MISSOURI MERGERS AND ACQUISITIONS

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After a rather slow start in 2014, the mergers and acquisitions (M&A) activity picked up considerably during the second half of the year. We look for a busy 2015 as the "chatter" throughout the industry continues. Many discussions are starting, but making it to the finish line remains a challenge. Each deal seems to face its own set of issues, whether it is the disconnect between buyer and seller of the true fair-market value of the target bank or regulatory issues, which cause the application to be kicked to Washington (where it remains in the "black hole" of red tape and continuous delay).

Most experts have predicted a wave of M&A activity for the last three or four years, as the banking industry continues a move to consolidation. Maybe 2015 will see a deluge of activity based on pent-up demand. Among the factors that could fuel such an increase are increased compliance costs spread over a larger asset base; transaction risk reduced as asset quality improves; prices of M&A deals edging up; many management teams aging and rural banks facing difficulty in finding successors; and "banker fatigue" occurring in both management groups and boards, as they tire of working harder and facing unrelenting regulatory pressures but receive lower profits and rewards. All this on top of a difficult environment for smaller institutions to raise the capital needed to meet increasing regulatory requirements.

As the number of banks considering sale increase, buyers are reaching the conclusion they must grow to survive. Buyers who find the right acquisition can gain market share in current markets or expand into new and complementary markets, build a larger base to spread costs, and attain/retain talent to solve succession issues at all levels.

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As a result, we predict a significant increase in activity in 2015. Although prices won't reach pre-recession levels, the multiples of book value and earnings are trending up. Recently announced deals evidence that buyers are willing to pay additional premiums for the right fit. We also note as succession planning has increased, boards are facing the realities of aging management and major shareholders are seeking an exit strategy.

In past years, talk of a "merger of equals" (MOE) was met with disbelief, concluding there would always be a winner and a loser in such transactions. In 2014, we have witnessed several successful MOEs, allowing the combined entity to gain sufficient size to survive the onslaught of compliance costs. Each of these MOE transactions had similar factors, which led to success: CEOs and boards set aside egos in an effort to make it work; early meetings of small groups resolved many of the social issues (e.g., name, board membership, management positions, employee benefits, etc.); shareholders of each group remained as owners through a stock exchange merger (non-taxable reorganization) and pricing was based on equal values; organizations had similar cultures and business plans at the start; and great efforts were made by both organizations to coordinate integrating the employees and taking advantage of the best practices of both groups.

As bankers approach 2015 and begin the strategic planning process, they should assess their current position in the market and where they want to be in the near future. This will include a thorough understanding of the impact of Basel III capital requirements, management capabilities, and the local market for deposits and growth. If the bank desires to grow through acquisition, it will require an organized strategy that is proactive by identifying new potential markets, evaluating target banks and assembling a team within the organization to carry out the acquisition strategy. Retaining the proper third-party advisors (lawyers, accountants, investment consultants) is also key.

If the bank believes it is time to sell, there are various actions to undertake as well. The most important is to take care of house cleaning prior to starting the process. This includes making sure loan files are organized and complete, updating of change-in-control agreements, mitigating employee or litigation issues, and avoiding long-term commitments, such as long-term leases or contracts. The board will need a complete understanding of market valuation "drivers" (profitability, fee income, core deposits and market-to-market impact). In addition, the board will need to assemble an internal team to work on preparing and negotiating a sale and hire the appropriate third-party advisors.

Happy holidays and best wishes for a successful 2015! ■