STRATEGIC M&A - THE FIRST AND LAST QUESTION

by Steve Brown

They say almost 60% of acquisitions fail to meet the pro forma performance numbers outlined to the buyer's board. While oftentimes this is a problem with integration, mostly this is the result of the fact that the acquisition should never have happened in the first place. If there was ever a situation for group think, it is often present when it comes to acquisitions. Once there is an emotional investment, it is hard to disengage, especially when you involve the myriad of investment bankers, lawyers and consultants that all get paid to see the acquisition go through. This is why it pays to have a discussion of M&A at least annually in the context of strategic planning. In our opinion, acquisitions should not be a strategic initiative unless you are one of the select numbers of banks that are trying to do a roll up strategy, bulk up and then sell. Those banks aside, bigger is not always better and it can be easily argued that the opposite is true. If you are not already a superior performing bank, it is likely that an acquisition isn't going to improve performance. Combining two average performing small banks just makes a larger average performing bank. If your strategic initiative calls for expanding into new geographies, increasing lending expertise, adding retail products, or any number of fundamental changes; then an acquisition should be considered (along with partnering and organic development). That said, we don't mean that M&A shouldn't be part of everyone's plan Ã¢Â€" just the opposite. The market is such that the decision to continue to run the bank should be one of the first questions asked. No matter what your performance, start a strategic discussion with a question Ã¢Â€" should we sell and at what price? If the answer is yes, and the price range is within the current market range (1.4x tangible book or less for the most part) then a good strategic initiative would be to devote a stated amount of resources to explore the option (have discussions, hire an investment banker, etc.). On the other hand, if the price is well out of range or the answer is no, then it is back to fundamental strategic planning. If this is the path, the last question of strategic planning discussion should be Ã¢Â€" do we want to devote resources to acquire in order to fulfill a stated strategic initiative? Should you wish to acquire, gaining the expertise to pull off a transaction is worthy of a strategic initiative. Knowing what a target bank will look like helps management focus limited resources. Size, geography, expertise, customers, performance (do you want a problem bank at a discount or a well run bank at a premium) and especially culture all should be outlined and stated in writing to ensure all are singing from the same sheet of music. At the outset, a buyer must decide whether they are open to purchasing just assets (like a branch), a whole bank or either. Even more importantly, how will the bank decide between the two alternatives? Will stock, cash or a combination of both be used to purchase? What type of resources should be employed just to determine a potential target? Will due diligence be done with existing resources or will you outsource? Who is in charge of choosing advisors? Is the Board OK with 100% of the CEO's time spent on this or just 10%? Spending time outlining what a successful acquisition would look like is an excellent first step that will act as a filter to prevent time and money being wasted on opportunities that don't meet a strategic objective. A successful acquisition is a combination of the right strategy, fair terms, execution of the purchase and execution of integration. By making selling the first question and buying the last question, the answers to both will help ensure that your bank is spending its resources wisely. You will not only raise the probability that the acquisition is a success, but will develop a competitive advantage in the strategic process itself.

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BANK NEWS

Closed (17 YTD)

Fort Lee Federal Savings Bank ($52mm, NJ) was closed by regulators and sold to Alma Bank (NY). Alma gets one branch, paid a 1.85% premium for deposits and buys $15.7mm of assets.

1Q Earnings

SunTrust Banks reported profit climbed 39%, as loan quality improved and it saw better than expected revenue. Loan loss reserves fell to $317mm from $327mm in 4Q.

Hiring

The National Association of Business Economics (NABE) found 39% of business owners expect hiring to increase in the next 6 months, up from only 27% in Jan.

Jobs Picture

A Gallup survey finds 68% of people say they know someone personally who has been laid off or lost their job in the last 6 months (the highest level in Gallup's history).

Stress Testing

The Fed announced the formation of the Model Validation Council, which will provide independent advice on models used in stress tests of banking institutions.

Economic Survey

A survey of economists by USA Today finds 16% expect the unemployment rate to fall below 7% by 2013, 53% say 2014, 22% project 2015 and 8% say 2016. Meanwhile, 35% say they are more optimistic than they were 3 months ago when the survey was last taken.

Customer Opportunity

You may want to launch a targeted savings account for parents of soon-to-be-college students. The data shows annual tuition, fees, room and board average $17k at public colleges and $39k at private ones according to the College Board. In addition, costs continue to rise at a rate of 6.0% for public and 4.4% for private colleges in 2011-12.

Mutual Funds

Bloomberg reports the top mutual funds by assets are: Vanguard ($1.4T); American Funds ($914B); Fidelity ($858B); Pimco ($477B); Franklin Templeton ($362B); T. Rowe Price ($301B); Columbia ($167B); Blackrock ($152B); JPMorgan ($152B) and Oppenheimer Funds ($148B).