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DeVoe & Company

RIA M&A Activity Sprinting Toward Another Record Year

M&A activity continues to occur at record levels for established RIAs.

RIA M&A activity accelerated its momentum with a strong second quarter and set the stage for yet another record year. The 33 transactions posted during the period continued a consistent pattern of strong volume, according to research by DeVoe & Company. Activity was well above the same quarter last year, which saw only 18 transactions, and far above the 12-month trailing average of 29.

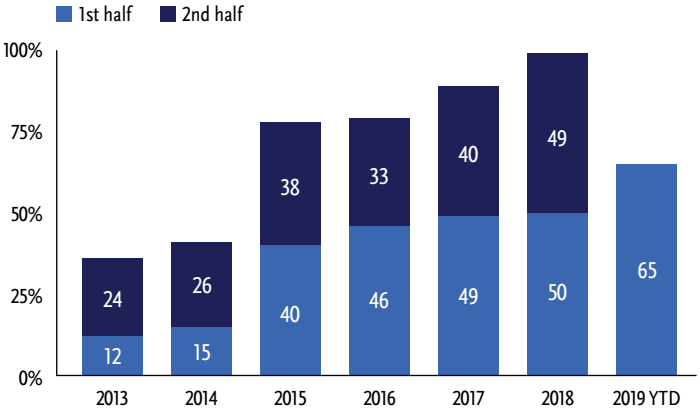
With 65 transactions in the first half, there is a clear path toward a new all-time high of annual activity. The activity in the first six months was a solid 30% higher than transactions in the first half of the last two years – both of which were successive records at 50 and 49, respectively.

With the last three quarters' rankings among the industry's top four quarters of all time, RIA M&A momentum has moved from a "spike" to a "surge" and is now trending toward a possible "new normal" of heightened activity.

"The industry is experiencing an unprecedented, sustained surge, which seems likely to continue," said Brad Grubb, Managing Director at DeVoe & Company. "High valuations, the interest in gaining scale, and the lack of succession plans will continue to contribute to the sustained pace."

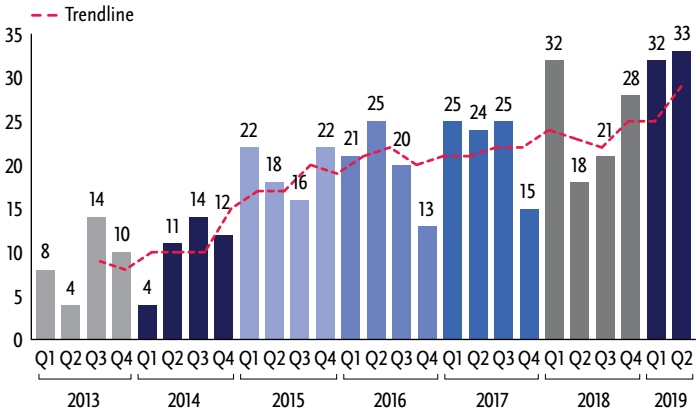
M&A activity soars in the first half

Semi-annual M&A activity



Record quarter for M&A activity

Number of transactions executed per quarter



RIA valuations journey toward a record high

Indeed, high valuations are a factor. "RIA valuations are officially at an all-time high," said David DeVoe, Managing Director at DeVoe & Company. "Over the last several months, valuations have hit new highs and have attained levels I have not seen during the 16 years I've focused on RIA M&A."

Buyers in today's market are not necessarily paying unjustified prices. Many acquirers are students of the industry and have learned from history.

In the early stages of the industry, RIA M&A was in the low double digits per year and acquirers were using tools borrowed from the CPA and legal industry. In the early 2000s, a new wave of sophisticated buyers entered the space, bringing better valuation techniques and deeper pockets. The oversimplified "2x revenue" rule of thumb was discarded, as buyers started using discounted cash flow models to separate the good acquisition targets from the bad. The myriad of valuation drivers could be easily assessed with these models. A buyer could now quickly tabulate how a seller stacked up in the details behind three major categories of valuation: Growth, Profit and Risk.

M&A activity began to increase as new buyer entrants started to compete with one another for sellers. Buoyed by the strong stock market and economy, RIA's high growth and expanding profit margins further rationalized higher valuations. Banks were not shy to write big checks as the competition for larger firms increased, while new less sophisticated buyers started irresponsibly over-paying for firms. These various drivers created a crescendo of M&A activity and a peak of valuations in late 2007 and early 2008.

Then the stock market dropped.

The stock market crash of 2008 hammered down valuations in a matter of weeks. The projections and assumptions of the three key valuation drivers – Growth, Profit and Risk – all went in the wrong direction. Transactions under discussion staggered to closure, as the sellers and buyers started to pull back. Valuations had moved from an all-time industry high to an all-time low within a matter of months.

Valuations ticked up as the stock market stabilized and started to improve. As the economy started to grow again, valuations clicked higher. Slowly and steadily, valuations increased over the last decade; as the future looked brighter, the underpinnings got stronger and RIAs became more attractive.

Why has the industry now exceeded the valuation apex that a decade ago was supported in part by irrational buyers? Are the current buyers unsophisticated and irrational? We think not.

Many of today's buyers are sophisticated and acutely aware of the high multiples. But more importantly, many of today's buyers are actually creating value – true value, beyond a future arbitrage opportunity or liquidity strategy. They have built scale, invested in technology and operations, created partnerships to drive growth – they have crafted intelligent business models and have the professional management in place to execute on the plan. In essence, today's buyers have built machines that can potentially achieve the old aspirational maxim of 1 + 1 =3.

So, the high valuations that have recently emerged are not necessarily unjustified. Depending on the business model and the valuations are fully rational.

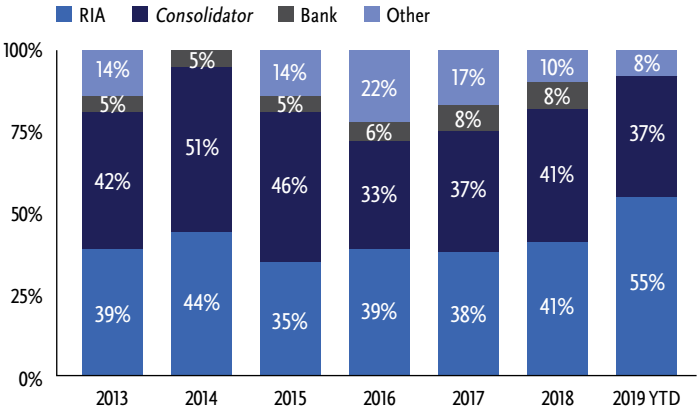
One thing we might expect is that these high valuations will attract more sellers to market.

Consolidators and serial acquirers support record pace

RIAs as a Buyer Category pushed their share of transactions above the 50% mark during the first half of 2019 – a majority that this group has not seen for years. A growing number of RIA owners are using M&A as a way to achieve strategic goals and objectives. Many sellers are not only attracted to the power of scale that many larger *RIA Buyers* offer, but they also value the concept of joining a company founded by "someone like me." There is a level of comfort in selling to someone who has sat in the same chair and built a similar business. As a result, RIAs like RegentAtlantic Capital and Klingenstein Fields Wealth Advisors, or even mega firms like Mercer Advisors and Wealth Enhancement Group are benefiting and winning new deals.

RIAs dominate as a buyer category, as *Banks* pull back

Acquisitions by buyer category



The *Consolidators* are not a group that sits idle on the sidelines. In fact, a sizable group of *Consolidators* racked up several transactions each. Seven *Consolidators* executed three or more transactions each during the first six months of 2019. Leveraging their M&A acumen, access to capital and seasoned management teams, these organizations put up impressive numbers of both direct and sub-acquisitions. An observer might also note that many of the *RIA Buyer* deals were supported by and ultimately roll into the *Consolidators*, in the form of sub-acquisitions (more detail below).

Focus Financial Partners broke away from the pack with 15 transactions year to date. Mercer Advisors and CAPTRUST Financial Advisors both completed four transactions, and four veteran acquirers — HighTower Advisors, Mariner Wealth Advisors, Emigrant Partners (formerly Fiduciary Network), and Wealth Partners Capital Group — were not far behind with three transactions each.

Banks as a buyer category were surprisingly quiet through the first half of the year, with the exception of a single loud crash. The ill-fated Luminous Capital / First Republic Bank transaction broke apart shortly after the provisions of their transaction structure expired, with $17B of assets fragmenting into two new breakaway firms. This event is a stark reminder of the complexity and risk associated with M&A. It also reinforces the fact that the long-term success of a transaction is driven by thoughtful strategic planning, alignment of long-term goals, true integration, and methodical execution.

Experienced acquirers show expertise matters

Firms with multiple transactions during first half of 2019

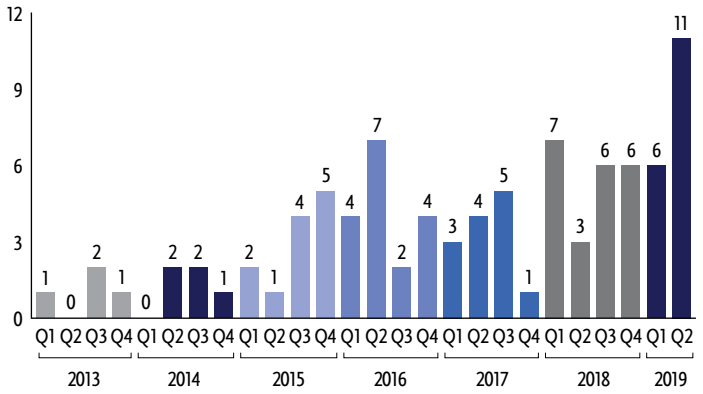
Firm	Total acquisitions	Parent acquisitions	Sub-acquisitions
Focus Financial Partners	15	3	12
CAPTRUST Financial Advisors	4	4	0
Mercer Advisors	4	4	0
Emigrant Partners (Fiduciary Network)	3	2	1
HighTower Advisors	3	2	1
Mariner Wealth Advisors	3	3	0
Wealth Partners Capital Partners	3	0	3
Buckingham Strategic Wealth	2	2	0
Carson Group Partners	2	2	0
Cerity Partners	2	2	0
Cresset Asset Management	2	2	0
Crestwood Advisors	2	2	0
MAI Capital Management	2	2	0
United Capital Financial Advisers	2	2	0
Wealth Enhancement Group	2	2	0

Sub-acquisitions spike

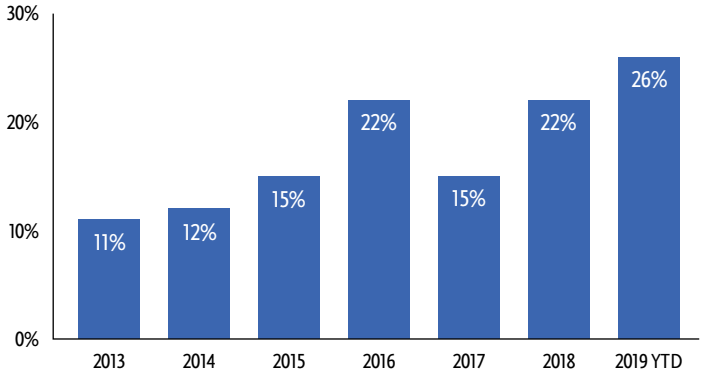
Sub-acquisitions rocketed to a breakout quarter in Q2, more than doubling their historic average. In the second quarter, the number of sub-acquisitions jumped to 11, beating the prior quarterly record of seven in the first quarter of 2018. Defined as acquisitions executed by firms that have themselves been previously acquired, these types of transactions are likely to further accelerate *Consolidators*' growth. Sub-acquisitions now represent more than 26% of all transactions – yet another record.

Sub-acquisitions hit a new high mark

Number of sub-acquisitions by quarter



Sub-acquisitions as percentage of transactions



Affiliates of Focus Financial Partners added a notable 12 sub-acquisitions in the first half and six in the second quarter. In a fireside chat with David DeVoe at the May **DeVoe M&A+ Succession Summit** in New York City, Rudy Adolf, Founder and CEO of the publicly traded company, elaborated on sub-acquisitions being a key part of the firm's growth strategy. "We do mergers on behalf of our partner firms, almost 30 deals in a typical year," he said. "Any Focus partner has access not just to our expertise but to our capital, and to our extremely low cost of capital." However, he explained a golden rule at Focus: Never strongly encourage a merger just for the sake of it. "The only thing that's worse than not doing a deal is doing a bad deal," Adolf said.

Wealth Partners Capital Group, which has been in high gear for the past year, helped its affiliates acquire three firms in the second quarter alone. Emigrant Partners (formerly Fiduciary Network) also supported RegentAtlantic with purchase of Hillview Capital Advisors.

The potential power of sub-acquisitions is too attractive of a strategy for *Consolidators* to ignore. DeVoe & Company expects this trend will accelerate over time and will have a growing impact on smaller transactions. Ultimately, this is a healthy development for the industry, as an increasing number of small and mid-sized firms will need to sell externally due to lack of succession planning.

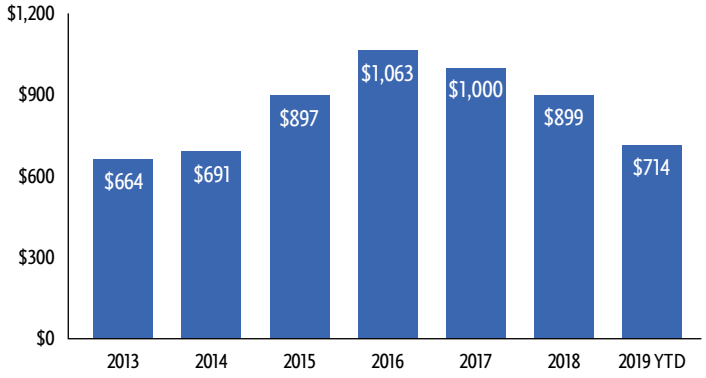
Average seller size still well below $1B

The average seller size (excluding transactions over $5B) ended Q2 at $821MM. Despite a more than $200MM bounce from the first quarter's average of $595MM, the average size of RIA sellers settled at $714MM for the midpoint of 2019 (all transactions over $5B are removed in this analysis for comparative accuracy).

Far off its full-year peak of over $1B in 2016 (and $1.8B for a single quarter), the average size has experienced a jagged decline over the last three years. This compression has been driven primarily by the efforts of successful buyers. In addition to the success of firms like Mercer Advisors, Wealth Enhancement Group and others that are targeting smaller and mid-size advisors, the sub-acquisition momentum also contributes to this decline in size.

Seller size remains below highs of past years

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

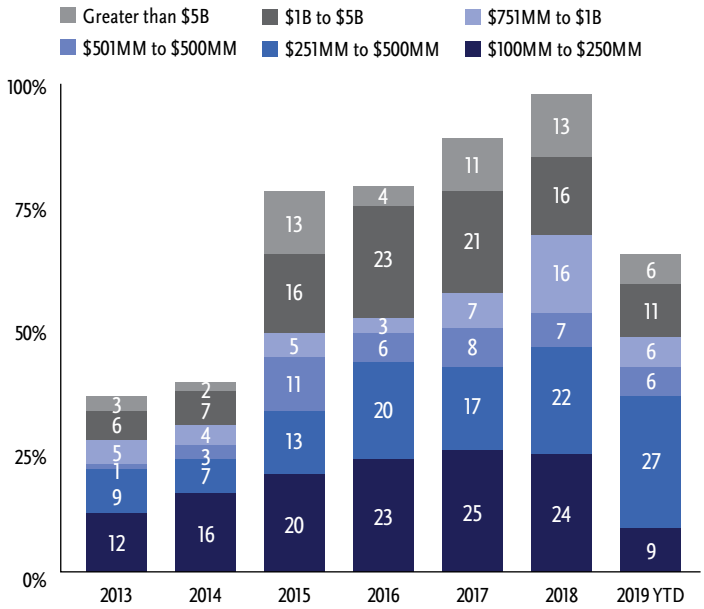


Due to the factors above, acquisitions of RIAs with $250-$500MM increased momentum with 27 transactions, representing 42% of all transactions in the first half of 2019. This is a sharp expansion from previous years; only 22% of sales in 2018 were in the $250-$500MM segment.

At the higher end of the scale, acquisitions of RIAs with $1-$5B made up 17% of all transactions in the first half, with 11 transactions, 8 this quarter alone, a near record. Given the pace of transactions in this size category, it's more than likely that 2019 will beat the five-year average of nearly 17 acquisitions of firms with $1-$5B.

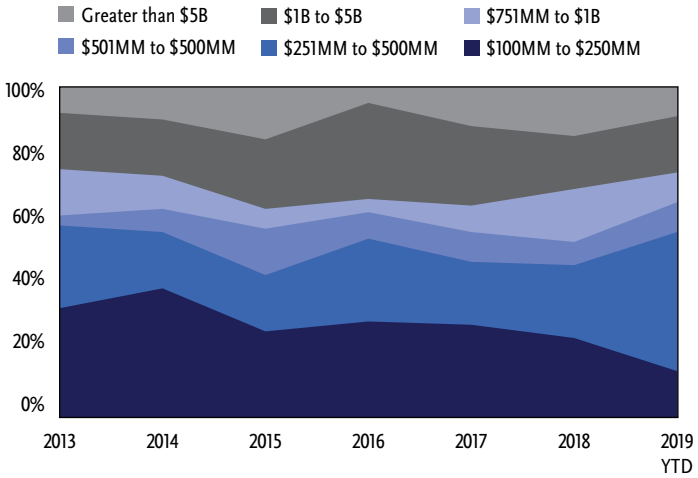
Spike in numbers of sellers in $1-$5B range

Number of transactions by seller AUM



Fast growing $250-$500MM advisor category

Percentage of transactions by seller AUM



United Capital to join Goldman Sachs

United Capital's sale to Goldman Sachs is an important flashpoint with long-term strategic implications and potential repercussions. The $750MM cash transaction is another step forward in Goldman's broader strategy to bolster its wealth management franchise and serve a broader client segment. The company is leveraging its strong brand to extend its wealth management strength as a leading ultra-high net worth provider to the high net-worth space. Anecdotally, the move may resonate with United Capital advisors and clients: DeVoe & Company was representing a $1B seller at the time of the transaction, and the RIA owner noted that Goldman Sachs was "the only Wall Street firm my clients would be comfortable with" in response to discussion of hypothetical strategic buyers who might acquire United Capital.

The transaction is another *proof of concept* to private equity firms investing in the RIA space. With two of the original *Consolidators* (Focus Financial Partners had a successful public offering in 2018) experiencing key liquidity milestones, private equity interest is likely to increase – and beyond the already very high level of interest. The sale bodes well for other private equity-backed firms such as HighTower, Mercer, Wealth Enhancement Group, and Allworth. And certainly, other Wall Street institutions are watching Goldman's move and considering how they might buy their way into a larger share of the RIA market.

Conclusion

2019 will likely be a banner year for M&A activity. But, more important than the number of transactions, is the number of options for sellers. Today's buyer pool is more sophisticated, better capitalized and has stronger business models than in the past. And that's good for RIAs. Sellers have the opportunity to be picky – to find the buyer that is truly the right partner. And sellers are better equipped to assess whether they need a buyer at all – or if they can continue to run fully independently.

The near-term future will likely have many interesting developments. How will other Wall Street firms react to the Goldman Sachs / United Capital deal? Will valuations continue to increase? Will Consolidators continue to refine their models, and will we see banks (finally) re-enter the market in a significant way? The RIA industry continues to be healthy and dynamic. And RIA M&A will continue to impact the industry.

Our methodology and the focus of the RIA M&A 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 16 years — longer than anyone in the industry — DeVoe & Company continues to evolve our methods and focus to best serve our readers and clients.

To this end, the RIA Deal Book's purview is to focus primarily on the acquisitions and mergers of true RIAs. 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, which has created murkier reporting and an illusion of higher deal volume, from our core analysis. We will touch on this category, when appropriate, but these transactions are not our focus.

In our earlier issues of the RIA Deal Book, we named this the category Established *RIAs* and that is now our primary focus. As always, we continue to report on transactions of RIAs with $100 million or more in AUM. Our reporting draws the line at $100MM to optimize the statistical accuracy of our reporting: We are confident that we can consistently capture the vast majority of transactions executed within this pool of 5000+ advisors. Dropping below $100MM AUM would expand the universe by another 7000+ firms, many of which would not report a sale or merger in the sources that we use to track deals, which, in turn, would erode the consistency and accuracy of our analysis.

DeVoe & Company Overview

Providing business strategy and M&A consulting services to the wealth management and investment management community

About DeVoe and 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 comprehensive valuation, strategy and M&A advisory services to help you accelerate the achievement of your business goals. Leveraging our team's 160 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 160 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. Half our team is McKinsey-trained management consultants and the other half is former COO's of $1B+ 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 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 of the 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.

DeVoe & Company executed more than 350 engagements in the last several years, supporting firms managing $50MM to over $8B in AUM

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:

- *DeVoe RIA Deal Book — The industry's leading quarterly RIA M&A deal tracker and fact book*
- *Succession Planning: Planning Your Future*
- *Putting Strategic Context Around Your Succession Plan*
- *M&A Surges: Why, and Will it Continue?*
- *Options, Options, Options*
- *Tailor-Made Successor*
- *True Value: Learn to Focus on the Things that Drive Up the Value of Your Practice*

Engaging DeVoe & Company

For more information or to engage our services call us at 415.813.5066 or send an email to info@devoeandcompany.com.

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From Nuveen

A new generation is flocking to cities, driving major economic and social shifts

Throughout the world, the story of the last century was one of dramatic population shifts that coincide with relentless industrialization. In this century, the pace of urbanization has retained its momentum as people migrate from rural to urban areas to seize greater economic opportunities and experience the dynamism of the world's metropolises.

According to the United Nations, more than half of the world's population already lives in urban areas today, and the organization predicts that this percentage will rise to 68% by 2050.

Read Nuveen Knows: Upcoming Urbanites, an in-depth look at the investment implications and opportunities of this megatrend. Areas of focus include:

- **Agriculture:** How will the agricultural sector keep pace with the needs of a rising global middle class in urban areas?
- **Infrastructure:** What must be fixed? What must be built? How will the public and private sectors collaborate to fund the work that needs to be done?
- **Impact investing:** One solution to the diminishing supply of affordable housing in urban areas is impact investing that's aimed at preserving rent subsidies while refurbishing the housing stock to create livable communities.
- **Real estate:** By 2030, Asia Pacific, led by China and India, will account for nearly half of the world's output, more than 50% of the world's urban population growth and almost all of the top 50 global cities

- **To learn more, contact your Nuveen Advisor Consultant team or visit https://www.nuveen.com/alternatives.**

Nuveen RIA and Family Office Advisor Consultants

■ WEST	**Chad Givens** MD, Advisor Consultant	415.595.5720	chad.givens@nuveen.com
	Vincent Chiu AVP, Advisor Consultant	415.650.6780	vincent.chiu@nuveen.com
	Ray Torres AVP, Advisor Consultant	732.832.6330	ramon.torres@nuveen.com
	Ed Rhee AVP, Internal Advisor Consultant	312.917.8209	edward.rhee@nuveen.com
■ CENTRAL/MIDWEST	**Trey Anton** MD, Advisor Consultant	949.331.2881	trey.anton@nuveen.com
	Doug Gowski AVP, Advisor Consultant	646.483.3032	douglas.gowski@nuveen.com
	Matt White, CAIA VP, Internal Advisor Consultant	312.917.8163	matthew.white@nuveen.com
■ MID-ATLANTIC & SOUTH	**Fred McAuley, CFA, CFP®** MD, Advisor Consultant	404.343.1523	fred.mcauley@nuveen.com
	John Hennessey AVP, Advisor Consultant	312.917.7908	john.hennessey@nuveen.com
	Chase Komatz AVP, Internal Advisor Consultant	312.917.8301	chase.komatz@nuveen.com
■ NORTHEAST	**John Hauck, CIMA®** MD, Advisor Consultant	617.512.8990	john.hauck@nuveen.com
	Joe McCaffrey AVP, Advisor Consultant	856.465.3115	joe.mccaffrey@nuveen.com
	Brett Pierson AVP, Advisor Consultant	847.691.7029	brett.pierson@nuveen.com
	Mark Johnston AVP, Internal Advisor Consultant	312.917.6966	mark.johnston@nuveen.com
	Andrew Abe Internal Advisor Consultant	312.917.8268	andrew.abe@nuveen.com

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