

NASHVILLE NOTES

Things Change

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By Jeff K. Davis

Jeff Davis is a veteran bank analyst. The views and opinions expressed in this piece are those of the author and do not necessarily represent the views of S&P Global Market Intelligence; Mercer Capital, where Davis is the managing director of the financial institutions group; or StillPoint Capital, where Davis is a registered representative.

In the spring of 2000, I worked with [Pinnacle Financial Partners Inc.](#) management on projections for a capital raise that were later presented to the commitment committee for JC Bradford & Co., where I was then the regional bank analyst. It was a different era: Analysts could work on investment banking deals as long as it was not a covered company, and de novo banks then sometimes raised capital via underwritten IPOs, as Pinnacle would do.

I told the commitment committee that the projections were a stretch, but the game plan of hiring ex-colleagues who were top producers at First American — where the Pinnacle executives worked when First American agreed in mid-1999 to merge with AmSouth (today Regions Financial) — should be successful.

Within a couple of years, the plan proved to be a phenomenal success, helped in part by inept execution by AmSouth management, super execution by Pinnacle and steady growth in the Nashville area. The projections that I thought were a stretch were decidedly too conservative.

Over the ensuing roughly 25 years, Pinnacle management rewarded shareholders with great execution and mostly organic growth while fielding periodic questions about the company's 49% interest in Bankers Healthcare Group. The shares rose from a split-adjusted IPO price of \$5 per share to an all-time high of about \$130 per share last year in the post-election bank stock frenzy.

Things change, however.

The verdict of the market, so far, is that the boards of Pinnacle Financial Partners and Synovus Financial Corp. made a mistake.

Pinnacle's [merger of equals](#) with [Synovus Financial Corp.](#) caught the market by surprise: Pinnacle's share price dropped nearly 22% from July 21, the day before Bloomberg ran a story that Synovus was talking to potential acquirers, through July 25, the first day of trading after the [merger was announced](#). The combined market cap of the companies' common equity declined to \$13.9 billion from \$16.7 billion. No doubt the bankers told both boards to expect pressure on the stocks, but not to this extent.

With questions about CEO succession and a high-growth Southeast footprint, Wall Street had designated Pinnacle as a seller, not a buyer or merger partner. I am sure there is a story, but it is not clear to me why there was not a clear internal successor to President and CEO Terry Turner inside the company.

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My take on board duties is that directors are to act in good faith and to execute duties of "care" (informed decision-making) and "loyalty" (i.e., shareholder interests over theirs and disclosure of any conflicts). Boards have substantial latitude in directing a corporation's affairs when they adhere to their duties, whether the board made the right decision or time proves the decision to be wrong or even disastrous.

Boards are to pursue policies that maximize shareholder value, but that does not mean next quarter or next year; it is a long-term view. To that point, [Holdco Asset Management LP](#) and two prominent analysts recently [raised questions](#) about [Comerica Inc.](#)'s long-term value-creation record and whether the company has [earned the right](#) to remain independent.

The form of consideration matters, too, when board decision-making involves a merger. Cash deals will entail a process to obtain the best price. There is more leeway with stock deals, however. Shareholders will continue to own shares in a merged company that may or may not produce more value than the standalone entities. Boards will not know the future performance; all they can do is make an informed decision.

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The negative reaction to the Pinnacle-Synovus merger is not about whether the exchange ratio was too generous to Synovus; rather it is primarily about the transaction itself, in which a growth company will merge with a slower-growing company with a different business model.

Immediately before Bloomberg published its story, Pinnacle was trading around 14x the next 12 months consensus earnings per share. Pinnacle shares now trade for less than 11x next 12 months EPS and roughly 9x 2027 EPS, when synergies should boost earnings. It is a pedestrian valuation for what has been a long-term growth stock. Investors have concluded that the decision to merge has diluted growth and increased the risk profile.

The one outcome that the market is not giving much weight to at this point is the possibility that the MOE will work — which it might.

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