Bank M&A - Present & Future

performance Mergers and Acquisitions

Summary: Bank M&A hit a low point this year. Yet, it is expected to ramp up in 2021. We review the M&A landscape.

The marriage rate dropped to a new low of 6.5 per 1,000 people in 2018, the lowest number recorded. Major events, such as the Great Depression, have affected this number too, so it could dip even more due to the effects of the pandemic.

Similarly, in 2020, bank mergers and acquisitions hit their lowest point since 2009 for both value and number of deals. But a report from FJ Capital Management in VA, predicts that the M&A market will bounce back and increase significantly over the next 10 to 15Ys. In fact, the report projects that the US, which currently has about 5K community banks, may have only half as many in 10-15Ys -- mostly because of mergers and continuing pre-pandemic trends.

A big change from 2019 to 2020. Data from S&P Global Market Intelligence shows that 2019 was a good year for bank M&A. The first quarter of 2019 saw 47 deals that totaled $6.7B, leaving out SunTrust's $28.3B sale to BB&T. That number dropped to 39 deals in the first three months of 2020, worth a combined $6.6B. Those 39 sales were the smallest number of closed deals in any quarter since 2011, when 33 banks changed hands in the first three months of the year.

Price-to-book ratios were lower for 2020 deals than in 2019 too. The median price-to-tangible-book ratio was 156.3% in the first three months of 2020. By comparison, that number was 170.5% for the last three months of 2019, and 159% for 2019 as a whole.

How future deals will be assessed. The economy will likely rebound as the pandemic recedes, bringing M&A interest and activity along with it. At that point, the factors that make banks attractive targets will probably be different than they were in 2019.

M&A buyers will now be looking for particular criteria: banks with **loan portfolios that did well** during the pandemic, **technological infrastructure and capabilities, earning capacity** during a near-zero rate environment, and **"excess" liquidity**. With this in mind, both sides might ask:

- How well did the bank's loan portfolio perform during the pandemic? What can we say, credit remains king.
- How up to date and firmly embedded are a target bank's technological abilities? Like many other office-based firms, banks have been forced into staffers working from home and helping customers do business virtually. Banks that have done that successfully, by leveraging technology to reduce overhead and increase customer self-service, will have a competitive advantage.
- How strong is a bank's ability to earn, given that interest rates are near zero? All banks' net margins are under attack, and that probably won't change in the next 18 or so months. Banks that have managed overhead while proactively developing fee income will be more attractive than those that have not.
- How much of the "excess" liquidity currently on the balance sheet is expected to stay? Banks that leverage the opportunities from PPP or look at longer-term trends in developing profitable relationships with strong core deposits are likely to be valued higher in a merger of equals.

These criteria may not be a surprise for many of you. However, they are important to remember, so that you have M&A options, if needed, down the road.

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