



Looking up

Deal activity has increased from 2003 in terms of volume, but not price

Volume of specialty finance mergers & acquisitions in 2004 is on pace to exceed levels recorded in each of the last three years, but it remains well below the late-1990s peak.

Year to date through the third quarter, a total of 96 specialty finance company sales have been announced, up from 86 through the full four quarter of 2003, according to the SNL DataSource. With an average of 29 transactions having been announced in the fourth quarters of the last three years, the industry is on pace to record upwards of 125 deals in 2004, the highest number since 2000, when 167 transactions were announced.

"It's been a good time to be in the specialty finance business," said Eugene S. Weil, managing director and co-founder of Milestone Merchant Partners LLC. Washington, DC-based Milestone ranked first among financial advisers through the first nine months of 2004 in terms of deal volume, according to the SNL DataSource, with seven transactions announced during that period.

"We're coming off of a tremendous rate environment, a tremendous origination cycle, so there tended to be a little bit less M&A work in the mortgage field in 2002 and 2003," Weil said. "Now, it is really picking up. A lot of these guys that were just making money hand over fist are saying, 'As my business slows down, am I better off partnering with someone else in a sale or merger and realizing the synergies?' So, that business has tended to pick up quite a bit."

Most recently, Milestone advised on American Home Mortgage Investment Corp.'s August acquisition of certain residential mortgage offices from Washington Mutual Inc. The largest transaction it worked on in the sector this year in terms of announced deal value was Sumitomo Corp.'s \$51 million purchase of Oxford Finance Corp.

AssetExchange Inc., which advises primarily on sales of credit union credit card portfolios, tied Milestone for first among financial advisers in terms of deal volume through the first three quarters of 2004, according to the SNL DataSource, but no prices were disclosed in any of the company's seven transactions. J.P. Morgan Securities Inc. ranked third with four transactions.

In terms of total deal value through the first nine months of 2004, the two financial advisers that worked on the Royal Bank of Scotland Group Plc acquisition of the credit card business of People's Bank MHC ranked first and second: Merrill Lynch & Co. was first with \$2.7 billion in deal value and Goldman Sachs & Co. was second with \$2.4 billion.

Skadden Arps Slate Meagher & Flom LLP ranked first among legal advisers in total deal value with \$3 billion through the first nine months of 2004. It tied with Wilmer Culter & Pickering for first in deal volume, with both having provided legal counsel on four transactions.

In the third quarter, 38 transactions were announced, up from 33 in the second quarter and 22 in the same period a year ago. It was the strongest quarter in terms of deal volume since the fourth quarter of 2002, when 39 transactions were announced.

But while activity has increased, aggregate price has not: 2004 continues to lack the blockbuster deals that have defined the merger market in six of the last seven years. In years past, 1997 saw the \$7.3 billion combination of Bank One Corp. and First USA Inc., 1998 had Household International Inc.'s \$8.5 billion acquisition of Beneficial Corp. and Conseco Inc.'s \$7.3 billion purchase of Green Tree Financial Corp., 2000 had the mega-merger of Citigroup Inc. and Associates First Capital Corp. in a deal first valued at \$31.1 billion, 2001 saw the \$9.4 billion acquisition of CIT Group Inc. by Tyco International Ltd., 2002 featured HSBC Holdings Plc's \$14.9 billion purchase of Household and 2003 had Citigroup's \$6 billion acquisition of Sears Roebuck & Co.'s credit card operations. To date in 2004, the largest purchase price on a single transaction was the \$2.4 billion Royal Bank of Scotland/People's Bank deal.

Year to date, total deal value amounted to \$8.9 billion through the quarter's close, some \$4.7 billion behind 1996's full-year level of \$13.6 billion, which was the slowest year in the last eight by a wide margin.

But Weil said he eventually expects a return of bigger deals in the mortgage sector once buyers get more comfortable with the impact of rising interest rates on loan originations.

"There's probably a bit of a wait-and-see approach where people are saying, 'Right now, we're in a transition phase where we're seeing rates go up and the refi business slow down, and we don't really know once things have gotten to a steady state in that new rate environment where it is going to end up,'" he said.

Third-quarter deal value totaled \$2.6 billion, ranking it fourth among the last seven reporting periods. The quarter's level was slightly ahead of the \$1.8 billion in volume recorded in the second quarter, but well short of the \$12 billion aggregate price posted in the year-ago period.

But the quarter featured a shift in the size of transactions being announced from very small deals previously to mid-sized ones. Eight transactions valued at \$100 million or more were announced in the third quarter, equaling the fourth quarter of last year for most deals of that size since the start of 2003. A total of six deals priced between \$100 million and \$500 million were announced, tying the third quarter with the fourth quarter of 2002 for the busiest period for transactions of that size in the last 12 reporting periods. Transactions of \$100 million or more in the quarter outnumbered deals with an announced value of \$100 million or less by a 2-to-1 margin for only the second time in the last three years.

Weil said Milestone's business pipeline remains "quite strong" in the mortgage and commercial finance sectors heading into the fourth quarter.

"We've got a bunch of deals in the market today," he said.

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