Consolidating positions

Firms forced into consolidation as tough times take toll

Advisories and broker-dealers in the ABS space are having to adjust to the challenges of operating in a market with reduced liquidity and low trading volumes. The halcyon days of a couple of years back have passed, leaving a great many entities chasing fewer opportunities.

One response to these more challenging conditions has been consolidation, with – for example – StormHarbour Partners and Fusion Advisory Partners recently linking up to enhance their client offering and strengthen their position in the market (see SCI issue 205). Other firms, like brokerage Odeon Capital Group, have actively expanded their own business, while many others are leaving the space and returning to banks.

StormHarbour says that adding Fusion to its US operations group strengthens its core business lines – sales and trading, structuring and advisory and capital markets. Although this may improve what the firms currently offer, Odeon Capital md and head of research Mathew Van Alstyne believes consolidation for consolidation's sake achieves little – with the key being the addition of capabilities that a firm did not previously have.

Van Alstyne explains: "If you are in the same sector, you need to reach more customers, so instead of just doubling up your numbers you have to broaden your product offerings. The most important thing is adding value to your services."

Green Street Capital principal Dean Atkins agrees. He says: "Consolidation does not necessarily make sense if it is a true advisory firm merging with another advisory firm. If consolidation is adding something that one of the institutions does not have, then it makes sense, but in the pure advisory world that is probably rare. In most cases, I think you have brokerages linking up with advisory businesses and branching out in that way."

The reason firms need to branch out is simple: market opportunities have shrunk drastically, while too many firms have not yet responded. Atkins explains: "There were numerous small outfits which got going from 2008 onwards. At one point, there were upwards of 30 new brokerage outfits in London alone. There was a time and a place for that, but the market opportunity did not last as long as those entities thought it would."

He adds: "It is now very hard to be a pure broker on an independent basis. Bid-offers have normalised and trading volumes are nowhere near where they were. This tough environment has already led to some consolidation and there has also been a return of some of the key players in smaller brokerages back to the banks."

This trend is also what London headhunters are seeing. Lisa Wilson, Invictus Executive Search managing partner, says: "There are just way too many firms now in the ABS advisory space. A lot of senior people set up their own companies and had a fantastic couple of years, but now they are finding there just is not enough business. It is the same situation as with the brokers, which played an important role when the banks could not participate but got squeezed out when banks came back."

She continues: "There will be a lot of people who left banks to run advisory shops or brokerages who will now be going back into banks. But after these guys leave, what happens to the firms they set up? A lot of these will fall by the wayside unless they can consolidate in the way StormHarbour has done."

However, Van Alstyne disagrees with Atkins and Wilson in their assertion that there are too many firms chasing too little business. He says: "There is enough business to be chased. The number of firms is not the only issue, because what also matters is how many people there are at those firms."

He adds: "What we have found is that we have been able to hire and continue to expand because there is more opportunity in the marketplace than we were able to service with our existing employees. The reason we have been able to do that is some of the bigger firms cut down on staff to the point where we felt clients were being under serviced."

Odeon's approach has been to grow organically, rather than consider consolidation. Van Alstyne says that after starting out focused on structured products and RMBS, the firm moved into CMBS, student loans and auction rate securities, before more recently covering high yield distressed corporate and bank loans. He believes product diversification is the way to achieve stability and growth.

He says: "Consolidation is something the industry broadly is going to have to do at some point because there are lots of firms out there filling niches and it is really by combining niches that firms are able to become more powerful and improve the services they offer to clients."

Odeon's steady expansion may serve them well, but Atkins cautions that it is not a model all firms would be able to adopt. He says: "Aggressive expansion worked very well for Jefferies and in the ABS markets I see them as one of the success stories. Evolution has adopted a similar approach, but I do not see similar results in the ABS market."

Atkins adds: "For a small independent which maybe started in 2008 or 2009, expanding rapidly now is very unlikely to work – especially now that the market has normalised, bid-offers are not the crazily wide ones which were available for a short time and trade flow is just not there. In the European ABS markets I do not think that strategy would work."

He says the squeeze being applied may well drive further consolidation among advisories and brokers, especially among the sector's smaller players. However, he and Wilson each believe that alongside consolidation there will be something of an exodus from firms as senior people return to the banks many of them left only a few years ago.

Wilson says: "As recruitment people, we are seeing a lot of interest from people who moved into those companies and now want to get back into a bank. The advisories can still get good fees for the rest of this year, but beyond that does not look so good. The chance to leave and go to run a structuring team at a bank will tempt a lot of people."

The window of opportunity that many thought they could take advantage of two years ago has shut faster than almost anybody expected. With no let-up to the tough market conditions in sight, many firms have been left needing to expand or consolidate if they can and get out of the space if they cannot.

Van Alstyne says: "This continues to be a very testing time for brokers and advisories. As the market has rebounded rapidly and spreads have tightened, it behoves you to be more nimble and be more value-added. There is no catalyst on the horizon to suggest the market will become any easier to navigate; if anything, this market is set to become more challenging."

He concludes: "This is going to separate the wheat from the chaff. The guys with experience who are able to offer more value-added services will be able to shine a bit brighter the tougher the market gets."

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