors have for entering into the programs. They can choose sometimes when they enter it, and ultimately, how many years one get paid out over. But it's pretty formulaic. It basically says, "If we're doing this much in business, you've been at the firm this long, then here's what you..." It's easier to understand. It takes away a lot of the negotiation that's necessary between buyer and seller.

Louis Diamond:

But it does box both buyer and seller into a prepackaged approach, versus in the independent space, there's limitless options for how to structure a deal. So maybe a seller wants to stay on for 10 years. So maybe they can sell 10% a year for 10 years. Or maybe they're really focused on selling the business for the highest number, and they think their business is worth way more than what a retire-in-place program is worth.

Louis Diamond:

So they're welcome to go take it to market, sell it for whatever they want. And same thing with the buyer: they can structure deals in different ways, they can use equity as a currency, they can change the duration of how long they're going to pay someone out over. There's just a lot of different ways that both buyers and sellers, I think, can meet their joint goals versus being locked into a preset approach, which is what happens in these retire-in-place programs that are part of the W2 world.

Mindy Diamond:

And I think if you are a next-gen successor and young enough with a long enough runway to retirement, there's a whole lot to gain to be building a business over time that eventually can sell for a multiple, anywhere from nine to, say, 15X.

Louis Diamond:

Exactly right. That's right. So because you're actually owning the business, if you're buying in as an independent, then you're able to go and sell the business for more because you actually own the business. And like we talked about before with operating leverage being a really important term. If I'm buying a business, let's say, I'm an advisor at Merrill who's buying a retiring advisor's book.

Louis Diamond:

Regardless of the size of that book, maybe I'm doing two million of annual revenue, I buy another $2 million book. Maybe I was at a 48% payout before I did the deal. Now, once I buy, maybe I'm getting a 49% payout or 48.5%. So now my business is significantly more profitable to the firm.

Louis Diamond:

But I'm not increasing my net payout as opposed to the independent world, where of course, you have to take into account the cost of debt and you have to actually pay someone for the business. But maybe I'm at 65%. Now after the deal, I'm at 70%. Because now I control the operating leverage versus my firm.

Mindy Diamond:

I think that's a big one. So I want to get to what an advisor or a team, who goes independent, needs to do to establish themselves as a buyer. Because I think that that's really the key to this episode. But before we get there, maybe we can talk about some examples of ex-wirehouse teams who have been successful acquirers.

Louis Diamond:

Sure. I'll actually just give three examples just from this podcast. So these are advisors that we've interviewed on this series. So anyone who's listening can check out those episodes, we'll put the links on the episode page. So there's a ton more. But I was using just the universe of folks that have been gracious enough to come on our show.

Louis Diamond:

So one that's very top of mind, it was actually an episode that will be very close in release to this one, is Todd Resnick, who runs One Seven. Todd and his team were managing about $600 million before they left Morgan Stanley. This is back in 2016. Today, they're about $2.8 billion. And much of that growth has come through M&A. They've sold a portion of the business to a family office, they've done a couple of notable acquisitions. And they've also been a very successful recruiter of top talent.

Louis Diamond:

So they're a really good example of a team that grew. They've grown organically, but much of their growth to $2.8 billion has been inorganic. So Todd's a great example. Another one would be Gerry Goldberg. His firm was GYL Financial Synergies. They were a Wells Fargo advisors group that moved over to Wells Fargo FiNet. And then, a couple of years ago, they launched into the independent space, partnering with Focus Financial Partners.

Louis Diamond:

And then have done a number of deals, and have more than quadrupled the business, largely, through M&A. And Focus is a great example of an enabler of acquisitions where they're the institutional capital, they're providing deal-making expertise. And obviously, Gerry and his team have to be doing something pretty special to convince others to entrust their life's work to them. But Focus is kind of the catalyst or the enabler of that.

Louis Diamond:

And then another one I'll give you, this one's a little bit different, but it's definitely an M&A strategy, would be Rob Sechan, who is running NewEdge Wealth as part of EdgeCo. They're backed by Parthenon Capital. Rob left UBS, managing about five billion in assets. And now, less than two years, they've acquired the practices of some very significant wirehouse teams that have broken away, and are very serious about acquiring RIAs.

Louis Diamond:

So that's three examples. They're all playing in different segments of the market. They have different capital partners. But I think what all of them have in common was a vision of doing something that they couldn't do at their current firm. They've all partnered with capital providers and those that can provide expertise in capital.

Louis Diamond:

And they also had really compelling value propositions where they knew what they were doing was a great model for attracting clients, but they were able to then go out and make that appealing to a broader audience. So I think all three of those are really good roadmaps, or examples or case studies of how these successful wirehouse teams became even more successful after going independent and turning to M&A.

Mindy Diamond:

I love that. So there were so many things that stick out to me about those examples. And I love the interviews we did with each of the three owners that you mentioned. But the thing that sticks out more than anything is that all three of them sold either all or part of their firm to some form of institutional capital.

Mindy Diamond:

So when I asked before about that billion-dollar firm, the owner of the billion-dollar firm who wants to grow by acquisition. And I said, "How likely is it that he will be successful?" And you said sort of low probability. Is that because one of the key ingredients to really establish yourself as a buyer is to take on some sort of capital pool?

Louis Diamond:

I think the short answer is yes. That is one of the hacks to becoming a successful acquirer, is aligning yourself with some sort of capital partner for a couple of reasons. I think one, is it's a really expensive endeavor to go out and acquire and just relying upon your own cash flow or turning to a bank for debt financing doesn't really get it done.

Louis Diamond:

You need that extra bit of fire power. It's also really hard to complete deals. So having access to groups that can structure deals, they have deal documents, they can do valuations, they can run a process, is extremely helpful. It also just puts you on the radar of folks like us, of investment bankers and other deal facilitators in the industry.

Louis Diamond:

Because we take much more seriously a firm that's backed by a credible capital source. So it's not the only way to become a buyer. And there's a couple buyers I can think of who purposely haven't taken on capital, but I think they're in the minority. And over time, they probably struggle to keep up with what these larger firms can do.

Mindy Diamond:

I actually think that you're right. And yet, someone like this gentleman that called me the other day, is hell-bent on spending the next five years really looking to add talent. So what are some of the other things that a buyer of any size, who either is or isn't backed by institutional capital or significant capital, what is it that they need to do in order to establish themselves as a buyer?

Louis Diamond:

So I think that first and foremost starts with what makes your firm different from everyone else? It's the old joke if you're at an industry conference, at an M&A session and someone asks, "Who's looking to buy?" 87% of the room puts their hand up. Who's looking to sell? Maybe one guy puts a hand up. And then a couple of people are too shy to answer.

Louis Diamond:

So that is kind of the dynamic. So you really do have to go out of your way to stand out from every other firm. Not just locally, but across the country. So it's what makes your firm different and unique. If you can't articulate that in a very clear and concise way away from, say, the table stakes, "We have great people, we have a really good brand, we care about our clients, we focus on planning," you probably shouldn't attempt M&A.

Louis Diamond:

So you have to just think long and hard about what makes your firm different and unique, not just to an end client, but to a perspective advisor or a business owner who might want to join you. I think another one is that you've really figured out how to grow organically. So you don't need to rely upon acquisitions to grow.

Louis Diamond:

Firms or advisors looking to join you, they're usually attracted to firms that figured out organic growth. So whether it's a lead generation program or access to a custodians' referral program or CPA referral networks, some sort of way that you can show advisors how they'll be better off financially by joining you, and why they can grow faster with you than without you. So I think if you crack the code in organic growth, and there's a way to scale what you're doing, that's a really compelling ingredient that you can use as part of your value proposition and stand out versus many others in the field.

Mindy Diamond:

So you talk about somebody like Todd Resnick going from $600 million to $2.8 billion. So it sounds like the most pivotal thing he did was to sell part of his firm to a family office, right?

Louis Diamond:

Yes. I think that was a catalyst. He was successful before. But they recently announced a merger with a billion-dollar-plus firm, and they announced that at the same time as taking on capital from Merchant, which is a family office.

Mindy Diamond:

So what you're saying is that Merchant, which was in this case, the source of capital, became the catalyst that gave them the money and the legitimacy to then go out and be attractive to sellers and other wirehouse advisors. Is that right?

Louis Diamond:

I think that's right. But I think Todd and his team had figured something out before. It wasn't just that they took on capital and now, all of a sudden, they're interesting and compelling. They built a really interesting firm, they had a clear message about what they can do for advisors.

Louis Diamond:

And they had a track record of proving how they recruited advisors. And those advisors were then able to grow faster than they could have grown without them. So it all goes hand in hand. But we'll say access to capital or selling a piece of the business, it might be the fuel that makes the fire spread. And without that, maybe it's a controlled burn versus something that can be taken nationwide.

Mindy Diamond:

And I think that's a really good point. So we're saying that all of these really legitimate buyers have one thing in common, and it's that they've taken on some form of capital. But if they didn't have a spectacular and unique value proposition, if they didn't have an infrastructure, a strong and robust infrastructure with excess capacity, if they didn't have systems and support to support it all and they didn't understand the market, they never would've been successful.

Louis Diamond:

I think that's right. And I think another really overlooked piece of being successful at this is having either a dedicated resource or maybe the leader of the firm whose almost entire job is to focus on M&A. It really doesn't work when you have the CEO, who's also an advisor, who also dabbles in M&A.

Louis Diamond:

Even though some people might like that they can empathize with the person they're talking to, it's really a full-time job to do this successfully. So by committing to investing in an M&A business, likely means hiring someone or reallocating your time and energy to M&A. And I think that's another piece of it is just you're committing to it. And again, it's all in or all out.

Mindy Diamond:

That's absolutely right. And it's also worth noting that not everyone who goes independent wants to become a prolific buyer, wants to become the next NewEdge, or the next One Seven or the next Gerry Goldberg's GYL Financial Strategies. And that's okay too. But if one's goal is to become a buyer and really build a firm that becomes a prolific acquirer, then a lot of what we're talking about matters.

Louis Diamond:

I agree. Yeah. We hear that a lot of times with teams considering independence is, "I don't want to acquire. Why should I go independent?" And the answer is there's many other reasons why you should. But for many, the idea of being an acquirer or being a recruiter of talent is one of the major reasons they want to go independent. So every advisor has their own reasons. And we're just giving some reasons why it might make sense to buy. But certainly, you can be a successful firm without being a buyer.

Mindy Diamond:

Yeah, and it's worth noting. I know you and I have moved plenty of breakaway advisors, that is advisors leaving the traditional space to go independent, who had zero interest in becoming acquirers out of the gate.

Mindy Diamond:

But as they began to really understand the notion of operating leverage, and as they began to really plant their feet on the ground and really wrap their head around being a CEO, the notion of acquisition or recruiting became really appealing to them. So it's not necessarily somebody's goal right out of the gate, but it oftentimes can be over time.

Louis Diamond:

And we've also seen it the other way where advisors try to bite off too much at once, where they're breaking away, they're going to be independent for the first time and they want to start acquiring recruiting right away. And that's not normally advisable either. So you've got to find the right time in the evolutionary business to consider buying, if there's any time at all.

Mindy Diamond:

Yeah, I agree. So let me ask you one last question. So if someone has now set themselves up as a buyer, how do you go about finding the right potential targets?

Louis Diamond:

I think the first thing is you have to take it upon yourself. So you can reach out to firms like ours, or investment bankers or centers of influence all you want. But if you're really serious about it, you have to take matters into your own hands. So to me, that means either hiring someone who's a full-time deal sourcer, in that they may find deals through cold-calling, or LinkedIn or networking through industry events. Many ways to go about it.

Louis Diamond:

But I think the first one is don't wait for the phone to ring. Go out and make it incumbent upon yourself to go and find targets. That's one. The other one would be to notify key people in the industry, whether it's centers of influence that you know interact with many advisors or firms. It could be your custodian's relationship manager. Again, firms like ours or investment bankers. It could be attorneys. Really anyone who traffics with potential targets.

Louis Diamond:

Another one I would say is just make yourself known. Be out in the public eye, whether it's being in the media or having a social media presence. You want to be known as a thought leader and be known as someone that if I sold one day, I would like to sell to that person. And the more you're out there and putting out unique content, the better chance you have at standing out. So I think that's a couple of ways that comes to mind.

Mindy Diamond:

You and I have built a business, where putting out smart and thoughtful content, not for the purpose of marketing or selling, but for the purpose because we wanted to put our thought leadership out there. And we've grown a lot because of it. We know better than anyone that that really works. So I love that idea.

Mindy Diamond:

Industry Update on M&A: Why Buy? Tips for Those with Their Sights Set on Becoming an Acquirer

A conversation with Louis Diamond.

So I think there's a lot to say. Buying can be very attractive. It also can be absolutely detrimental if it's not done the right way or not with the right firm, I should say. So Louis, I can't thank you enough for joining me. But any closing words of wisdom, if you will?

Louis Diamond:

No. I think the only thing to say, as I mentioned earlier, only approach M&A if you're really ready to commit yourself to it. If you're not, then it's okay to stay on the sidelines.

Mindy Diamond:

That's really good advice. Essentially, know thy self. Louis, I love doing these episodes with you. I think it's always really a smart back and forth. I thank you so much for joining me.

Louis Diamond:

Anytime. Look forward to the next one.

Mindy Diamond:

I thank you for listening. And I encourage you to visit our website, diamond-consultants.com, and click on the tools and resources link for valuable content. You'll also find a link to subscribe for regular updates to the series. And if you're not a recipient of our weekly email perspectives for advisors, click on the articles link to browse recent topics.

Mindy Diamond:

These written pieces are an ideal way of staying informed about what's going on in the wealth management space without expending the energy that full-on exploration requires. You can feel free to email or call me if you have specific questions. I can be reached at 973 476 8578, which is my cell. Or my email, mdiamond@diamond-consultants.com.

Mindy Diamond:

Please note that all requests are handled with complete discretion and confidentiality. And keep in mind that our services are available without cost to the advisor. You can see our website for more information. And again, if you enjoyed this episode, please feel free to share it with a colleague who might benefit from its content.

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