MORTGAGE BANKERS ASSOCIATION



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# Garth Graham of STRATMOR Group on the Current M&A Market

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Garth Graham

Garth Graham is a senior partner with STRATMOR Group, a 30-year-old mortgage banking consulting firm. He has more than 30 years' experience in mortgage banking, ranging from Fortune 500 companies to successful startups. At STRATMOR, he manages

M&A activities, providing strategies for independent and bank-owned mortgage lenders.

**MBA NEWSLINK**: What has been happening with M&A activity the past 18 months?

**GARTH GRAHAM**: The M&A market in our industry has gone through a big shift over the past year and a half. Last year was a great time for buying companies because of the challenges lenders faced at the time, but the market is considerably different today due to the sudden and sharp decrease in mortgage interest rates.

Until this spring, most companies that sold did so because of three factors: their balance sheet was under stress due to rising loan production costs and other issues; they couldn't keep up with the marketing and technology investments their competitors were making; or the company's owners were nearing retirement.

M&A activity is still strong, but with lower rates, many companies that were planning on selling put their decision on hold to take advantage of another refi boom. Lenders are making more money, and there are nowhere near as many sellers this year as we saw last year.

**NEWSLINK**: Is this a 'sellers' market' or a 'buyers' market?'

**GRAHAM**: Definitely a sellers' market. If 2018 was a good year to acquire mortgage companies, 2019 is a great year to sell them. The problem is a lot of companies that were thinking about selling are hanging on to take advantage of the lower interest rate environment when they might be better off pulling the trigger. It's always better to sell from a position of strength, or when your business is doing well, because buyers are more likely to pay a premium.

Another factor to consider is the likelihood that we may see another slow first quarter in 2020, similar to what took place last year. Many are predicting a recession in 2020, and that might dampen the expected increase in the purchase market next year. When a lender's retained earnings fall, its secondary investors and warehouse partners will place that lender on their watchlist, which was the case for more than a third of independent mortgage banks in the first quarter of last year. Another market slowdown [like last year] could create a glut of companies all trying to sell under duress [in the spring]. If you're one of them, that's not going to be a good thing.

**NEWSLINK**: What are some notable deals we've seen so far this year?

**GRAHAM**: There were several deals in early 2019. In fact, the number of deals in the first quarter of 2019 was up two to three times versus previous years. Most were consolidation deals, or bigger companies buying smaller ones. There have been other large, strategic deals from newer entrants that have the potential to alter our industry's landscape. Zillow, Amazon-Realogy and Berkshire

Hathaway have all made strategic acquisitions into our space. A lot of what is driving these new, strategic buyers is the perception that there will be greater consolidation between mortgage and real estate businesses. It will be interesting to see how these deals work out and whether there will be more.

**NEWSLINK**: Which category of mortgage lenders has been most active buying companies? Why?

**GRAHAM**: According to STRATMOR data, by far the most active buyers have been large, well-known independent mortgage bankers. It's been this way for the past three years. Banks are active, but what is interesting is that roughly half of the banks that are buying companies already have a business model similar to independent mortgage banks.

The reasons why large IMBs are leading the way is because they typically have plenty of capital and plenty of experience hiring and onboarding loan officers and branch managers, as well as experience growing organically.

**NEWSLINK**: What steps do you recommend lenders take who are looking to purchase another company? And lenders looking to be purchased?

**GRAHAM**: The process of buying and selling companies in our industry has evolved tremendously over the past decade. Before the meltdown, the market was nowhere near as complex or as highly regulated as it is today.

There's a lot more to doing deals today, and a lot more factors to consider, including a company's culture and its approach to and investment in technology.

For buyers, one of the biggest challenges is that companies will say they are not for sale even if they are willing to consider a deal. These potential sellers are afraid that word will leak out and impact their recruiting and retention efforts. So, sorting out how to straddle that line is tricky for sellers, and a lot of our work is helping them figure out the best approach for the seller to maintain confidentiality.

Another challenge for sellers is knowing what the company is actually worth. There are different ways to look at this and getting into the numbers as reasonable projections for the future is a key driver of value.

For each of these reasons and others, it's a good idea for both buyers and sellers to work with an advisory firm with deep M&A expertise. A good advisory firm can serve as a middleman to bring buyers and sellers together during the early, sensitive stages of making a deal. Another major benefit of using an M&A advisory firm is that they can help determine whether there is a good fit between the cultures of the buyer and seller.

The bottom line, whether you are thinking of selling a company or buying one, is to get help. Given the many challenges and volatility that exists in our industry, you're going to need it.

*(Views expressed in this article do not necessarily reflect policy of the Mortgage Bankers Association, nor do they connote an MBA endorsement of a specific company, product or service. MBA NewsLink welcomes your submissions. Inquiries can be sent to Mike Sorohan, editor, at msorohan@mba.org; or Michael Tucker, editorial manager, at mtucker@mba.org.)*

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