

## Coupling up – Aberdeen Asset Management and Standard Life keep it local

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Boom times are back if you happen to be an M&A banker, especially one that specialises in financial services (FIG). After a decade of sluggish deal activity since the ill-fated bank mega-mergers that preceded the financial crisis, FIG M&A is back with a bang. As the dust settles on the failing Deutsche Boerse-LSE exchanges deal, the asset management sector continues to surf a wave of consolidation. First there were the Janus Henderson and the Amundi Pioneer deals of last year and more recently the highly unusual acquisition of Fortress, the US private equity business, by Japan's SoftBank group; and now the announcement that the two Scottish firms, Standard Life and Aberdeen, are in talks to merge in a deal worth around £11bn, creating an asset management powerhouse with an AuM of £660bn.



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*« Boom times are back for M&A bankers specialised in financial services as the need for scale has never been more apparent in a sector which is dominated by a few global giants, but has an incredibly long tail of smaller players. »*

### Why the sudden rush of deals?

It has been a long time coming, but the collective headwinds for the sector are proving too much to bear alone for many asset managers. The relentless rise of ETFs, persistent fee pressure, struggling fund performance, rising regulatory and compliance costs and higher capital requirements are making life tough for stand-alone and sub-scale asset managers. The need for scale has never been more apparent in a sector which is dominated by a few global giants, but has an incredibly long tail of smaller players. Finding the right partner and coupling up seems to be the strategy pursued by many management teams.

### The merger of Aberdeen Asset Management and Standard Life Investments into the newly-created Standard Aberdeen: a win-win deal

It is no secret that Aberdeen, itself a product of acquisitions, has been in the market for another game-changing deal. Speculation has been rife that it is either a target for a larger firm or it is on the lookout for a deal for itself. Martin Gilbert, Aberdeen's well-known CEO, acknowledged that the Janus Henderson tie up was a smart deal and that he was on the lookout for something similar. He briefly had a look at Pioneer's US business, but unable to compete with Amundi's firepower, dropped out of the running. After presumably having scoured the market for US-centric opportunities, Aberdeen has found what looks to be a great deal on its own door step. The cost synergies are clear given the operational and geographic overlaps.

The products and distribution are complementary and with an AuM of £660bn, the deal will catapult the combined entity well ahead of the likes of Schroders or M&G to create a regional asset management powerhouse and globally relevant player. The one drawback for Aberdeen and Gilbert is that for the first time since it was founded, it finds itself as the junior party to a tie-up. Still, this is no time to be choosy, especially when the rationale stacks up so well.

For its part, Standard Life which is suffering outflows from its blockbuster Global Absolute Return (GARs) product, gets access to Aberdeen's emerging market and Asian equity franchise at a time when sentiment looks to be turning for the better. On top of this, the deal will bolster its product range in solutions, property and alternatives. With both asset managers under pressure and looking to diversify, this deal couldn't come at a better time.

## A growing split between large scale companies at one end and boutique players at the other

We think sector consolidation has some way to play out. Investment bankers are no doubt busily assembling pitchbooks of every conceivable company combination, and beating a path to the various CEOs' doors. In the rush to couple up, the fear of being left behind, single and unwanted, may force management teams into unwise transactions.

Executing a deal is tough in a people business where cultures are strong and personalities forceful. For all its merits, some cracks are starting to emerge as Henderson and Janus begin to integrate the two businesses, triggering a recent spate of high profile departures. Nevertheless, we see the sector bifurcating between the large-scale, diversified players and the niche or boutique houses.

While the former will provide a supermarket of investment solutions, the latter will continue to be alpha generators and key to innovation in the sector. These types of boutiques will earn their place in a consolidating sector and perhaps even see even greater opportunities if the diversified giants lose their inventiveness and alpha-generating capabilities.

## Is it time to hold investment banks?

Investment bankers are currently riding a high. Mega deals are back and trading activity has been surging on the back of the Trump reflation trade. The question we have been asking ourselves is whether we would want to own an investment bank at this stage? Within the financial sector, we have had a clear preference for asset managers for their strong cash generation and solid balance sheets, and on the whole they have outperformed the other sub-sectors. However, with markets at or near all time highs and structural pressures weighing, the outlook for the asset management sector is challenged. Investment banks on the other hand have been a value trap in recent years but with volatility near its low, as contrarian investors, we need to ask ourselves whether our preference for asset managers still holds.

Could we be at the beginning of a multi-year rally in banks as interest rates and trading activity normalise? Maybe, but for now we remain unconvinced that European IBs would meet our quality criteria. There are some good businesses in Europe – UBS, for example, has the leading global wealth manager and a capital light IB. However, risks remain. Deutsche Bank's giant capital raise reminds us that balance sheets still need to be repaired in many cases.

Furthermore, the flurry of trading activity unleashed by Trump's election could prove to be short-lived. JP Morgan, one of the industry leaders, dampened expectations on trading activity last week suggesting that the Trump-related euphoria of recent months has begun to settle. Investment bankers probably still have high hopes for 2017 and beyond. We are wary - in the past this has often been an indicator of market complacency and elevated valuations.

For now, Aberdeen and Standard Life's proposed deal will grab headlines. If the Janus Henderson tie up was the template for a long distance partnership, Aberdeen and Standard Life are trying to prove that sometimes the best relationships can be found closer to home.

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