

VALUE FOCUS

Investment Management

Fourth Quarter 2023 | Segment Focus: Wealth Managers

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This quarter we take an in-depth look at the trends affecting wealth managers and the broader RIA industry, including the performance of publicly traded investment management firms and deal activity across the sector.

In the public markets, traditional asset and wealth managers performed well in Q4, although they underperformed all other RIA sectors and the S&P 500 for the last year.

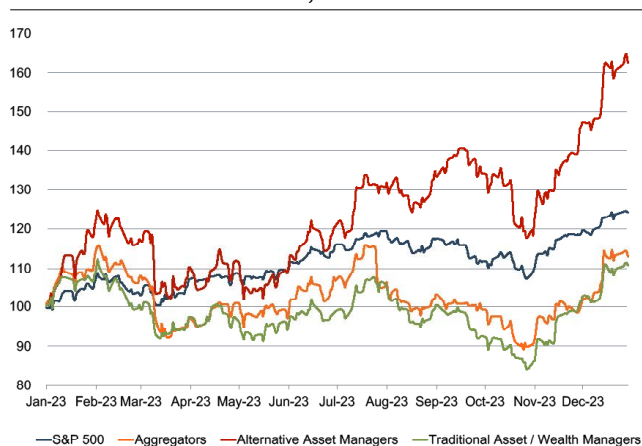
In the private market, deal count has declined modestly since the end of 2021, although total value has remained stable over the last year as average deal size has increased and multiples have held up reasonably well.

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Segment Focus: Wealth Managers

As the financial landscape continues to evolve, the RIA industry experienced a notable shift in 2023, diverging from the challenges faced in the preceding year. Despite predictions going into 2023 that persistent inflation and elevated interest rates would lead to an economic downturn, no recession came to pass, and all sectors of the RIA industry appreciated as markets rebounded from the 2022 slump.

Investment Manager Performance by Sector Year Ended December 31, 2023



Source: S&P Market Intelligence

Given the direct impact of the stock market on Assets Under Management (AUM) balances and the inherent operating leverage in the RIA model, investment manager performance tends to closely follow market trends. Public firms with substantial operations in the wealth management space were up 11% year-over-year, underperforming the broader market (the S&P 500 was up 24%) and alternative asset managers (up 62%). This is in stark contrast to the downtrend seen for much of 2022, where traditional asset managers and the broader market were down 27% and 19%, respectively.

Despite favorable market performance in 2023, the year ahead presents several challenges for the RIA industry. Although inflation has begun to subside, interest rates remain at a 15-year high, and the Federal Reserve has been hesitant to confirm rate cuts in 2024. In a recent interview,

Federal Reserve Governor Christopher Waller said that lowering interest rates will need to be “carefully calibrated and not rushed.”

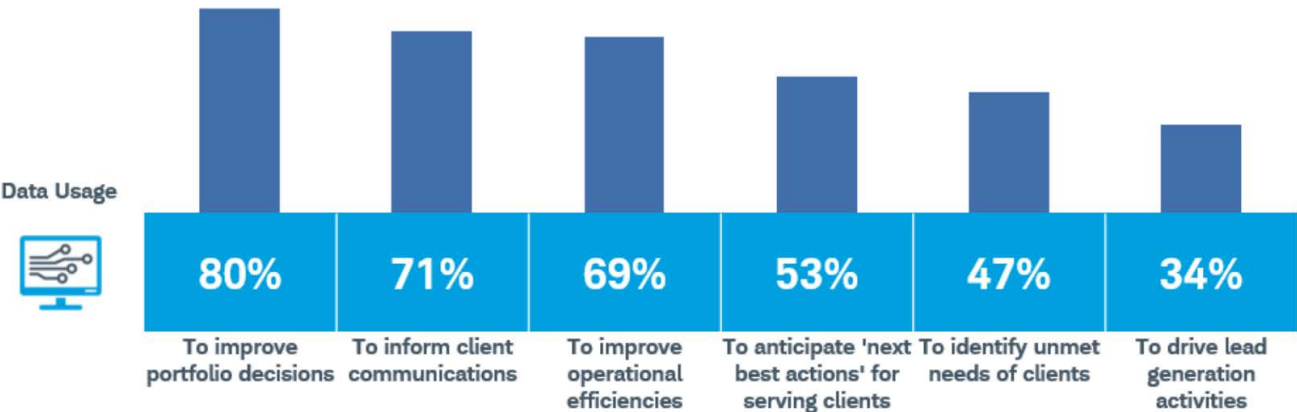
Valuations may face additional pressure as elevated interest rates result in higher yields for other income-producing assets (making them a more attractive alternative to investing in RIAs), and the cost of capital increases on both the equity and debt sides of the equation for leveraged consolidators of wealth management firms. While facing uncertainty heading into 2024, it will be important for wealth management firms to have a strategy in place to navigate these challenges and capitalize on opportunities that may arise.

Against this backdrop, the role of data has become increasingly prominent, offering new avenues for growth, scale, and service. Industries across various sectors are unlocking opportunities through advanced data utilization, and RIAs are no exception. Schwab's annual survey of wealth management firms confirmed this sentiment, with over 76% of respondents saying data use provides the opportunity to serve their clients better. In practice, a significant number of advisors are already harnessing data insights: 80% leverage data for improved portfolio decisions, and 69% utilize it to enhance operational efficiencies.



Beyond operational enhancements, the study reveals the transformative impact of data on the client-advisor relationship. Experts interviewed emphasize how data can inform the customization of offerings, anticipate client needs, and foster greater client engagement in the wealth planning process. A substantial portion of RIAs (47%) currently use data to identify unmet client needs, with another 39% planning to

do so in the next three years. Furthermore, 53% are currently tapping into data to anticipate the ‘next best actions’ for client service, with 35% planning to do so in the near future. Successfully leveraging these resources to improve client service and lead generation can translate into improved client retention and organic growth.



Source: Spring 2023 Schwab Advisor Services Independent Advisor Outlook Study

Performance of Publicly Traded Asset / Wealth Management Firms

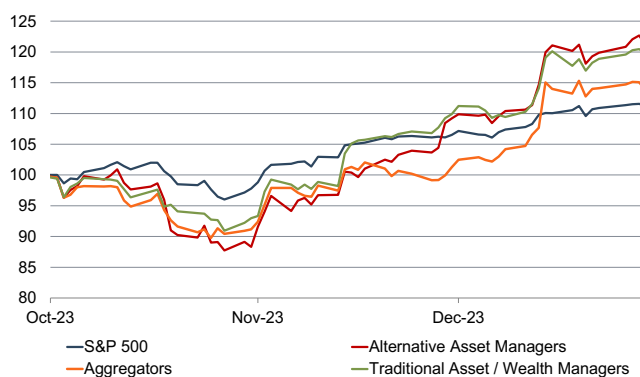
Share prices for most publicly traded asset and wealth management firms trended upward with the broader market during Q4 2023. For the second quarter in a row, alternative asset managers outperformed the market and other RIAs, ending the quarter up about 21% compared to 11% for the S&P 500. On a year-over-year basis, all sectors of RIAs appreciated as the markets rebounded from the 2022 turn. RIAs directly benefit from improving market conditions as they result in a stronger asset base on which to collect fees.

Performance by Sector

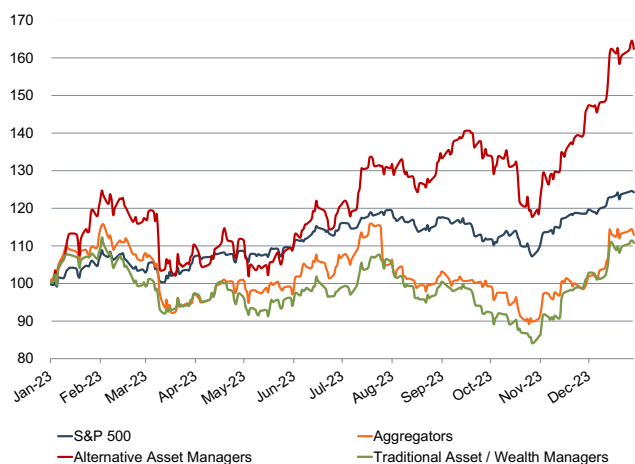
The market uptick in Q4 translated to increased prices for most public RIAs. Prices for alternative investment and traditional asset managers experienced a stronger increase than the S&P 500. In the last twelve months, most RIA sectors saw a decline in year-over-year revenue despite rising AUM reflecting fee compression. Year-over-year price performance showed this, with aggregators and traditional asset managers underperforming the S&P 500 in 2023. Notably, however, alternative asset managers outperformed for the year. Market volatility since 2020 is one of the factors

responsible for the increased demand for alternative asset manager stocks. Private equity funds and other alternative investment vehicles typically lock in assets for ten to twelve years, leading to a more predictable and stable revenue stream that is less correlated with the broader market.

Investment Manager Performance by Sector Q4 2023



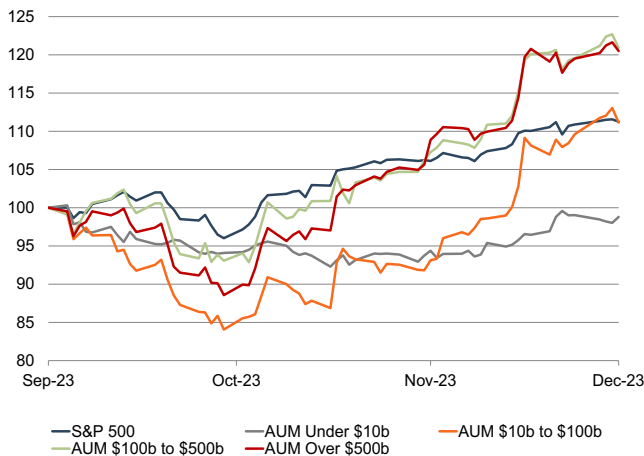
Investment Manager Performance by Sector 2023



Performance by Size Category

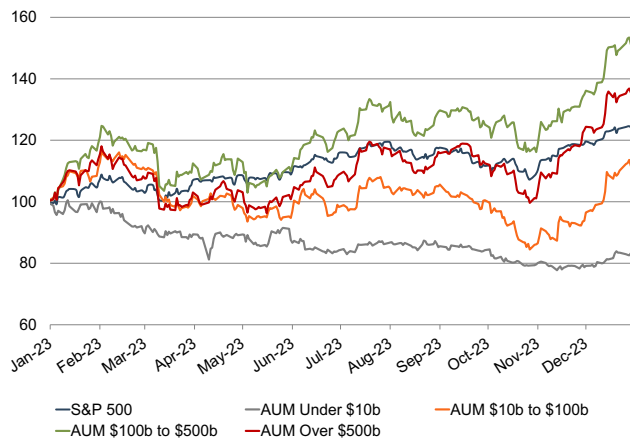
RIA performance during Q4 varied by AUM size. Larger RIAs (those with AUM over \$100B) outperformed the S&P 500, RIAs with AUM between \$10B and \$100B performed on par with the S&P, and the smallest RIAs (those with AUM under \$10B) underperformed. Similar trends exist for the full year 2023. The smallest RIAs depreciated in 2023, whereas all other RIA size groups and the S&P increased in value over this time.

Investment Manager Performance by AUM Size
Q4 2023



Source: S&P Market Intelligence

Investment Manager Performance by AUM Size
2023

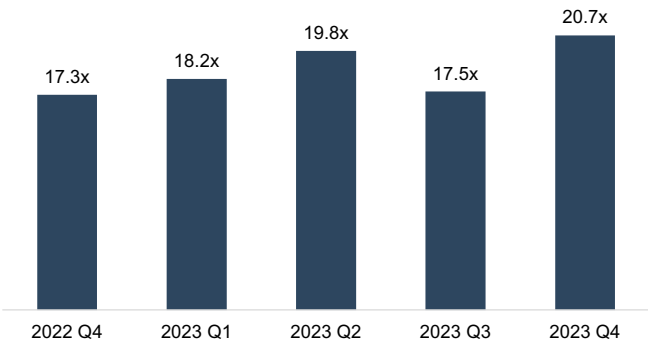


Source: S&P Global Market Intelligence

Pricing Trends

The median LTM earnings multiple for publicly traded asset and wealth management firms increased 18.3% during the fourth quarter of 2023. After trending downwards for most of 2022, multiples began to increase during the first half of 2023 as LTM earnings metrics began to fully reflect the impact of 2022 market conditions. The multiple increase in Q4 represents a recovery from the short-lived Q3 trough inflicted by price declines.

Price to LTM EPS for Traditional Asset /
Wealth Managers

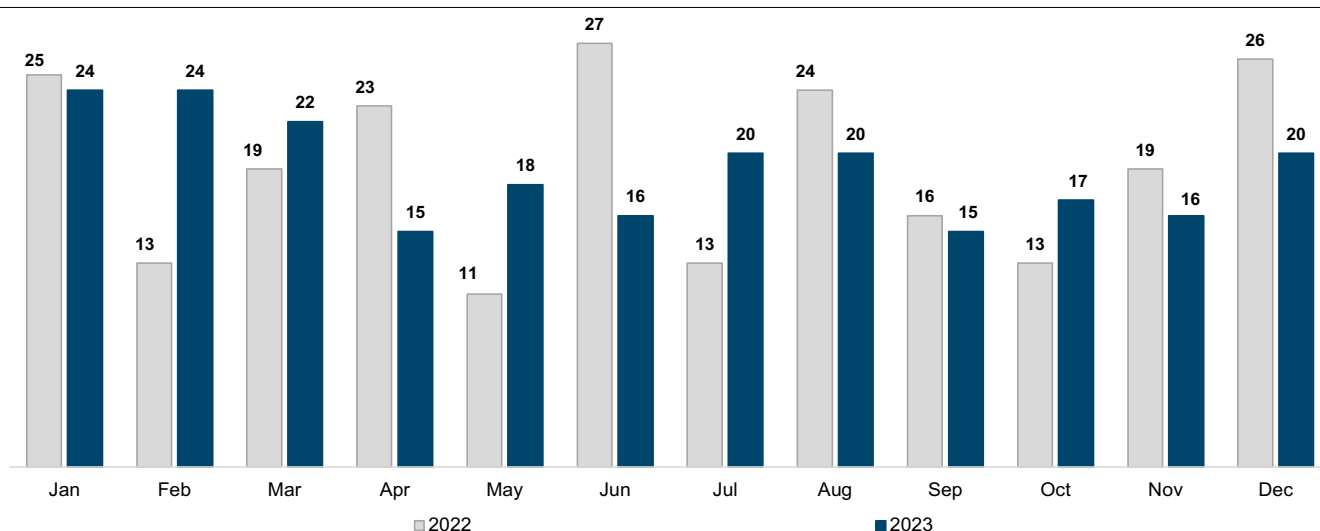


Source: S&P Market Intelligence

RIA M&A

Fourth Quarter 2023

Number of RIA M&A Transactions, 2022 vs 2023



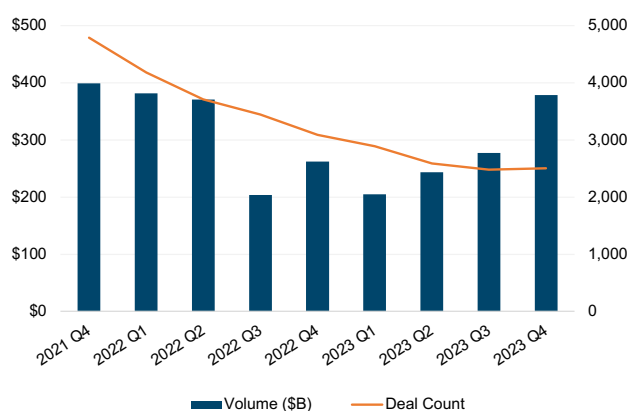
Source: Fidelity

RIA M&A activity has demonstrated remarkable resilience, defying initial expectations of a slowdown amid challenging macroeconomic conditions. As the economy entered 2023 facing high inflation, rising interest rates, and tight labor markets, many anticipated a decline in M&A activity. However, Fidelity's November 2023 Wealth Management M&A Transaction Report listed 210 deals through November 2023, up 3% from the 203 deals executed during the same period in 2022. Notably, there was a significant uptick in total transacted AUM during 2023. Total transacted AUM through November 2023 was \$336.6 billion—a 25% increase from the same period in 2022.

While deal volume for 2023 has been roughly in line with 2022 levels, there was a notable slowdown during the second quarter of 2023 as total transactions fell approximately 20%. Deal volume recovered in the second half of the year, with 90 deals from July to November, representing a 6% year-over-year increase in deal count. Per **Echelon Partners'** recent report, "We attribute this increase to the continued influence of fundamental forces driving consolidation in the industry and to buyers and sellers gaining greater confidence in the macroeconomic environment."

Relative to the broader M&A market, RIA deal activity has been exceptionally robust. The overall M&A transaction value for all industries (excluding the RIA industry) decreased 9% year-over-year through the fourth quarter of 2023 (per Bloomberg).

Global M&A Activity (Excluding RIA Industry)



Source: Bloomberg

In contrast, RIAs' total transacted AUM (a proxy for transaction value) increased by 25%. The average AUM per transaction during 2023 was \$1.6 billion, a 21% increase over the prior year. The increase in deal size has been an encouraging sign, given the rise in the cost of capital over the past year. Echelon's RIA M&A Deal report stated that the growth in deal size can primarily be attributable to "an increase in equity markets and the consistent deployment of newly raised capital by firms like Mercer Advisors, Corient, HUB International, and CAPTRUST. Echelon estimates that large wealth platforms raised an incremental ~\$7.2 billion to pay down debt, increase war chests for acquisitions, and invest in growth."

Another contributor to the increase in deal size has been RIAs partnering with private equity firms. According to Fidelity's November 2023 Wealth Management M&A Transaction Report, private equity backing was involved in 94% of the transactions in November. Private equity acquirers directly invested in wealth managers with assets totaling \$877 billion in the third quarter of 2023, more than tripling the amount in the second quarter of 2023 (per Echelon's Q3 2023 RIA M&A Deal Report). This increase was due to some of the largest wealth management consolidators taking on new private equity partners. Notable transactions of this nature include **CAPTRUST**, which sold an undisclosed stake in its wealth management business to Carlyle Group; **Prime Capital Investment Advisors**, who received a minority investment from Abry Partners; and **Titan Wealth Holdings**, who sold an interest in its business to Parthenon Capital.

The prevalence of serial acquirers and aggregators has continued in the RIA M&A market. In recent years, the professionalization of the buyer market and the entrance of outside capital have driven demand and increased competition for deals. Serial acquirers and aggregators have increasingly contributed to deal volume, supported by dedicated deal teams and access to capital. Such firms accounted for approximately 68% of transactions during 2023. Waverly Advisors, Wealth Enhancement Group, and Focus Financial Partners all completed multiple deals during the fourth quarter.

Deal activity has also been supported by the supply side of the M&A equation, as the impetus to sell is often based on more than market timing. Sellers are often looking to solve succession issues, improve quality of life, and access organic growth strategies. Such deal rationales are not sensitive to the market environment and will likely continue to fuel the M&A pipeline even during market downturns.

What Does This Mean for Your RIA?

For RIAs planning to grow through strategic acquisitions: Pricing for RIAs has trended upwards in recent years, leaving you more exposed to underperformance. While the impact of current macro conditions on RIA deal volume and multiples remains to be fully seen, structural developments in the industry and the proliferation of capital availability and acquirer models will likely continue to support higher multiples than the industry has seen in the past. That said, a long-term investment horizon is the greatest hedge against valuation risks. Short-term volatility aside, RIAs continue to be the ultimate growth and yield strategy for strategic buyers looking to grow their practice or investors capable of long-term holding periods. RIAs will likely continue to benefit from higher profitability and growth than their broker-dealer counterparts and other diversified financial institutions.

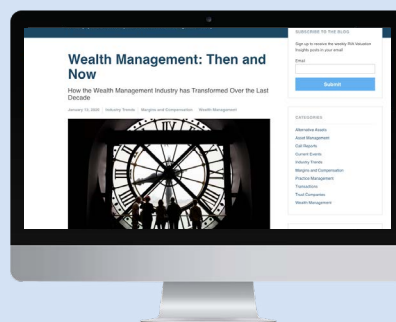
For RIAs considering internal transactions: We're often engaged to address valuation issues in internal transaction scenarios, where valuation considerations are top of mind. Internal transactions don't occur in a vacuum, and the same factors driving consolidation and M&A activity have influenced valuations in internal transactions as well. As valuations have increased, financing in internal transactions has become a crucial secondary consideration where buyers (usually next-gen management) lack the ability or willingness to purchase a substantial portion of the business outright. As the RIA industry has grown, so too has the number of external capital providers who will finance internal transactions. A seller-financed note has traditionally been one of the primary ways to transition ownership to the next generation of owners (and, in some instances, may still be the best option).

Still, an increasing amount of bank financing and other external capital options can provide selling partners with more immediate liquidity and potentially offer the next-gen cheaper financing costs.

If you are an RIA considering selling: Whatever the market conditions are when you go to sell, it is essential to have a clear vision of your firm, its value, and what kind of partner you want before you go to market. As the RIA industry has grown, a broad spectrum of buyer profiles has emerged to accommodate different seller motivations and allow for varying levels of autonomy post-transaction. A strategic buyer will likely be interested in acquiring a controlling position in your firm and integrating a significant portion of the business to create scale. At the other end of the spectrum, a sale to a patient capital provider can allow your firm to retain its independence and continue operating with minimal outside interference. Given the wide range of buyer models out there, picking the right buyer type to align with your goals and motivations is a critical decision that can significantly impact personal and career satisfaction after the transaction closes.

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A weekly update on issues important to the Investment Management industry.



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Investment Manager Multiples by Sector

				Pricing as of December 31, 2023			
	Ticker	12/31/2023 Stock Price	% of 52 Week High	Price / Trailing EPS	Price / Forward EPS	Enterprise Value / AUM (%)	Enterprise Value / EBITDA
TRADITIONAL ASSET / WEALTH MANAGERS (AUM UNDER \$250B)							
Diamond Hill Investment Group, Inc.	DHIL	165.59	85.7%	17.6x	nm	1.83%	11.0x
GAMCO Investors, Inc.	GAMI	19.11	87.7%	10.9x	nm	1.19%	nm
Hennessy Advisors, Inc.	HNNA	6.71	66.1%	12.4x	nm	1.00%	4.6x
Silvercrest Asset Management Group Inc.	SAMG	17.00	73.3%	23.9x	12.1x	0.66%	7.8x
Virtus Investment Partners, Inc.	VRTS	241.76	97.4%	16.3x	11.0x	1.05%	8.2x
Artisan Partners Asset Management Inc.	APAM	44.18	96.2%	24.6x	15.7x	2.98%	13.2x
Victory Capital Holdings, Inc.	VCTR	34.44	97.8%	12.7x	7.7x	2.02%	7.9x
BrightSphere Investment Group Inc.	BSIG	19.16	71.3%	12.3x	11.7x	0.97%	7.0x
WisdomTree, Inc.	WT	6.93	91.8%	21.3x	19.1x	1.33%	17.0x
AITi Global, Inc.	ALTI	8.76	31.9%	10.3x	292.0x	3.17%	nm
Westwood Holdings Group, Inc.	WHG	12.57	88.5%	58.9x	nm	0.38%	7.9x
Group Median			87.7%	16.3x	12.1x	1.19%	7.9x
TRADITIONAL ASSET / WEALTH MANAGERS (AUM OVER \$250B)							
BlackRock, Inc.	BLK	811.80	99.1%	31.9x	22.0x	1.36%	18.2x
Federated Hermes, Inc.	FHI	33.86	74.3%	13.3x	10.3x	0.37%	6.7x
Franklin Resources, Inc.	BEN	29.79	86.7%	16.2x	12.6x	1.15%	7.6x
Janus Henderson Group plc	JHG	30.15	96.3%	19.4x	12.9x	1.23%	8.1x
Affiliated Managers Group, Inc.	AMG	151.42	83.8%	13.4x	8.2x	1.19%	7.0x
Invesco Ltd.	IVZ	17.84	86.8%	10.1x	12.5x	0.92%	10.3x
T. Rowe Price Group, Inc.	TROW	107.69	81.1%	17.5x	14.5x	1.66%	8.9x
Group Median			86.7%	16.2x	12.6x	1.19%	8.1x
ALTERNATIVE ASSET MANAGERS							
Apollo Global Management, Inc.	APO	93.19	96.8%	nm	14.2x	9.89%	nm
Ares Management Corporation	ARES	118.92	98.3%	236.3x	33.4x	9.74%	31.4x
Associated Capital Group, Inc.	AC	35.71	85.4%	nm	nm	24.81%	nm
Blackstone Inc.	BX	130.92	98.0%	111.9x	33.5x	11.29%	nm
The Carlyle Group Inc.	CG	40.69	95.8%	131.4x	12.9x	5.83%	nm
Cohen & Steers, Inc.	CNS	75.73	96.0%	33.1x	27.1x	4.77%	20.2x
Hamilton Lane Incorporated	HLNE	113.44	97.0%	105.3x	30.8x	4.01%	18.4x
KKR & Co. Inc.	KKR	82.85	96.7%	40.2x	24.5x	26.07%	nm
Group Median			96.8%	108.6x	27.1x	9.82%	20.2x
OVERALL MEDIAN			90.2%	18.5x	14.2x	1.51%	8.2x

Mercer Capital's Investment Management Industry Expertise

Mercer Capital provides RIAs, independent trust companies, and alternative asset managers with business valuation and financial advisory services related to corporate disputes, litigated matters, tax compliance, and financial reporting requirements. Mercer Capital also provides transaction advisory and consulting-related services.

Mercer Capital provides a comprehensive suite of valuation and financial advisory services to meet your needs. Experience includes:

- Corporate valuation services for clients ranging from start up managers with as little as \$50 million in assets under management to established industry leaders managing over \$400 billion
- Litigation support services and expert witness testimony in matters involving economic damages, shareholder disputes, and marital dissolution
- Transaction advisory services involving investment managers from sell-side, buy-side, and mutually retained perspectives
- Providing financial statement reporting services related to purchase price allocation and goodwill impairment testing
- Assisting RIAs and other investment managers with annual ESOP valuations, fairness opinions, and appraisals for gift and estate tax compliance

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