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New deal frees WealthTrust to chart own its course

Thomas Coyle - 14 November 2006

Private-equity firm **Circle Peak Capital** and junior capital provider **Falcon Investment Advisors** have backed the management buy-back and re-capitalization of wealth-management holding company **WealthTrust**, a subsidiary of regional brokerage **Morgan Keegan** and **Regions Financial**. WealthTrust, which has pulled in 10 affiliates in about seven years, says the deal means it can resume an ambitious acquisition strategy aimed at establishing itself as a national wealth advisory.

"We went looking for a private-equity partner so that we could expand geographically," says **Rusty Benton**, CEO of Nashville, Tenn.-based WealthTrust. "Morgan Keegan did not want us going outside its footprint, which is essentially the Southeast. With Circle Peak, we share a common goal of working to create and realize the company's value."

Benton, a 12-year veteran and co-founding principal of Brentwood, Tenn.-based asset manager **Weaver C. Barksdale & Associates**, founded WealthTrust in 1997 with the idea of buying equity in private-client investment advisories, re-branding them as WealthTrust affiliates and centralizing their compliance, human resources and other support services in the name of cost efficiency.

Within two years WealthTrust had made several acquisitions, and by the end of 1999 Memphis, Tenn.-based Morgan Keegan had agreed to help bankroll its regional growth strategy for a 50% stake in the company.

Through the next three years WealthTrust continued gobbling up advisories, primarily in the South and Midwest. But by 2003 the pace of mergers had slowed. In mid 2004, WealthTrust made its ninth acquisition overall and its last as a subsidiary of Morgan Keegan.

Benton says the slowdown was partly due to a general slowdown in the aftermath of the 2001 economic recession and the market meltdown that started in 2000 and continued through early 2003, and partly to the fact that WealthTrust had maxed out on its home turf.

"We can see there are a lot of firms out there nationally," says Benton. "That's why it was frustrating to be stranded geographically."

Morgan Keegan couldn't be reached for comment, but **Elizabeth Nesvold**, a managing director with New York-based investment bank **Cambridge International Partners** who helped broker the multi-party transaction between Morgan Keegan, its Birmingham, Ala.-based parent Regions and WealthTrust and its private-equity partners, says the brokerage "realized it had to make the determination to be in this business whole heartedly or to find the right home for management to expand as aggressively as their model warranted."

R. Adam Smith, New York-based Circle Peak's managing partner says his firm's deal with WealthTrust "best the elements of the partnership model" -- typified in the asset-management realm by **Affiliated Managers Group's** (AMG) holding-company strategy -- "with a complementary set of services and products for partner firms to enhance and broaden their offering to clients."

Smith's emphasis on the end-client isn't just lip service. Circle Peak is focused on consumer-driven industries like fitness, food, medical devices and -- says Adam -- private-asset management.

Between January 2000 and July 2006 there were 228 merger transactions involving independent investment advisories with an aggregate price-tag of \$1.5 billion, according to a new study sponsored by Jersey City, N.J.-based clearing firm **Pershing** and conducted by Seattle-based business consultancy **Moss Adams**.

Lucky few

A 2005 study by **JPMorgan Asset Management's Undiscovered Managers** says that independent advisors have to contend with two main trends over the next 10 to 20 years. One is general attrition as an aging population of firm owners sell or shutter their firms as a prelude to retirement. The other is a growing gulf between "have" and "have not" firms.

Have-not firms may compensate their owners quite well, but they lack the resources to underwrite expansion or to react nimbly to changes in the marketplace, according to Undiscovered Manager's ***Back to the Future*** report. So as the advisory space becomes more rationalized through improved technologies and more robust performance reporting, have-not firm owners will have to run harder just to stay put.

"[The have-not] group includes about 94% of all industry participants and all of those firms [with] less than \$25 million [in] assets under management," says the 2005 study. "A majority of the industry's mid-sized participants also fall into the have-not category because they too are unprofitable as businesses despite operating at or near capacity." The have-not category also includes "firms that generate between \$1 million and \$3 million in annual revenues but have unattractive client bases or are inefficient."

The haves meanwhile are "mid-sized firms with annual revenues of \$1 million to \$3 million, and a small percentage of organizations that have less than \$1 million in annual revenue but more than \$25 million of assets under management," according to ***Back to the Future***. "Although not yet large companies, these mid-sized firms have robust client bases, are profitable and have the resources to grow their organizations over time."

Another theme of the Undiscovered Managers study is that the divide between have and have-not firms will widen as the haves, pressured by large competitors, coalesce through merger and acquisition into a group of 40 or 50 highly profitable organizations, each with at least \$15 billion in assets under management, that look rather like multi-family offices for the mass affluent.

The newer Pershing study says that investment-advisory consolidators accounted for 21% of the merger transaction in the space last year. Typically, these acquirers look for motivated partners with excellent track records and strong growth potential, and principals who believe in the national holding-firm model and want to keep running their practices -- at least through a reasonable and mutually accepted transition period.

With its holding company approach and its focus on advisories catering to clients in the \$2 million to \$5 million in investable assets, it's pretty clear that WealthTrust wants to one of these middle-market "have-firm" aggregators.

"Our goal is to create a national wealth-management firm that's not a bank, not a brokerage, not an insurance company or a mutual-fund company, but a fee-based advisory," says Benton. "I think there's room for an independent company like that to serve the needs of a growing client base."

Benton says outfits like **Boston Private Financial Holdings**, which has 14 private-banking or wealth-advisory **affiliates**, and **Mellon's Private Wealth Management** group, another serial consolidator, don't conform to his ideal because of their origins as banks.

"Banks want to own 100% of the firm and fold it into their operations," Benton told *Investment Advisor Magazine* in 2004. "This means the advisor has to start managing money the way the bank wants."

Track record

New York-based **Focus Financial Partners**, which got a \$35-million investment from Boston-based private-equity firm **Summit Partners** late in 2005 and went on to acquire its first six advisory affiliates this year, may be more analogous to WealthTrust.

Like Focus, WealthTrust helps its affiliates' founders partially monetize their business equity, offers them help with later-stage succession planning and provides firm-wide infrastructure cost savings. In essence, both holding companies seek to consolidate on its affiliates' behalf anything that can be consolidated.

"What has to be local is portfolio management, research and client service," says Benton. "Beyond that nobody cares who pays the bills or if the reporting comes from here [in Nashville] - especially if it helps everyone keep costs down."

Ben Phillips, a managing director in **Putnam Lovell NBF's** New York-based investment-banking practice, says that Summit's investment in Focus is an early indication of private equity interest in private-client advisory as distinct from an established attraction to pure-play high-net-worth asset management and retail-oriented investment-platform providers.

For one thing, venture capitalists have come to see that investment advisories aren't very capital intensive by broad industry standards and they "throw out a lot of cash" even in down cycles, making them fairly attractive places to park cash, according to Phillips.

Mainly though, if private-equity firms are indeed glancing appreciatively at advisory collectives it might be because there are few others left to flirt with. "There's a \$300-billion overhang in private equity right now," says Phillips. "That's money they've yet to invest."

In his year-long search for venture backing Benton says he encountered "a tremendous amount of interest" from potential investors. But he says that wasn't as much because they had cash burning holes in their pockets as much as it was a response to WealthTrust's track record.

"We made our first acquisition in 1999 and we've done 10 transactions since then," says Benton. "We know how to partner with these firms and how to manage them."

Cambridge International's Nesvold has seen evidence of WealthTrust's superior management skills in the protracted run-up to its buy-out from Morgan Keegan. "[WealthTrust] did an incredible job balancing multiple parties' objectives -- including its own -- in one of the most complicated transactions on record," she says. "They've done right by their past partners and will do right by their new capital partners and future acquisitions."

And future transactions won't be long in coming, says Benton. The tenth WealthTrust acquisition he mentions -- that of Scottsdale, Ariz.-based **DeGreen Wealth Management** -- in fact followed the Circle Peak deal this week.

"You can look at DeGreen as a model for the kind of acquisitions we'll be pursuing," says Benton. "That's both in terms of the kind of firm and the aspect of geographic expansion."

WealthTrust's other affiliates are Memphis-based **Delta Asset Management**, St. Louis-based **WealthTrust · DunckerStreett**, Bethesda, Md.-based **WealthTrust · FBB**, Greenwood, S.C.-based **Greenwood Capital Associates**, Louisville, Ky.-based **Harvey Investment Company**, Richmond, Va.-based **Kanawha Capital Management**, **Optimum Investment Advisors** with offices in Chicago, Dallas and San Francisco, Norfolk, Va.-based **Wilbanks Smith & Thomas Asset Management** and **WealthTrust Advisors**, which has offices in Charlotte, N.C., Nashville and Paducah, Ky.

DeGreen Wealth Management will be re-branded as **WealthTrust Arizona**. -FWR