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YourQ&A: Will Credit Woes Spur Manager Mergers?

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Question:

BlackRock's Larry Fink says the asset management industry is in store for dramatic consolidation due to the ongoing disruption in the markets (for *FUNDfire* article, see below). Do you expect the current market disruption will spur intense consolidation?

From Advisor, Service Provider, Northeast

Answer:

Elizabeth Bloomer Nesvold is managing partner of Silver Lane Advisors, an M&A advisory firm specializing in the investment and wealth management industries.

The industry has been consolidating since the repeal of the Glass-Steagall Act—which paved the way for increased Wall Street mergers—with peak activity of 204 transactions recorded in 2007. Larry Fink's comment is best highlighted by the bust up of Bear Stearns, cherry picked for its prime broker, asset manager and digs on Madison Avenue. However, the empirical evidence suggests that recent activity is driven by a flight to quality, rather than quantity, and that the small- to mid-sized players are the more likely targets for consolidation.

After a tough lesson from the Fed, Wachovia, Lehman and UBS were proactive in raising money to avoid a similar fate. National City is reportedly raising capital and Jeffries also announced the sale of a "strategic interest" to Leucadia National. These examples are counter-evidence that the big guys are ready to fall, and suggests they aspire to be the consolidator, not the consolidated. If there is another shock to the financial system, we will undoubtedly see some larger players consolidate.

In terms of growth, larger firms tend to "revert to the mean," which supports the notion of acquisition. BlackRock, however, continues to defy the odds, racking up an impressive 20.6% increase in assets over 2007. A small percentage was attributable to the Quellos acquisition—a $22 billion fund-of-funds. The BlackRock-Quellos combination is representative of the kind of acquisitions we will continue to witness as we close out this decade.

YourQ&A is your opportunity to get your pressing questions answered by industry leaders.

BlackRock CEO Sees Industry Consolidating

By Pete Bucci

Published on Apr 17, 2008

The CEO of BlackRock[1] says he sees the asset management industry going through significant consolidation in the wake of the credit crisis. **Laurence Fink**, BlackRock's chairman and CEO, made his comments while announcing that the firm saw a rise in first-quarter profit as managed assets increased, Reuters reports.

However, first-quarter profit declined from the fourth quarter of 2007. The firm was cautiously optimistic about its performance for the rest of year, noting that its business is diversified and there is a record level of $105.8 billion in new business on the way, as of April 14.

BlackRock shares fell in the wake of the report, while other fund managers saw significant gains, Reuters reports. However, analysts see positive signs for BlackRock in 2008, and some say less diversified firms that have bigger woes will post weaker results.

Fink expects companies hurt by low price-to-earnings ratios or declining asset quality to look to shed asset management businesses. He said BlackRock itself would be selective going forward in making acquisitions.

First-quarter net income was $242 million, or $1.82 per share, compared to $195.4 million, or $1.48 per share, a year ago. According to BlackRock, first-quarter earnings included a non-operating loss of 12 cents a share, net of controlling interest, from losses on seed capital investments in hedge funds and real estate.

In the fourth quarter of 2007, BlackRock earned $2.43 a share, Reuters reports.

Acquisitions fueled an 18% jump over the previous year in managed assets, which rose to $1.3 trillion as of the end of March. The firm bought Quellos Group[2]'s fund of funds business for $1.7 billion last year.

Meanwhile, Reuters reports, hedge fund performance fees fell to $42 million in the first quarter from $153 million in the fourth quarter. BlackRock says that was primarily because there were fewer performance fee contracts with performance measurement periods that end in the first quarter.

In the first quarter, BlackRock took in $35.2 billion in net new business, with its cash management business seeing most of the net inflows.

BlackRock is managing $30 billion in Bear Stearns[3] assets as part of the Federal Reserve[4]'s bailout of the investment bank. Fink says it is negotiating with a number of other firms to come up with remedies for its distressed assets.

According to Fink, BlackRock is vying for two mandates worth more than $20 billion in total.

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