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GOLDEN HELLOS

It's all change on London's wealth management scene, with a wave of mergers amid concerns over competition and regulation. So should firms stick or twist?

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Mergers on the wealth management scene are like buses: too many people crammed into a small space, causing sweaty neighbours, debates about which route to follow and too many loudmouths on their Blackberrys. No, wait, let me try that again. Mergers on the wealth management scene are like buses: you wait years for one, then a glut come along at once.

This spring, we saw three high-profile unions on the normally placid London scene: private investment office Lord North Street and multi-family office SandAire announced in March they were merging; in early April Rathbones bought parts of Jupiter and Tilney for £57 million; and later in April Thurleigh (£300 million AUM) began a merger with the much-larger Ingenious (£1.2 billion). These follow the approval of the Quilter-Cheviot merger and Schroders' acquisition of Cazenove last year. So why are these mergers happening now? Why are their non-merging rivals so pleased? And what does this mean for clients?

There has been, as a report from Aite dramatically put it, a growing 'hunger and expectation' for consolidation. (A PwC report called the industry, with slightly less drama, 'fluid'.) The author had observed it in most parts of the wealth management sector, like big banks, IFAs and sales to private equity, but not — and he's clear about this — in the family office segment, which is precisely where it is now happening. According to PwC, it's only going to continue.

The conditions which have inspired these bouts of matrimony range from the local to the global. Most obviously, thanks to quantitative easing and the world's eventual recovery from recession, with accompanying market booms, there is more money about; companies have been stockpiling for years and profiting of late, and now there is M&A activity in every sector. Britain's wealth businesses — with £4.5 trillion under management — are no exception.

But counterbalancing this opportunity are plenty of threats, strong drivers to safer harbours. Unremitting waves of regulation are one of these. William Drake, co-founder of Lord North Street, says cost and complexity had in part urged them to their merger: 'It's getting more and more expensive to be an asset management company, so a bit more size will make it a little easier to do the things we wanted to do.' Charles MacKinnon of Thurleigh talked of an 'increasing tide of regulation', now swollen to engulfing proportions.

Even before the financial crisis, the Financial Services Authority had set in motion the Retail Distribution Review, meaning advisers had to be properly qualified, to choose between giving independent or restricted advice and to charge for their advice, rather than taking kickbacks from those whose products they sold. While a quarter of financial advisers consequently left the industry, those at private banks and wealth managers had largely already qualified, though some senior staff had to crack open their textbooks and take their exams. The financial crisis then entailed much more regulation, from London, Brussels and Washington. The EU promulgated MiFID II, which sounds like a nuclear weapons programme but in fact affects anyone who deals with financial instruments, while America developed FATCA, a demanding and demoralising law which means that anyone who has US clients needs to submit data on them to the IRS. The larger your firm, the less burdensome this becomes.

Interestingly, RDR also motivated the Thurleigh merger in a positive way: MacKinnon says it will let the new company offer Thurleigh's 'intellectual strategy, our portfolio' to many more people, farmers in Cirencester as well as plutocrats in Chelsea. He compares it to Heston Blumenthal: he can have both the three-Michelin-starred Fat Duck restaurant and 'he can sell Christmas puddings on the shelf in Waitrose'.

And no sooner have we consumed this year's candied-lemon-stuffed Blumenthal Christmas puddings than it will be time for the 2015 general election, which has been presaging political risk for wealth managers. 'We're very aware,' says MacKinnon, 'that there's an election coming, and around elections there are often tax changes. We have a very positive environment for entrepreneurs and there's a fear that environment might fall away. Is it why we did the deal? No. Is it why we did the deal *now*? Yes.'

FUTURE TENSION

Timing has been important in another way too. Firms which have survived the financial crisis have proved their essential stability (and indeed profitability), but now five long years of reaction are giving way to thoughts of what comes next. Existential questions are being asked — about the values that motivate a firm, its principals and its employees, about the responsibilities running a firm entails, about belief in the importance of independence. Asking these questions when there is plenty of hungry money around is a lot easier, of course.

Daniel Pinto of Stanhope Capital, three times winner of a Spear's Wealth Management Award and with no plans to merge any time soon, says we are seeing an evolution: 'The first period of multi-family offices was all about using your network of contacts, the founding families, the friends of the founding families, and in fact behaving like a club of wealthy co-investors. There is a second stage now, which is probably a sign that this sector is becoming more mature, where people say it's not just about being a club of wealthy co-investors, it is about performing, it is about investing in research.'

Then there is the cyclical aspect: 'Turn, turn, turn,' MacKinnon says, quoting the Byrds. 'Cycles are natural. There will be a cycle of agglomeration that we're now in, which will create larger firms, which will eventually split up.' His thirtysomething team members would, in a decade, decide to strike out with their own small firms, having seen how business was done on a bigger scale.

If size makes the firm's regulation more manageable, does it necessarily make its intellectual firepower more, well, powerful? In a *Spear's*/Speechly Bircham debate in 2010, Charlie Hoffman of HSBC Private Bank suggested to William Drake that banks had the advantage over independent wealth management firms because they could cover more asset classes more deeply.

Drake, whose firm will go from 25 people to 50 after the merger, is as dismissive of this argument today as he was in 2010: 'If you're picking stocks and trying to cover all the stocks in the world, you couldn't possibly do it. But what we're doing is asset allocation and manager selection,' perfectly pos- »

Illustration by Will Ings

sible with a team the size of his. If you take care of the strategy, his argument runs, the tactics will only matter moderately. Today's accessible but in-depth technology, MacKinnon says, allows even small firms to compete. (The exact word he used when I suggested bigger meant better was 'rubbish!'.)

Pinto, whose firm has £6 billion under management, thinks size matters. He contrasts his 70 employees, including eighteen exclusively on investment research, with other firms: 'If you look at some of these private investment offices, their *combined* employee base was eighteen people, including everyone — the secretaries, the business developers etc.' But it's not wholly a numbers game: 'It doesn't mean success is a function of the number of people you have — it's not — but you need to invest in your investment capabilities.' He says he wouldn't be surprised to see firms with between 100 and 200 people (which Stanhope is approaching), and he says it with confidence, with desire.

One factor Pinto is at pains to emphasise is that wealth managers which don't have the 'best' structure will fall away: without the right incentives — an equity share for key employees is vital, he suggests — you won't attract the right people and if you don't attract the right people, you won't make enough money to keep them and hire new ones. 'When you look around, very, very few firms had done that, either because they had a founding family that was not willing to use equity to attract talent or because you had one or two founders who decided they should keep their stake… Because they had the first step wrong, they were never able to grow substantially, were not able to make enough money and therefore had to sell themselves or merge.'

There are certainly firms which have merged of which this is true, but both Lord North Street and Thurleigh would dispute that it was true of them; in addition, William Drake says equity in a firm is only one way of keeping talent and Charles MacKinnon says some of his employees have equity shares.

There is, of course, a brand of wealth manager which prides itself on not growing but which is now, perhaps belatedly, realising it can't always cope: the hyper-exclusive single-family office.

FAMILY AFFAIRS

Single-family offices, which only become practical given wealth in the nine digits, might be thought almost by definition to be able to afford the best advisers. But as Stanhope partner Guy Paterson says, they are conceding that larger, independent wealth managers might be necessary to pick managers once asset allocation has been settled internally.

In addition to performance and regulation, single-family offices are finding one of their original purposes frustrated too, Paterson says: 'A lot of these family offices were set up to have absolute privacy; well, as you will know absolute privacy doesn't exist any more — what you have is relative confidentiality. Once you've accepted you can't have absolute privacy any more, you may as well get the best performance.' This potential flow of mega-money is thus both a cause and an effect of mergers: firms attracting it become more desirable partners and larger firms are more likely to attract it.

Amid the joyful pealing of wedding bells, there are some parties who may find these marriages less than congenial: the clients.

DNA PROFILING

Entrusting your money to one of these wealth management firms is more than a matter of bonds and basis points. If you'll forgive the florid term, it's about philosophy. (I bet I know exactly which private bank Plato would have gone with.) One signs up to Thurleigh or Lord North Street or another wealth manager because you like their people and agree with their investment approach, which are anyway intertwined. When two firms become one, a critical risk is that this investment philosophy is diluted.

Daniel Pinto thinks this is a critical issue: 'Every firm has an investment DNA… If you merge with a firm that doesn't have the same culture, it could be that the clients feel it's not what they signed up for.' That is, one new philosophy may disappoint two sets of clients.

William Drake robustly denies this is the case with his company, saying the whole point of the merger was that the two firms' investment philosophies were similar: he and Alex Scott of SandAire realised 'the businesses, through separate routes, had come to a very similar business model and we shared values'. After some time, the two firms will compare their processes and adopt the best of each other's.

A merger may mean changes in staff and their influence too, says Pinto: 'It is clearly challenging because it's one thing to deal with an owner and when you merge, very often the balance of power in the combined entity has changed. You create instability, and the enemy of client satisfaction is instability.' Guy Paterson adds: 'We're all people-businesses and if you're distracted by internal politics, by what your personal position is, that can't help in terms of maximising risk-adjusted returns.'

This fear of instability has clearly been behind pronouncements from merging firms. William Drake says: 'We're going to keep both companies running as regulated entities for a little while and use both names, and over a year take advice on which brand to use or whether to come up with a new brand.' The same from Thurleigh: no new brand for at least a year. If I had to help choose the new name, I'd go for Ingenurleigh — which is probably why I ought to stick to writing about these mergers, rather than orchestrating them.