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Q&A: Land of 10,000 deals?

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Marquette Financial Cos. is no stranger to financial services mergers & acquisitions, having made five purchases in a range of business lines since 1993, three of which occurred within the last 12 months. But with an increasingly competitive pricing environment taking hold, the company is also looking to add experienced management teams to enhance existing businesses or enter new niches, in addition to potential deals.

The company's most recent transaction involved the addition of long-time Dallas lenders James E. Casper, Michael D. Haddad and Jim S. Johnson to lead de novo unit Marquette Business Credit Inc., an asset-based lending organization, focused on providing alternatives to traditional bank financing.

Marquette is controlled by the Carl Pohlad family. Pohlad is best known for his role as the owner of the Minnesota Twins baseball franchise, but his company has made a name for itself in commercial banking, commercial real estate and commercial finance through its recent deal activity.

Marquette completed three acquisitions in 2003, adding Arizona-based Valley National Corp. in July for $13.8 million, the commercial mortgage operations of Legg Mason Inc. for $16.2 million in cash and a $6.9 million non-interest-bearing note in October, and Texas-based factoring company KBK Capital Corp. for an undisclosed amount in November.

Albert J. Colianni, executive vice president and COO of Marquette Financial, said his company is on the prowl for more acquisitions and, as large regional and national banks consolidate, additions of experienced lending professionals.

In recent interviews with SNL Specialty Finance Mergers & Acquisitions Editor Tim Zawacki, Colianni and Casper, Marquette Business Credit's CEO, agreed that market conditions offer plenty of opportunities both for the start-up lending unit and the Marquette organization as a whole.

"We're enthused about the opportunity because we believe we've hired an outstanding, well-known team of asset-based lenders in the Texas market," Colianni said. "The growth of that market combined with what we believe has been consolidation amongst asset-based lenders and asset-based lenders going upstream to larger companies, we believe there is a real niche for a lender that's locally managed and able to deal with small- and mid-market requests on a very service-intensive basis."

What follows is an edited transcript of those conversations.

SNL: Discuss some of the opportunities your new company has in this market.

Casper: We had a good opportunity with the Marquette Financial Cos. to establish an asset-based-lending company that served the smaller commercial market — wholesalers, manufacturers, service companies — in the $1 [million] to $10 million loan range.

What we had seen was a great deal of consolidation in the industry in the banks — just a real necessity on their part to kind of go up-scale to the larger transactions of $10 million and above. So, we felt that the market in the $1 million to $10 million range was really not being served by the banks, and certainly not [doing] the intensive monitoring we do on the receivables and the inventory and machinery and equipment.

We just thought it was a good time … to come together and do this.

When you look at your prospective client base, what is the industry focus?

Casper: It's really pretty broad-based. We generally find ourselves doing wholesalers, such as lumber wholesalers, plumbing wholesalers, food wholesalers, but at the same time we also have some … light manufacturing companies: aluminum extrusions, that type of thing. We also do service companies that might be in the staffing industry.

You're starting in Dallas and then branching out?

Casper: It's really more focused on Dallas because we're located here and the activity level is here. The individuals that are involved … we've had national exposure, so we have contacts in most of the major cities.

We're going to look at loans primarily across the Southeast and Southwest. We think that it's a real good market at this point in time.

Do you expect the former KBK business and your Marquette units to be a source of business for you?

Casper: Yes, and it has happened already. [KBK] have a primarily factoring orientation, whereas ours is an asset-based orientation where we do receivables and inventory and machinery and equipment, so there is going to be quite a bit of back-and-forth cross-selling.

When the economy was weaker two years ago, there was talk about limited financing options for your targeted customers. Is bank consolidation having the same impact this year?

Casper: That's my opinion of it.

I come out of Bank of America, which of course was the product of a merger between BankAmerica and NationsBank. At NationsBank, we have an asset-based-lending business, and BankAmerica had an asset-based-lending division. Those consolidated, and instead of having two competitors out there in the marketplace, you had one.

They would raise the minimum size of a loan that they would look at. It would go from $5 million to $10 million and then to $15 million. It didn't happen on a daily basis, but it was a gradual sort of thing, simply because of their size.

At the same time, there was another competitor — Fleet Capital — and now Bank of America and Fleet have merged, and that will eliminate another competitor. We've also seen Bank One and J.P. Morgan [merge] and both of those banks operate in Texas and on a national basis. We've eliminated another competitor.

For the companies out here that are looking for financing, it's eliminated having multiple sources. It leaves this market, under the $10 million mark, to the small, community banks and regional companies. We think it is a very good market niche for us. The companies probably will be more collaterally intensive in that they're borrowing against their assets and rapidly outgrowing their base, and therefore they're finding it more difficult within the smaller banks to find that type of financing. …

What we're looking for is to serve the banks who simply don't have an asset-based-lending capacity.

Is a de novo the best way to pursue this business right now, rather than acquisition?

Casper: It's a good way for us, simply because we know it and we have a lot of contacts in it. It avoids having to pay a tremendous premium and trying to absorb somebody else's portfolio, which you may not know as well as one you've completely underwritten yourself.

What's the growth target for this business?

Casper: It's certainly a much smaller number [in the near term] as we get the basis for operation. But hopefully, over a five-year period of time, we can grow the assets to approximately $200 million in loans.

How is the new asset-based-lending business going to fit into the Marquette organization and complement some of your other businesses?

Colianni: We believe there are synergies amongst our businesses. We've focused on commercial finance as one of three strategic focuses for our holding company, and within commercial finance, we have two factoring companies and two asset-based-lending companies. We think there is a real, natural interplay between the factoring companies and the asset-based lenders … for internal referral opportunities, but also through giving us the ability to service the customer through a longer phase of what I'll call their credit cycle. Some customers are going to gravitate from a factoring company either as they increase their capitalization or see stronger financial results … to an asset-based lender, or vice versa.

Why de novo with this company and use acquisition to build the factoring business?

Colianni: We have a history of acquiring businesses, acquiring divisions of businesses and starting businesses. In our holding company, we have nine operating subsidiaries today, and four of those subsidiaries were started by us.

One always has to do what I'll call a 'buy-versus-build' analysis. If you can buy a good company, at the right price, with the right management team, obviously the premium is well worth your investment. If you have the opportunity to build that same company, the inherent premium is going to be the operating losses we incur.

In this situation, it has been our strategic focus for a few years to grow in asset-based lending, and we continue to look for asset-based lenders to buy. But here we had the opportunity to hire three very, very experienced people. We did the analysis and found that we would be better off to hire them and live through those early years of operations, and hopefully we'll build a company of significant value at what would be a smaller premium than [what we'd pay] to buy it.

Are you looking at entering new markets and lines of business through acquisition?

Colianni: The answer is yes on both.

Our strategic plan is focused on three broad areas of business. … Our broad, overarching mission is that we're going to serve business owners and their businesses with financial services.

Under that, we believe that we're very good at extending credit in a safe and sound manner. Credit is an underlying theme. We're in three principal business lines: commercial banking, commercial mortgage banking and commercial finance. And we're looking to expand in all three. Commercial banking through acquisition and de novo; Our commercial banking operations are headquartered in Phoenix right now, but we're looking across the Southwest. In commercial mortgage banking, our company is called NorthMarq Capital Inc., and we believe it is the third-largest commercial mortgage banking company in the country, with 28 offices. We'd like to expand that, both in terms of the commercial real estate services products we offer, but also geographically.

The third area is the broad area of commercial finance. Today, we are in commercial finance through six subsidiaries in asset-based lending, factoring, builder finance — residential developers and builders, and we have a licensed SBIC doing private capital investing with mezzanine debt. We're looking to expand in all segments of that area.

We continue to look at other areas of commercial finance, looking for the right fit. Obviously, we're missing a commercial leasing or equipment leasing company and we view that as a necessary service for business owners and their businesses. We're open to other areas also.

Comment on positive and negative trends you're seeing in financial services M&A.

Colianni: On a broad level, the positive is that there's no doubt we're seeing a rebounding economy and good business activity. Our businesses are doing well from a macro level. Secondly, we think that the continued consolidation amongst financial services being so aggressive, on a positive level, we think there are very good professional employees that are disaffected somehow, either they don't like the culture of the combined organization or whatever. There's natural displacement, so we can be opportunistic in hiring good people.

Additionally, I would say that customers, whether perceived or real, feel some disaffection toward consolidation. There's always a group of customers that, for all of the benefits that these powerful organizations offer, they'd rather deal with a smaller, more service-intensive company where they can really get to know the execs.

Those are all opportunities for us.

On the negative side, there's no question that premiums in all business lines have gone up and gone up somewhat dramatically. It does cause us to look more seriously at hiring management teams and integrating them into our existing platforms or beginning new businesses like we did with Marquette Business Credit. We still are very disciplined in our acquisitions. We're a cash buyer [so] we have to stay disciplined.

Accordingly, our acquisitions, while we try to stay competitive in those areas that are strategic for us, we look opportunistically, be it somebody who wants to maintain ownership, but wants capital, or someone is encountering some obstacles and we can come in and basically be a help with our money and strategic expertise. We have to look for those special situations because to go in and compete with some of the big buyers that are willing to pay hefty premiums with high-priced stock is difficult.

You avoid some of the surprises adding a management team that you might get with an acquisition.

Colianni: Thank you for saying that because, while we believe we do very careful due diligence on our acquisitions … the necessity for the due diligence is always so strong. The higher the premium, the higher the risk category of asset pool you're buying, the more difficult it is to do due diligence. The market is forcing you to pay a high premium on, maybe, an asset category that is deemed higher risk. That's sort of a double-whammy, and it certainly factors into our decisions whether to buy a small company versus a large company or to build a company versus to buy a company. If it's a company that we are growing, it is either small when we buy it or it's something that we start, frankly we can be very judicious on each loan we make. …

One has to be very strategically focused and one has to be careful on the prices you pay. That being said, we don't want to scare away potential sellers, where something could be very strategic to us. At the end of the day, one is going to pay more for something that is very strategic. For us, that could be, 'Well, they don't just have an earnings stream, they have a very strong management team that plays into our defined strategy.' Of course, one has to stand back and look at that. …

Each deal is different.