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Recent Transaction Activity

In the changing world proposed by the Cooper review, of most concern to planners and Licencees are the proposed opt-in requirements, the banning of commissions and Licencee rebates.

These proposals have resulted in an increase in enquiry about selling, merging and in some cases buying, and has translated into an increase in transaction activity. Despite the uncertain environment, completed transactions still reside in the 2.8-3.5x annual recurrent revenue range with a few exceptions. There is no softening **yet** of these multiples, or the terms that go with them.

Based on recent transactions we have been involved in, large Capital city Practices with an investment bias, and an annual recurrent revenue of circa $1.5m or more, continue to attract EBIT valuations with prices at a multiple of 5 to 7x EBIT, depending on payment terms.

For regional Practices, there is a lower supply of both opportunities and of buyers, so the market is quite choppy. Where there is competitive pressure in transactions, prices are holding, where there isn't, sellers are having to be negotiable on terms, to achieve their price ambitions.

Risk books continue to be in high demand and trade at the top end of these multiples. These books are sort by other risk specialists, by investment planners and more recently mortgage brokers, who are looking to diversify their income sources.

In case you missed it.....

Over the last 6 months, it feels like the' perfect storm of government enquiries', Ripoll, Cooper, Henry... and a significant paradigm shift in the Financial Advice end of the industry is proposed.

In summary, it is proposed to

- Introduce a fiduciary duty for Financial Advisers;
- Ban commissions on the sale of investment/superannuation products and on volume based rebates from July 2010;
- Have clients sign each year, an agreement on the level of advice fees.

How have my peers responded, what will the Cooper recommendations do to the value of my Practice?

Based on our conversations, Financial Advisers are responding in at least 5 different ways –

1. Enquiring about, and positioning for the sale of their Practice; or
2. Re-engineering their business, by selling 'C+D' clients, and developing a fee based proposition for the higher value clients; or
3. Finding a merger partner who has already implemented a fee based model; or
4. Returning to a specialised personal or business insurance offer, or
5. Migrating away from the managed fund platform based business model, to an MDA/UMA enabling in-house asset management and administration business, on which

all asset based fees are retained within the Practice/Licencee. This is particularly prevalent among Practices in the SMSF and HNW investor space.

We currently receive between 10-15 calls a week to discuss these options, and have been a sounding board for a range of ideas.

One thing we are confident of – through our experience of the last 22 years, the Advice industry has shown extraordinary resilience and entrepreneurial ability to adapt to environmental change, and this time will be no different.

Will Cooper erode the value of my Practice?

There is some nervousness among Advisers on the potential impact of a ban on commissions on the value of their Practices. Our position is that, at an industry level, the price of books is underwritten by three things:

- Supply and demand - demand from funded buyers still exceeds the supply of quality Practices for sale, and Banks continue to offer commercially priced lending facilities for buyers;
- Institutional buyer of last resort facilities – our estimate is that around 35-40% of Planning Practices in the industry still have these arrangements(or a proxy) in place, and their 'multiple of annual revenue' based buy-backs provide a floor price for Practice valuations and transactions in the industry,
- Double digit long term growth rates for the industry – despite the investment environment, we have ongoing growth in superannuation contributions, and we know Australians still remain under-insured.

Assuming the ban on commissions is enacted - a word of warning - for a period of time the certainty of income from these books will see them retain their value. However it is reasonable to expect that trail commission based books will begin to decline in value through the natural forces of client attrition.

If the client base has no insurance cross or up –sell potential or ability to migrate clients to a fee for service model where the annual revenue of a Practice can be preserved (or increased), then there will be further pressures on value.

We believe that Cooper may well be the start of an attempt to address a broader range of perceived conflicts of interest at the Advice end of the industry. This could mean that the role of common Licencee offers such as buyer of last resort facilities will begin to be debated, and reviewed.

A ban on commission and a review of BOLR's, would significantly impact pricing dynamics, and the value of Practices across the industry.

It might drive valuations to more common methodologies, and accelerate the need for Financial Advice Practices to be of sufficient scale to derive a genuine EBIT, to maintain their value.

Licencee Land

There is little doubt that the proposed ban on rebates from Platform providers to Licencees, favours the institutionally owned and funded Licencees. Prima facie, these Institutions are able to fund and cross-subsidise their Licencee channels from the profits of their Platform, without contravening Cooper's recommendations.

There is some debate on how an Adviser in an institutionally owned Licencee, can recommend that Institutions product and platform solutions, and reconcile the recommendation with the fiduciary duty to act in the best interest of every client. Conforming to this obligation becomes a little more complex when the Advice practice receives subsidised Dealer services from the same Institution.

For non-institutionally owned Licencees who rely on the Platform rebate to fund their services, seeking other ways to replace volume based bonuses will be a priority. We see tactical responses such as Platforms paying fixed fee marketing allowances, and separately wholly owned Licencee subsidiaries receiving service allowances.

We expect other Licencees will respond in a more strategic way, migrating to in- house asset management and administration, others will buy in technology enabled administration and asset management services at a fixed price and deliver to clients on an asset fee basis.

We are seeing the top end Practices of all Licencees starting conversations about coming together to form new 'integrated' advice, investment and administration business models – stand alone Private Wealth Management models for the medium to HNW and SMSF market.

Technology is enabling these Practices to own all the revenue in the value chain, and reduce the need to utilise external fund management offerings, such as managed funds.

The greater revenue and business value these Practices derive by changing their client offer and business model, will accelerate change in other Practices and in the Advice landscape over the next 3 years.

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