

November 26, 2007

New Suitor Sets Sights on Wealth Firms

by Tom Stabile

The wealth management sector has a new suitor, adding to a busy year for firms injecting capital into independent advisor shops. But unlike most “roll-up” or aggregator firms that have been buying up stakes in wealth managers, the latest entrant is not taking equity in the advisors.

The new deal involves New York-based Asset Management Finance (AMF) supplying capital to Chicago-based Gresham Partners in return for a limited-term share of revenues from the high-end wealth manager. Gresham advises on \$2.7 billion in assets for a slate of 65 ultra-wealthy investors, who average \$40 million per client. The firm’s minimum investment is \$20 million.

Wealth management firms seek capital from such outside investors in order to execute succession plans, acquire other outfits, develop new products, or make other transition- or growth-oriented moves. But because AMF seeks no equity in return for its capital infusion, it allows wealth management firms to retain control of their businesses – a feature that was attractive to Gresham, says Ted Neild, president of the firm. Gresham's management is using the proceeds of the deal to allow the second generation of executives to buy the ownership stake of Ben Beavers, the 10-year-old firm’s co-founder and chairman, who is 65.

“We’re taking equity and moving it to the second generation, and hopefully then to the third generation,” Neild says. “The challenge is that these firms have become so valuable.”

Neild says the deal also penciled out to be better than a standard bank loan, because the covenants, costs, and guarantees of that option were “onerous.” The financing deal has a seven-year payback window during which AMF can tap into Gresham’s revenue.

“It’s basically a form of financing, and with a seven-year amortization window, it’s probably a good deal for the younger advisor buying in,” says Mark Tibergien, CEO of Pershing Advisor Solutions of Jersey City, N.J. “It could have appeal to [registered investment advisors] and be competitive.”

AMF’s seven earlier deals have been with money management firms. It uses the same “Revenue Share Interests” model in which it provides capital to the asset management or wealth advisory firm and over a set timeframe collects a fixed percentage of the revenue. Overall, it has arrangements with firms that manage or advise \$40 billion in assets. While the Gresham deal is its first wealth manager, AMF expects to make more deals with multi-family offices and registered investment advisors (RIAs), says Sean Gally, v.p. of the firm.

“We’ve looked at wealth managers before,” he adds. “We always knew it would be a market that would fit with our strategy.” The firm expects to also make deals with alternative investment and mutual fund managers.

The model could have appeal to wealth managers, says Elizabeth Bloomer Nesvold, managing partner of Silver Lane Advisors, a New York-based investment bank. She introduced Gresham and AMF before the deal, and has worked with Gresham through her current firm and in prior professional stops.

“There are several banks that understand the nuances of these businesses and are willing to lend to fund transition plans, and there are a few sophisticated private equity firms that will take minority stakes in smaller businesses, but I’m not sure there is a pure play that ‘rents’ revenues for a finite period of time like the [AMF] model,” she adds. “It won’t work for all firms in all cases. AMF is looking for a certain return from future revenues, and that will dictate what funding will be made available.”

The roll-up model – in which aggregator firms often offer centralized resources and access to investment products – would still be appealing to some RIAs, she adds. Firms that haven’t built out their systems infrastructure, are stuck in terms of growth, or have challenges attracting the next generation might gain capabilities through the leverage that a roll-up can provide, she says.

In Gresham’s case, however, preserving control of ownership – and of the firm’s conflict-free advisory approach – was a primary goal, Neild says.

Under the deal, whose financial terms neither side would divulge, AMF will collect a fixed percentage of Gresham’s revenues during the seven-year time period, with the amount rising and falling based on the wealth firm’s fortunes. There is no guarantee of AMF receiving any specific dollar amount during the life of the contract, which makes it materially different from a loan, in which the bank or other lender expects to receive back the principal plus interest, AMF’s Gallyary says.

AMF’s deals have windows from seven to 20 years, and the average is around 11 years, says Barry Klayman, managing director of the firm. At the end of the contract period, the firm’s interest in the revenue expires. AMF has two business method patents pending regarding the structure of the technique, he adds.

Another difference from the roll-up market is that there are no formal connections between the firms within AMF’s network. Gresham, for instance, has no plans to use the asset management firms that already partner with AMF. The various AMF firms do partner informally, however, Klayman says.

The deal adds to a busy season in the wealth management sector. A few weeks ago, WealthTrust of Nashville, Tenn., acquired two RIA firms to bring client assets of its affiliated firms to \$8.6 billion. A few weeks earlier, United Capital Financial Partners of Newport Beach, Calif., brought its asset total to \$8 billion by acquiring four RIAs. And New York-based Focus Financial Partners unveiled five stake-buying deals in early October that put assets in its affiliated firms at \$25 billion.

All of the firms use different strategies and take varying levels of ownership stakes in wealth management shops.

Perhaps the closest aggregator in terms of its model to what AMF is doing is the approach by Fiduciary Network of Dallas, which has three firms with \$3.2 billion in client assets. That firm buys a non-voting equity stake in the wealth managers in a bid to provide capital while collecting a share of earnings over a fixed timeframe.