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More M&A heat, but no fire yet

By Ed Moisson 26 May 2020

Discussions about potential mergers and acquisitions among asset managers are “hotting up” through the coronavirus-related crisis, with expectations rising that more deals will be completed as a result.

European mutual funds have suffered record outflows this year as the crisis spread across the continent, resulting in an estimated hit to firms’ annual revenues of €11.5bn.

Depressed assets under management have compounded the cost pressures active fund houses were already dealing with before the crisis.

Many listed asset managers’ share prices have not recovered from the falls they suffered two months ago, despite improving over the succeeding weeks.

Dean Frankle, UK asset management lead at Boston Consulting Group, says: “Conversations [about M&A] are definitely hotting up.”

Mr Frankle says he believes there will be “more M&A”, adding that for firms “going shopping, things are cheaper”.

Firms with “deep pockets” are thinking this could be a good time to find firms that offer revenue-generating synergies, he says.

These synergies can come either from investment capabilities, such as private assets, or from distribution, such as having a sales presence in a particular market.

Asset managers are “not rushing around” to find acquisitions, but looking for targets that offer “clear logic” at a time when organic growth is “tough” for most firms.

He says: “There is excess capacity in the industry and there are scale benefits in pretty much all underlying drivers of a business. This is not always for creating a trillion-dollar business, but scale where it matters, [such as] in a core investment competency.”

Jonathan Doolan, head of Europe, the Middle East and Africa at consultancy Casey Quirk, says that early in the crisis he had “lots of conversations” with private equity and asset managers about potential M&A deals.

However, the increased interest in acquiring asset managers is not yet translating into the prospects of deals completing, experts say.

“The fruit is just not ripe enough yet. It’s not yet falling from the tree,” Mr Doolan says.

Larger firms with depressed asset values are aiming to “just hold on” through the crisis and wait for asset values to rise, unless they have a “really serious debt issue”, he says.

Kevin Pakenham, co-founder of Pakenham Partners, an independent M&A consultancy, agrees, saying: “The fall in markets and pressure on revenues increase enthusiasm for consolidating acquisitions, either as an offensive or defensive strategy. This turns up the volume of M&A discussions.”

“But increased market uncertainty makes fair value harder to establish and makes transactions harder to complete,” he says.

As a result, Mr Pakenham says: “If markets rally, we shall see more M&A. If not, not.”

Ray Soudah, chairman and founding partner of MilleniumAssociates, an M&A advisory firm, says: “Most such mergers occur when share prices are high and boards of directors see only sunlight all around, rather than the current cloudy skies.”

If acquisitions do take place, then “pickings will be slim”, and limited to small and mid-sized acquisitions, according to Mr Doolan.

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He says captive asset managers – those owned by banks or insurers – are among those more likely to look for acquisitions.

Captive fund houses that fail to demonstrate the benefits of active fund management through the crisis may respond to the pressure of Mifid II's evolving suitability requirements by looking for acquisitions.

"Captive managers may open up their purse strings to buy high-quality investment capabilities," Mr Doolan says.

Meanwhile, Mr Soudah says it is a "false view" for large asset managers to think that merging with peers or smaller firms will "solve their challenges".

"Theoretical cost-cutting synergies" often lead to "significant client defections" given the disruptions "frequently experienced" from mergers or takeovers, he says.

"Serious players will no doubt be considering their options but the majority are best advised to stay calm, and focus on existing client retention and technology-driven efficiencies," he adds.

Additional reporting by Dawn Cowie.

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