Rudy Adolf dodges questions on Focus Financial earnings call, possibly because one inconvenient question overhangs a PE firm's $53 share price offer

The New York City rollup CEO said take-private negotiations precluded answering analyst questions; one big question is why the company accepted a $53-a-share offer only 4.5 years past its IPO

Author **Brooke Southall**

February 21, 2023 at 9:42 PM

1 Comment

Rudy Adolf: We will not be opening up the lines for Q&A as we normally do, but want to thank everyone as always.

> ***Brooke's Note: If Focus Financial completes its sale to Clayton, Dubilier & Rice (CDR), it will have completed an IPO, a take-private deal, dozens of sub-acquisitions and several wholesale purchases of large RIAs all in a span of five years. Its executives will also continue to deny the company is primarily an act of "financial engineering." Based on CDR's "best-and-final" offer [that makes a sale-for-parts a potentially lucrative worst-case scenario], it does not seem the New York private equity firm is under any illusions about what it is getting. Nor are the analysts, who were not allowed to ask questions last week. Rudy's rebuff provided them with an answer in itself.***

Focus Financial declined to take questions from Wall Street analysts on Feb. 16, citing overriding concerns about the take-private deal it hopes to execute with a private equity buyer.

The New York City rollup, earlier this month, entered into an exclusivity arrangement with Clayton, Dubilier & Rice, which CEO Rudy Adolf cited in concluding the meeting. See: Focus Financial is pushing shareholders to take a take-it-or-leave-it private equity offer worth about $6 billion -- including $2 billion debt assumption -- despite a break-up value near $10 billion

Matt Crow: 'It seems a little cautious.'

"We will not be opening up the lines for Q&A as we normally do but want to thank everyone as always for your time and interest in Focus," he said.

Certainly, Adolf might prefer that certain questions go unasked, chiefly about whether the $53-a-share offer is a good deal.

It still seems a tad hypervigilant, says Matt Crow, CEO of Mercer Capital.

"It seems a little cautious but maybe they were advised to stick to a script (?)," he asks in an emailed response from Memphis, Tenn.

"I saw an article posted in which a number of (unnamed) sources are complaining that the going-private price is too low."

Clayton, Dubilier & Rice characterized its bid as a "best-and-final" offer.

Deal supported

Public companies do not have to accept questions from analysts under Securities and Exchange Commission (SEC) rules but typically do so to foster cordial relations with Wall Street and investors.

Analysts have all but proclaimed the sale a done deal despite the lack of a binding offer.

"There do not appear to be material contingencies against the deal," wrote Morgan Stanley analyst Ryan Kenny in a research note. Our conversations with investors suggest general support for the deal."

Nor do hostile bidders appear ready to step in and up the bid – making it a situation with neither upside nor downside, say two other analysts.

"We do not expect another bidder to emerge given that Focus (FOCS) already shopped the company around to other potential buyers and has since entered an exclusivity arrangement with CD&R," RayJay Analyst Jack O'Shaugnessy said in a note to clients.

Yet the deal is far from done.

No competing bids

The deal would be "subject to negotiation with CD&R of definitive agreements on mutually agreeable terms," Focus stated upon signing of the letter of intent, announced Feb. 2.

BMO has already downgraded the shares after reaching the same conclusion that the deal is cast in stone at $53 a share. BMO previously set $55 as its target.

Shares closed today (Feb. 21) at $49.75, down 37 cents or 0.74%. Shares are continuing to edge lower in after-hours trading.

"Given this is an exclusivity agreement, we do not expect a competing bid, and believe a definitive agreement is the likely outcome," BMO analyst James Fotheringham wrote in a note on Thursday.

Dan Seivert: 'The stock price tells the story.'

The motivation for Adolf to end the meeting with no Q&A could be an excuse or a contract provision, says Ari Sonneberg, partner at Wagner Law in Boston.

“Entering into merger negotiations can be, and even often is, predicated on a nondisclosure agreement,” he says. “That said, saying one can't speak on a topic as a result of a pending deal could also just be an excuse not to answer questions.”

Market speaks

Though it's unknown how analysts took the rebuff, Raymond James downgraded Focus shares the next day citing the lack of upside potential for the shares and its shopworn state after months of negotiations.

Crow agrees that the market has spoken.

“I haven’t spent the time to do the math, but it’s hard to make that argument given 4.5 years of public trading activity [largely below a $53 share price.] Water finds its own level.”

Dan Seivert, CEO of ECHELON partners of Manhattan Beach, Calif., agreed and questions the utility of Q&A “blather” in this case at this point. “The stock price tells the story…lots of blather from Rudy about all the deals and all the progress and no enterprise value creation to show for it,” he said.

“Their best bet is to jump at the opportunity to go private and somewhat bail out their investors.”

Brooke lives on a houseboat, works in an office and juggles calls across the five time zones and four countries his small team works. He's out to prove an economic major can make a living as a journalist and that articles need not be a loss leader if they are written well and geared to an intelligent readership. @RIABiz

Keith Girard contributed to the editing of this article.

Dan Seivert

ECHELON Partners | Matt Crow | Mercer Capital

Related Moves

Dan Seivert's ripping success in RIA M&A deals has odd side effect of having some sidearm staff leave for new vistas

Carolyn Armitage and Mark Bruno left to mutual benefit, while Echelon Partners roars on, feeding the beast of deal-crazed RIA buyers and sellers.

July 19, 2021 at 9:17 PM

(1) COMMENTS

Roger M.

February 22, 2023 — 12:44 AM

When in doubt, sell out. So much for fiduciary.

POST A COMMENT

Focus Financial is pushing shareholders to take a take-it-or-leave-it private equity offer worth about $6 billion -- including $2 billion debt assumption -- despite a break-up value near $10 billion

Clayton, Dubilier & Rice's $53-a-share, or $4.1 billion, offer is predatory but likely to be accepted, in the sense that analysts imagine the rollup could be sold off in parts; Buckingham, alone, may fetch $2 billion.

Author Brooke Southall

February 2, 2023 at 10:03 PM

0 Comments

Focus Financial could get rolled down if Clayton, Dubilier & Rice takes over.

> ***Brooke's Note: My three sources were pretty much unanimous in saying that if you live by the sword of engineering arbitrage, you will also die by it. Focus Financial was early enough to the game to buy up a world of succession and liquidity-minded RIA owners at a six-times to nine-times valuation. Now it's competing against a new world of "operating" rollups that pay as much as 20 times. Worse yet, to move the needle, Focus needs to keep buying lots of RIAs and their AUM at high multiples at a time when public markets provide no arbitrage. Clayton, Dubilier & Rice smells blood and sees an opportunity. The price is right, and now it may arbitrage Focus's RIA units by buying them at 12 times on the public market and selling them for much more in private transactions.***

One of the oldest private equity firms in the world is making its first foray into financial services with a reported $4.1 billion offer (plus assumption of maybe $2 billion in debt) for Rudy Adolf's Focus Financial Partners.

Clayton, Dubilier & Rice (CD&R) of New York City made a "best-and-final" offer of $53 per share – enough to gain it exclusive negotiating rights. The stock (FOCS) closed today (Feb. 2) at $50.01, up $3.74, or 8.08%.

"Given this is an exclusivity agreement, we do not expect a competing bid, and believe a definitive agreement is the likely outcome," BMO analyst James Fotheringham wrote on Thursday (Feb. 3). Fotheringham previously had a "target" price of $55 and lowered it to $53.

The private equity firm is best known for buying retail service firms like Hertz, Brake Bros., FedEx Office, Uniroyal Goodrich Tire Co. and Lexmark.

But the deal appears to be too good to pass up, if not much to brag about, considering Focus is freighted with debt. The offer likely falls well below the breakup value, pegged at $10 billion. It's a bitter pill to swallow but sweeter than some alternatives, says Matt Crow, president of Mercer Global, an RIA M&A valuations and research firm in Memphis, Tenn.

Rudy Adolf is considering a sale of Focus Financial after struggling with debt.

The $4.1 billion valuation suggests it is worth more dead than alive. Just one of its 100-plus RIA firms – Buckingham – is likely worth more than $2 billion, Crow says.

Indeed, a quick glance at Focus Financial suggests it has a breakup value of about $10 billion. Focus shareholders have a claim to about $6 billion, according to Brent Brodeski, CEO of Savant Wealth Management, which has acquired 17 RIAs with $14.3 billion in assets under advisement.

Divvying the pie

“The $33 IPO and $53 takeout represents about an 11% return while they were public,” Crow says.

“That’s better than the major U.S. indices over the same period, but not the kind of ROI they seemed to be hoping for when they went public.

Matt Crow: ‘Almost all of that return is coming from the deal premium.’

"Almost all of that return is coming from the deal premium. The $53 price is about what FOCS was trading for a year ago,” he said.

Shares hit a 52-week high of $54.61 last February.

Though the offered price only restores the valuation to where it stood a year ago, Focus Financial published a press release today (Feb. 2) to offer a more glass-half-full perspective.

“The contemplated purchase price of $53 per share represents a 36% premium to Focus's 60-day volume weighted average price as of yesterday's close,” the company stated in its corporate release.

“And [it's] a 48% premium to Focus' closing stock price on December 28, 2022."

Deal squeeze

Focus also disclosed that the exclusive bidding rights were granted after other potential bidders rebuffed it.

"On December 28, 2022, the day the Special Committee specifically authorized its financial advisors [Jefferies LLC and Goldman, Sachs & Co.] to broaden their outreach and contact other potential bidders regarding interest in a definitive transaction,” it writes.

Funds managed by Stone Point Capital LLC are considering retaining a portion of their investment and providing new equity financing as part of the proposed transaction, the release noted. See: Stone Point and KKR buy Focus Financial for $2 billion by employing massive leverage

The deal would be "subject to negotiation with CD&R of definitive agreements on mutually agreeable terms,” it added.

Much of that is likely banged out already, Fotheringham suggests in his report.

"We see a fairly high probability of CD&R closing," he writes.

Hard place

In back-of-envelope figuring, RIAs hold the other $4 billion of value because RIAs typically only sell 50% of their cash flow to Focus, Brodeski says.

The owner of a rollup competitor who asked not to be identified offered this analysis in an email:

“Figure $350 million-400 million of EBITDA even trading at 12.5x is a 20% premium and my guess is Buckingham is one-quarter to one-third of the EBITDA, and that would fetch $2 billion alone easy plus Colony, SCS etc, plus all the small firms.”

Brent Brodeski: ‘Focus is in a tough place. CI

Yet Focus – and perhaps its oligopolistic competitors – may not be in a place to realize their intrinsic values on their own, says Brodeski, who plans to purchase seven to 10 RIAs per year in coming years.

Financial is in a tough place.'

"Focus is in a tough place. CI Financial is in a tough place. Hightower just raised capital on not so favorable terms."

Toronto's Globe and Mail newspaper published an unflattering article, Jan. 27, criticizing CI Financial Chief Executive Kurt MacAlpine for his "growth at any cost" strategy.

In just three years, he built a $2.85-billion empire of 30 wealth management firms, nearly all in the United States. Then, he moved its headquarters to Miami while leaving a mountain of debt behind in Toronto. See: CI Financial will cut off U.S. RIA unit from Canadian cash infusions as part of 2023 IPO but with a giant parting gift -- total forgiveness of its substantial mountain of debt

Before a rebound in recent weeks, CI stock was trading at pre-COVID-19 levels last seen in 2012, the article noted.

Need to compete

It's hard for the Focus sale not to elicit introspection, Crow says.

"I'm not suggesting that a Focus going-private event is an existential crisis for RIA aggregators, but it's a case study worth considering."

It's absolutely an existential threat to the big non-operating style rollups because the game has changed radically in the past 10 years.

For years, he says, these pioneering large aggregators could procure cheap capital and buy succession and liquidity-minded sellers for six to eight times cash flow.

Now deals are getting done nearer to 20X for RIAs with younger principals at a time when the capital is more expensive and harder to come by, Brodeski says.

The difficulty for these firms is that they need to compete in the marketplace with Creative Planning, Savant, CapTrust and other rollups that can afford to pay higher multiples because they can pull them into an operating company and grow them.

It's even harder for Focus Financial because it is a public company, Crow adds.

“As a public company, if you tell the market you’re going to keep debt under 4.5 times and you go to 4.51, everyone freaks out.

"As a private, you tell your board and move on. Still, dealing with analyst scrutiny is part of the process of proving a business model,” he explains.

Rollup turmoil

It's definitely part of the process to keep debt minimized, says Brodeski.

“My counter to [Crow's ‘freak-out’ observation]: Why would you ever have 4X debt? I couldn't sleep with that [even as a private operator].”

I’m not suggesting that a Focus going-private event is an existential crisis for RIA aggregators, but it’s a case study worth considering," says Crow.

In another sign of rollup turmoil, Sanctuary Wealth today, (Feb. 2), announced its founding CEO Jim Dickson has been replaced by Adam Malamed, the former chief operating officer of Ladenburg Thalmann, an independent brokerage and advisory firm.

Kurt McAlpine has been criticized in Canada for his ‘growth at any cost’ strategy.

Sanctuary grew largely by getting a Merrill Lynch guy in Dickson to recruit from Merrill Lynch. See: A 20-year Merrill Lynch veteran got Sanctuary Wealth to $10 billion in AUA in 15 months with no outside capital and no time in bed: 'Nobody's slept since April'

Malamed speaks the *lingua franca* of new-era roll-up leaders.

“I am a big believer in taking the best elements of a firm's culture and aligning it with an institutionalized strategy and scalable solutions that consistently elevate the financial advisor and client service experience,” he said in today's release.

“This is precisely what we will achieve together at Sanctuary going forward.”

Brooke lives on a houseboat, works in an office and juggles calls across the five time zones and four countries his small team works. He's out to prove an economic major can make a living as a journalist and that articles need not be a loss leader if they are written well and geared to an intelligent readership. @RIABiz

Keith Girard contributed to the editing of this article.

Rudy Adolf | Brent Brodeski

Focus Financial | Mercer Global Advisors | Matt Crow | Savant Wealth

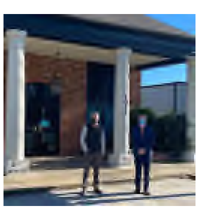
---

Related Moves

With RIA valuations ticking down and successions ticking up, Focus Financial deep sixes 'drunken sailor' pause, forgoes buyback plan and adds a CEO

CEO Rudy Adolf sees a 'softening' in multiples after a couple of frothy years when CI Financial dominated headlines and big RIA deals

August 12, 2022 at 8:39 PM



Looking past Covid-19 pandemic, Louisiana RIA buys $1-million building after hitting $1 billion in AUM and hiring the town's mayor

Summit Financial Wealth Advisors was sold to Focus Financial in 2014, growing its assets by $400 million since then but keeping staffing about the same

December 16, 2020 at 10:02 PM

Mentioned in this article:

Focus Financial Partners, LLC

Consolidator/Roll-up Firm

Top Executive: ***Rudy Adolf***

Savant Capital Management

RIA Serving Endowments/Foundations

Top Executive: ***Brent Brodeski, CEO***

Mercer Global Advisors

Advisory Firm

Top Executive: ***David Barton***

POST A COMMENT

CONNECT

RIABiz, Mill Valley, California