



Booming boutiques

By Pierre Paulden

Tired of conflicts, red tape — and traders — top bankers are fleeing big firms for independent boutiques — and shaking up the corporate advisory business.

Joseph Perella has a classical philosophy of what makes a great investment banker. “It is one of the few remaining industries that follow the renaissance model,” says the veteran merger adviser. “You don’t pick up a book to learn how to do it. You learn on the job under an experienced hand, like going to the studio of Leonardo da Vinci or Michelangelo to chisel marble.”

But this da Vinci code may be in peril, suggests the 64-year-old Perella, who has tutored generations of merger bankers during more than three decades on Wall Street. “The renaissance model requires that the mentors be around to teach the people coming in,” he explains. “Whenever there is an exodus of senior people, that model is going to get tested.”

Now is one of those times.

More and more seasoned Wall Street bankers are abandoning bulge-bracket investment houses for advisory boutiques, potentially changing the M&A advice business in the process. The lure: a more entrepreneurial ethos, less bureaucracy, fewer conflicts of interest and, not to be discounted, more money and power. These bankers long to work in smaller shops where their compensation is linked more directly to the business they bring in — and where they don’t have to feel like second-class citizens to the Street’s resurgent trader class.

Perella is himself a pioneer boutique. He quit First Boston Corp. in 1988 with his co-head of M&A, Bruce Wasserstein, to form one of the original merger boutiques: Wasserstein Perella & Co., which was acquired 13 years later by Dresdner Bank. After a falling out with Wasserstein, he



FT Partners' McLaughlin: The ex-Goldman banker's boutique is wrestling away deals from bigger competitors

Thomas Broening

joined Morgan Stanley in 1993; last spring he resigned as a Morgan Stanley vice chairman while that firm was in tumult. The lanky, bearded *über*banker has been recruiting star deal makers for what many Wall Streeters anticipate will be the ultimate boutique provider of strategic advice for corporations. Already its gallery of old masters includes onetime Morgan Stanley investment banking division chief Tarek Abdel-Meguid as well as Jon Anda and Paolo Pereira, that firm's former heads of capital markets and European M&A, respectively, and former Goldman Sachs International CEO Peter Weinberg.

Perella's yet-to-be-named firm joins a growing contingent of small-scale but high-powered boutiques — about two dozen so far — that are threatening to upset the established order in the lucrative and prestigious art of advising CEOs on mergers. Esteemed émigrés from the merger departments of big, full-service banks have brought with them not only well-honed deal-making skills but also high-level corporate relationships.

The result has been a slew of lucrative deals for their new firms: Independent advisory shops offered counsel on one third of the 20 biggest mergers announced last year, including SBC Communications' \$22 billion purchase of AT&T Corp. and Bank of America Corp.'s \$35 billion takeover of credit card company MBNA Corp., which Perella advised even before he had even started his new firm. That deal, which closed in January, is the second-biggest merger to be completed so far in 2006. Boutiques Evercore Partners and Rohatyn Associates, along with Lehman Brothers, are coadvising AT&T on its pending \$67 billion purchase of BellSouth Corp. Evercore is also a co-adviser to Dutch

media company VNU on its \$9 billion sale to a group of private equity firms, announced in early March.

Nor is the strong showing by boutiques a one-off event. As recently as 1999, independent firms were involved in fewer than 10 percent of global public-company mergers, according to an analysis conducted by New York research firm Dealogic for Goldman, Sachs & Co., which has more than a passing interest in the topic. By last year their market share exceeded 25 percent.

What makes the boutiques such a potent force? Can they hold on to — and perhaps even grow — their market share? Many observers, at both small and large firms, now see the independents not as a fly-by-night phenomenon but as a permanent and significant fixture of the M&A landscape — for a host of reasons.

CEOs have become concerned that Wall Street houses are more likely than in the past to place their own interests ahead of their clients'. Goldman, for instance, makes the bulk of its profits from trading and principal investing, and much of this activity involves the firm's risking its own capital rather than serving clients. The biggest firms also want to lend clients money, underwrite their securities and advise their clients' competitors.

"With each passing year these firms increasingly become principals and not advisers," says Scott Bok, U.S. president of Greenhill & Co. and a former Morgan Stanley M&A banker. "The percentage of the firms' profits from advisory has become smaller and smaller, and the M&A banker no longer feels like it is core relative to trading."

Moreover, as investment banks have grown ever larger and evolved into publicly held financial supermarkets (and have had to answer to impatient shareholders), they have concentrated on the clients paying the richest fees, often leaving smaller companies in the unsure hands of junior bankers. Some CEOs worry that merger advisers at the big houses may not go all out for them in negotiating deals, lest they offend a more important client — or potential client — on the other side of the table.

Also, directors of public companies are more attuned to the need for independent merger advice in the wake of the 2002 Sarbanes-Oxley Act and other market reforms that have piled greater liability onto board members. (Bulge-bracket firm executives say that none of the potential conflicts they face is so severe as to hamper their ability to serve their clients.)

William Zollars, CEO of Yellow Roadway Corp. (renamed YRC Worldwide in January), picked a boutique, Integrated Finance Limited, to steer the trucking company through its \$3.7 billion acquisition of rival USF Corp. last May. Zollars had relied on the judgment of IFL's James Hamilton when the banker was with J.P. Morgan and later with Deutsche Bank, and didn't hesitate to call on him when he departed for IFL.

"They're a small firm, and they don't have any money to give you," says Zollars "So we used a couple of other banks to help finance the deal and relied on Jim to give us the right advice."

While IFL provided counsel on merger tactics, earning a \$6 million fee, Credit Suisse and J.P. Morgan Chase & Co. helped with the financing. New York-based IFL was founded three years ago by well-known former J.P. Morgan execs Peter Hancock and Roberto Mendoza and Nobel laureate Robert Merton.

To be sure, the growing might of the boutiques hardly portends the imminent end of merger advisory work for traditional deal-making houses. Today's M&A boom ensures that there's more than enough business to go around: Rainmakers at the top four M&A firms — Goldman, Morgan Stanley, Citigroup and J.P. Morgan — generated an astronomical \$5.9 billion in advisory fees last year, up from \$4.8 billion in 2004, according to their financial statements. Global M&A volume reached \$2.2 trillion last year, twice 2002's level and the highest since the bubble-inflated record of \$3.4 trillion in 2000.

Yet some speculate that the factors underlying the defection from Wall Street firms of both bankers and clients could mean that one day the big securities houses won't even count merger advice as a significant client activity.

"Ten years from now the advisory business at the major investment banking and securities firms will resemble your appendix," contends veteran retail industry banker and former Lehman partner Peter Solomon, who formed boutique Peter J. Solomon Co. in 1989. "I hope to be alive to see it."

Solomon's and other boutiques are certainly doing everything in their power to make merger advice a vestigial organ at Wall Street firms. Evercore, a New York advisory shop founded in 1996 by former Lehman partner and onetime deputy U.S. Treasury secretary Roger Altman, now 61, recently hired Jane Wheeler, a financial services banker, from Morgan Stanley, and William Repko, a top adviser to distressed companies, from J.P. Morgan. In October, a few weeks after joining Evercore, Wheeler advised her longtime client E*Trade Financial Corp. on its \$700 million takeover of rival online broker HarrisDirect. Her boss, Eduardo

Mestre, quit as Citi's investment banking chief to run Evercore's corporate advisory group in late 2004.

Another gung-ho recruiter among boutiques these days is Greenhill & Co., founded in 1996 by Robert Greenhill, now 69, who had previously been Smith Barney's CEO and Morgan Stanley's president (see box, page 54). In 2004, Greenhill & Co. launched its own hugely successful IPO. And in the past year, the New York-based, 150-person firm — which advised MCI Corp. on its \$7.8 billion sale to Verizon Communications in January — has picked up some experienced bankers: UBS vice chairman Kenneth Crews; Citi financial institutions M&A co-head Robert Smith; and two senior Morgan Stanley professionals: Dhiren Shah, that firm's global technology banking chief, and Peter Stott, its co-head of U.K. investment banking.

Advisory boutiques come in as many forms as mergers themselves. Perella sees his nascent venture becoming a broad, lasting institution focused on strategic advice — not just on mergers but also on capital markets transactions. Sagent Advisors, a 40-person New York firm founded in 2004 by the former heads of M&A at Donaldson, Lufkin & Jenrette, also focuses on advice, not raising money for clients (see box, page 52).

Others, such as two-year-old, New York-based AGM Partners, revolve around the relationships and expertise of a single deal maker and serve clients in a particular industry; AGM's founder is former Lehman media banker Alan Mnuchin, 41. Often such firms specialize in smaller deals that Wall Street behemoths purport to welcome but don't always execute well. Steven McLaughlin, a former Goldman financial technology banker, is making a handsome living doing just that as head of San Francisco

FT Partners: Nanotech banking

“We provide a service and an expertise that do not exist at a large bank,” boasts Steven McLaughlin, the 40-year-old founder and CEO of Financial Technology Partners, a San Francisco investment banking boutique.

Brash words, maybe, but they resonate with Edward Uzialko, founder and former CEO of Lynk Systems. Three years ago, when he decided to sell the Atlanta-based credit card processor that he started in 1991, Uzialko hired Merrill Lynch & Co. to run an auction.

But the bids came in unacceptably, and unaccountably, low, he says. Uzialko suspected that Merrill was preoccupied by its ongoing relationships with Lynk's bigger rivals, such as Denver-based First Data Corp.

"I was a small fish," he says. Merrill "had stronger relationships with larger competitors in my space, and they just wanted to peddle me to one of those."

So after several months Uzialko ditched Merrill for FT Partners. McLaughlin had founded the firm in 2002 after seven years as a Goldman, Sachs & Co. banker. For the tiny boutique

— it employed ten at the time — Lynk was a hugely important client. McLaughlin worked tirelessly to attract a wider group of potential buyers. In September 2004, Royal Bank of Scotland paid \$525 million for Lynk — significantly more than the value of any previous offer, according to Uzialko.

"Steve had the experience of working with larger firms," says the ex-Lynk CEO. "He knew the industry, and he had the raw talent."

Patrick Olson, who worked on the Lynk deal for Merrill, denies that the firm was more concerned with other clients than it was with Lynk. But he acknowledges that focused boutiques can often get better results for clients — so much so that last year he left his post as head of financial technology banking at Merrill to work for a boutique-like advisory division of money management firm BlackRock.

FT Partners, which doesn't underwrite or trade securities, has been involved in some of the biggest M&A deals in its chosen sector: financial tech companies. In 2003, McLaughlin advised investment bank SoundView Technology Group, which had been taken public that June by

Goldman, on its \$345 million sale to Charles Schwab Corp. In February 2005, FT beat out bulge-bracket shops to advise Liquidnet, a fast-growing electronic network for block equity trades, on the \$250 million sale of a minority stake to private equity firms Summit Partners and Technology Crossover Ventures. In January the firm advised electronic payments company Verus Financial Management on its \$325 million sale to Sage Group, a software concern.

As gratifying as such small-scale deals may be to McLaughlin, they will never make FT a dominant player in the larger merger market. Yet the boutique, with a staff of only 15, is undoubtedly taking some fees away from big firms. What's more, with FT's extraordinarily low overhead, sole owner McLaughlin is faring far better than he would have had he stayed at Goldman.

Restless bankers at big firms are bound to be watching with envy, much as traders at such firms dream of starting hedge funds. "Boutiques are like the new hedge funds," says McLaughlin. "We'll never hit the high end of the league tables, but we are going to win virtually every deal we compete for." — **Pierre Paulden**

boutique Financial Technology Partners (see box, page 51).

Still others advise middle-market companies across the spectrum of industry sectors. Minneapolis-based Houlihan Lokey Howard & Zukin — with fewer than 500 professionals, paltry by big-firm standards — was the top adviser on mergers valued at less than \$750 million in 2005, according to Thomson Financial.

Some of the more established shops, such as Evercore and Greenhill, have grown rapidly by diversifying their businesses and enticing frustrated bulge-bracket bankers to join them.

Of course, veteran bankers have fled big firms before to start free-spirited boutiques. In the mid-1970s, Hambrecht & Quist, Montgomery Securities, and Robertson, Stephens & Co. sprang up to serve Silicon Valley start-ups. All three wound up being acquired by banks in the late 1990s. The firms lacked the capital and breadth to offer clients an array of services, and founders figured it was time to cash in their valuable equity stakes.

The latter motivation hasn't been lost on the latest wave of Street expatriates. Bankers at old-line firms have been getting a smaller share of two things they hold dear: money and power.

Consider the situation at Goldman. In the three years leading up to the firm's 1999 IPO, 17 to 20 percent of its revenues came from advisory fees. By last year that figure had dropped to 7.2 percent — during a merger bonanza. (Goldman officials note, however, that the M&A advice business has a sizable knock-on effect in capital markets and other businesses.) At Morgan Stanley and Lehman, M&A fees account for 5 percent or less of revenues. The real riches are in trading — sometimes for customers but also on behalf of the firms, using their own capital. Critics say some securities firms are now nothing but giant hedge funds.

On Wall Street, where the money goes, power soon follows. Promotions to senior management, as well as the biggest chunks

of the bonus pool, are increasingly going to traders. Goldman president Lloyd Blankfein, who is the front-runner to eventually take over the firm, came up through the trading ranks. So did Zoe Cruz, Morgan Stanley's co-president. Last month Morgan Stanley CEO John Mack appointed veteran M&A banker Robert Scully as co-president, in an attempt to restore a balance of power. But bankers, known as the "House of Lords" at First Boston in Perella's day, and traders, who were the "House of Commons," have been somewhat humbled by the new order.

"As the traditional bulge-bracket firms have become larger, the relative importance of the advisory business has declined," says Evercore's Mestre. "The drivers of profitability — and therefore of organizational importance — have migrated to a great extent to trading."

Adds veteran recruiter Russ Gerson, who heads his own Wall Street search firm, Gerson Group: "Bankers in the largest firms are not necessarily recognized for the value that they add. They are viewed as a commodity alongside lending and capital raising."

Ingenuously or not, some bankers complain that clients no longer really matter at big firms. Veteran M&A banker Herald (Hal) Ritch, a co-founder of Sagent, puts it bluntly: "You have these traders who are in charge of some of the major firms. At times they treat their clients like they're counterparties on a trade."

Changes in the ground rules of the securities business have heightened old-line bankers' unease. In 1999, Congress did away with the Glass-Steagall Act, which for 60 years had barred commercial banks from investment banking. Citi and J.P. Morgan soon muscled their way into deal making by flexing their balance sheets. Today the pair rank third and fourth, respectively, behind Goldman and Morgan Stanley as recipients of M&A advisory fees, according to Dealogic.

Sagent: Staking out the high ground

"Pure advice" is the mantra of Herald (Hal) Ritch and Joel Cohen, the co-founders of Sagent Advisors. The duo, who ran the M&A division of Donaldson, Lufkin & Jenrette when Credit Suisse First Boston bought that firm in 2000, hark back to the days before Wall Street became the preserve of financial supermarkets. The impulse to sell as many products and services as possible, the veteran bankers contend, can cause banks to put their own interests ahead of their clients'. Consequently, two-year-old Sagent eschews securities underwriting, lending and trading.

"In the early days of my career, firms had multiple businesses under one roof," says Ritch, 53, who was global co-head of M&A at Citigroup before forming Sagent. "But it was part of the ethic of the place to be relationship-oriented." Today's financial supermarkets, by contrast, are more transaction-driven, he says.

His new firm, a New York-based partnership that employs 36 bankers, sees its greatest opportunity in offering advice on mergers to middle-market companies. In August, Sagent

advised electronics distributor Carlton-Bates Co. on its \$250 million sale to rival Wesco International. Over the summer Sagent worked with hedge fund Angelo, Gordon & Co. on its \$45 million acquisition of Crunch Fitness from troubled exercise chain Bally Total Fitness.

Sagent's founders, like many other boutique bankers, believe that bulge-bracket investment banks have become so large through multiple mergers that they now focus almost exclusively on big clients, disdaining fees from smaller deals. "The middle market has been abandoned," asserts Cohen, 68, who was an M&A lawyer at New York firm Davis Polk and Wardwell before joining DLJ in 1988.

Sagent also caters to corporate boards, whose decisions are under intense scrutiny following years of corporate scandals and subsequent regulatory reforms. Increasingly, boards want advice from firms like Sagent that don't do underwriting or lending and thus don't pose the same potential for conflict of interest as full-service banks.

Last March, Genworth Financial's board re-

tained Sagent to advise it and to provide a fairness opinion on General Electric Co.'s decision to reduce its stake in the insurer. Also last year the independent directors of Nuveen Investments turned to Sagent for advice on how to handle St. Paul Travelers' public sale of a \$2.6 billion stake in the broker. (Merrill Lynch & Co., Morgan Stanley and Citi lead-managed the equity offering.)

Ritch and Cohen have recruited bankers from big firms such as Bank of America Corp.; Bear, Stearns & Co.; and UBS. But most of Sagent's bankers once worked for DLJ, and the energetic, upbeat spirit of their old firm — a stated objective at DLJ was "to have fun" — resonates in Sagent's Park Avenue offices, which overlook DLJ's former digs.

Cohen and Ritch won't disclose Sagent's results, but they plainly hope the firm can channel DLJ in financials as well as in fun. During DLJ's last five years as a stand-alone firm, when Ritch and Cohen ran mergers, the firm's M&A revenues rose more than 20-fold, to \$883 million.

— P.P.

So-called universal banks such as Citi and J.P. Morgan exploit their lending relationships to win M&A advisory mandates. And like Goldman and Morgan Stanley, they often bundle the advice with capital markets services. Naturally, this makes the brawn of their balance sheets almost as important as the brains of their bankers in the competition for deals. Boutiques, of course, have no such leverage. One example: Mittal Steel Co., a longtime client of Perella's, has engaged a collection of universal banks — Credit Suisse, Citi, HSBC and Société Générale — and Goldman as advisers on its hostile bid for Luxembourg-based rival Arcelor.

Another grievance aired by merger bankers is that the biggest investment banks, having gone public in recent decades, must contend with revenue and earnings targets. That can create pressure to bring in more advisory fees, even if it means counseling clients to do questionable deals.

Starting or joining boutiques can be the best therapy. Most independent advisory shops remain private partnerships. Some, though, such as Greenhill and Lazard — now headed by Perella's old partner, Wasserstein — have gone public recently and now must also confront the challenge of meeting Wall Street expectations. The private boutiques largely don't engage in proprietary trading or capital markets activities, and their shorter client rosters pose fewer conflicts. Bankers say they feel free to give clients the best advice, including to not do a deal.

But the benefits are more than just psychic. Boutiques can be much more remunerative for top bankers than big banks. For a start, bankers have a more direct claim on the profits they earn for the firm. And there's always the chance of becoming fabulously wealthy if the firm goes public or is sold.

Greenhill, following its \$87.5 million IPO in May 2004, currently has a market capitalization of \$1.6 billion. Several of the firm's partners, including its U.S. president Bok, have stakes in excess of \$100 million. Greenhill himself owns 6 million shares valued at a whopping \$387 million. Perella, meanwhile, expects his new firm to generate \$120 million in investment banking fees in its first year and \$254 million in year five. Perella's sizable share of that should keep the Ferrari collector in Testarossas for a while.

"If the deal flow is there, an investment banker at a boutique is in a far better position," says recruiter Gerson. "Without the overhead associated with distribution, sales, trading and capital markets, the margins are very, very high."

Corporate clients are drawn to boutiques for many of the same reasons that bankers are. Some prefer to deal with firms that concentrate on advisory work. That's particularly true for heads of smaller public companies, which don't generate the lavish fees that command the full attention of giant firms. CEOs may also favor boutiques because they're wary of the mounting potential for conflicts of interest at the big investment banks as they grow in size and scope, pushing into more and more once-fringe areas.

Goldman became a focal point for such concern last year when it advised the New York Stock Exchange on its acquisition of



Chad Banks

Sagent co-founders Cohen (left) and Ritch: Focusing on "pure advice"

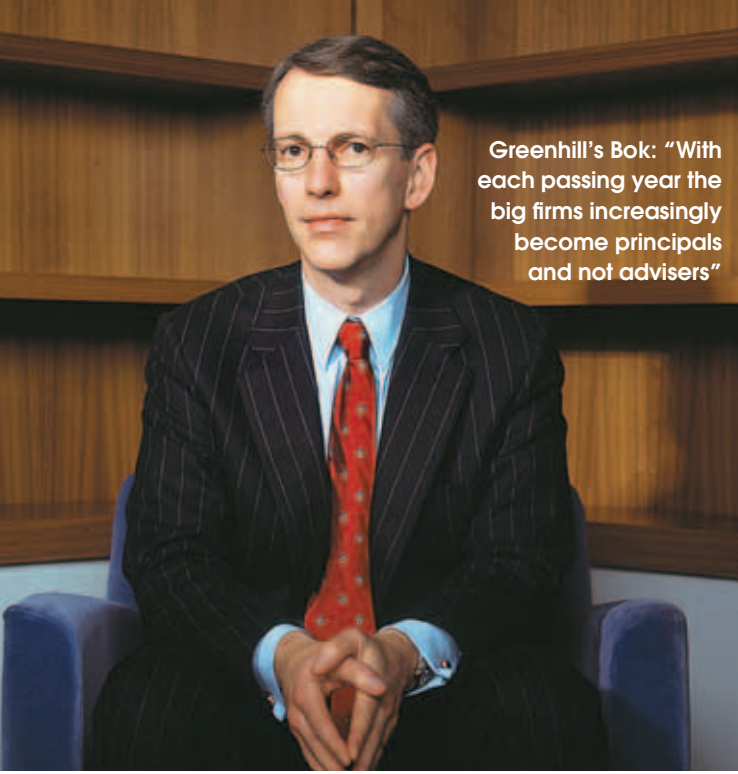
Archipelago Holdings — while simultaneously counseling Archipelago on the deal. Goldman had plenty at stake on all sides: It owned 15 percent of Archipelago as well as 21 of the NYSE's 1,366 seats. Moreover, NYSE CEO John Thain used to be Goldman's co-president and helped to oversee the firm's investment in Archipelago. Goldman has publicly dismissed talk of a conflict, saying that both clients were happy with the deal. But it did bring in Greenhill to provide an independent fairness opinion on the transaction. The NYSE also hired Citi for a second opinion on the deal before moving forward with it.

The potential for conflicts is especially high in leveraged buyouts. Private equity firms like Blackstone Group and Kohlberg Kravis Roberts & Co. have become huge fee generators for investment banks, paying a total of \$1.9 billion to the Street for advisory and financing services last year, according to Dealogic. This year private equity firms have a war chest of \$150 billion, says J.P. Morgan, and thanks to the debt markets, that sum could be leveraged to underwrite more than half a trillion dollars in buyouts.

The influence of buyout firms raises questions about whether banks can fairly advise corporations that compete with LBO firms for deals. "If you are the corporate client and know the person sitting across the table pays a bank \$100 million in fees, you ask, 'How does the bank get tough with that customer?'" says Gerald Rosenfeld, CEO of advisory firm Rothschild North America.

The inconvenient fact that many investment banks have their own private equity divisions may also give corporate clients pause. When J.P. Morgan ran the auction of Dunkin' Brands for Paris-based Pernod Ricard last year, the bank's buyout unit, JP Morgan Partners, was among the bidders. Ultimately, it bowed out of the bidding, and it is in the process of being split off from the bank, which will still retain a smaller private equity business inherited from its acquisition in 2004 of Bank One.

But other leading M&A shops, including Goldman, run big private equity operations that can compete with clients. Morgan Stanley chief Mack has vowed to ramp up the firm's LBO business. Officials at both firms point out that some boutiques engage in private equity investing. That's true: A few, such as Evercore



Greenhill's Bok: "With each passing year the big firms increasingly become principals and not advisers"

Chad Baraka

and Greenhill, have merchant bank units of their own. But these firms tend to focus on big advisory clients while investing as principals in smaller deals, thus minimizing the potential conflict. Most boutiques don't invest as principals or offer financing and thus can hold themselves out as independent, unbiased advisers.

Not surprisingly, the Sarbanes-Oxley Act has been a boon to boutiques, because it impels CEOs and directors to solicit just the sort of untainted advice they purport to provide. This rectitude can lead to unusual mandates. Health insurer WellPoint's \$6.5 billion acquisition of rival WellChoice closed in December. But before the deal could take place, the New York Public Asset

Fund, which owned 62 percent of WellChoice, sought advice on the merits of the merger — and stipulated that it would only consider firms that pledged not to underwrite securities or loans for the merged entity for two years.

Mallory Factor, chairman of NYPAF, which was formed in 2002 to hold WellChoice shares when New York State's health provider, Empire HealthChoice, converted to a for-profit company, wanted to ensure that the fund's adviser would not recommend a course just because it might engender capital markets fees. No major banks sought the mandate. Instead, NYPAF hired Sagent, which earned \$5 million for the assignment, and Blackstone's advisory unit, which got \$1.5 million. Goldman and Lazard, meanwhile, advised WellPoint. Factor, who sits on many corporate and charitable boards, says NYPAF's concerns are not uncommon. "People, as objective as they try to be, will always act to further their economic interests," he says. "It's human nature. The conflicts are very real and not just perceived."

Relationships are another reason boutiques rake in fees. When General Electric Co.'s NBC television unit acquired Vivendi Universal Entertainment last year, NBC chairman Robert Wright turned to his longtime banker, Mnuchin of AGM. The boutique shared \$28 million in fees with Credit Suisse for the \$14 billion transaction. Since then AGM has won a slew of mandates for media companies, most recently representing college sports channel CSTV Networks in its \$325 million sale to CBS Corp. in January.

"When you're a small company," says Brian Bedol, CSTV's chief executive, "you feel there is a much tighter bond and opportunity to work more closely with the principals at the boutiques than there is with the bulge-bracket factories."

But independent firms must also demonstrate that they're able to transcend the existing relationships of founders and new hires to win deals from new clients. One approach they're taking is to stress the blue-ribbon service they provide. "Our big advantage is

Greenhill: Building a legacy

Robert Greenhill founded his eponymous investment bank in 1996 with little more than his Rolodex. Then again, few bankers have ever possessed a better set of contacts. In May 2004, Greenhill & Co. went public in a deal that valued the firm at \$525 million. Since then its market capitalization has skyrocketed to more than \$1.5 billion. Greenhill shares trade at 35 times earnings, compared with just 13 for Goldman, Sachs & Co. Revenues have soared from \$36.9 million in year one to \$221 million in 2005.

Now the 69-year-old Greenhill, who established Morgan Stanley's M&A group back in 1972 and was Smith Barney's CEO for three years before starting Greenhill & Co., is focused on ensuring that his firm can retain its boutique culture — and survive long after he hangs up his deal-maker pinstripes. To be sure, the Minnesota-born fitness fanatic isn't likely to retire anytime soon, say those who know him well.

As boutiques go, Greenhill is something of an anomaly. It employs 150, including 32 managing directors who each generate an average of \$1.6 million in annual revenues.

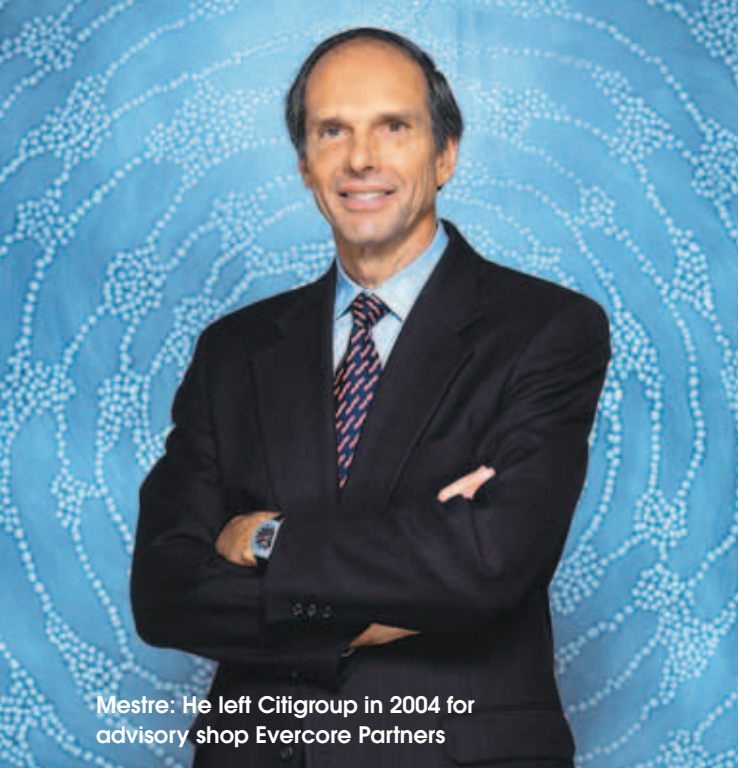
Greenhill has been winning the sort of high-profile M&A advisory mandates that bulge-bracket firms brag about, including MCI's \$7.8 billion sale to Verizon Communications in January. More than half of its advisory revenues come from outside the U.S. In August, for example, the firm advised German tourism and logistics company TUI on its \$2.3 billion purchase of Canada's CP Ships.

Blockbuster deals like these may help explain why Greenhill & Co. is able to attract top talent. "We continue to see growing interest from senior investment bankers wanting to join the firm," notes its U.S. president, Scott Bok.

Still, Greenhill faces complications arising from its very success. Although going public gave it a long-term capital base that can't be un-

dercut, as can a partnership's, by the departure of senior people, it also created pressure to satisfy Wall Street's expectations for revenue and earnings growth — potentially, an incentive to push deals rather than cultivate long-term client relationships. In 2000, Greenhill & Co. started a middle-market merchant banking business to diversify its revenue. Although advisory fees grew by just 9 percent last year, revenues nearly doubled. That makes the firm less susceptible to M&A cycles but adds a potential conflict that many big firms wrestle with: profiting from principal transactions as well as from client work. And as the firm hires more bankers, red tape is bound to appear.

Bok, himself a former Morgan Stanley banker, insists that Greenhill is definitely not a one-man shop and that it is determined not to grow so fast that it resembles the behemoths: "Even doubling in size is not going to create a big bureaucracy." — P.P.



Mestre: He left Citigroup in 2004 for advisory shop Evercore Partners

Chad Barber

the high level of attention our clients receive from senior advisers,” says Evercore’s Mestre, who advised SBC on its acquisition of AT&T. “That is something the large firms, given the breadth of their coverage and client business, simply cannot match.”

Don’t bury the bulge-bracket banks quite yet, however. Even with boutiques flourishing, Goldman and Morgan Stanley remain entrenched atop the M&A league tables. Meanwhile, universal banks, such as Citi, J.P. Morgan and UBS, are throwing more resources into investment banking.

Indeed, not all senior bankers leaving top advisory shops are going to boutiques. In June, Citi hired Morgan Stanley M&A co-chief Raymond McGuire as co-head of global investment banking. McGuire, who learned his trade under Perella, was lured by the prospect of marrying skilled bankers’ intellectual capital with Citi’s financial might — brains and brawn again — to pursue the behemoth’s goal of building the world’s premier investment bank. In December Citi advised Wichita, Kansas-based Koch Industries on its \$21 billion buyout of Georgia-Pacific Corp. Tellingly, the bank provided \$11 billion in debt to finance the deal. Citi also is co-advising BellSouth, along with Goldman, on its pending sale to AT&T.

Big firms and boutiques are not always squaring off. In fact, they often share mandates and fees — a rarity ten years ago. Witness the tag team of Evercore, Lehman and Rohatyn Associates, essentially a one-man shop run by former Lazard chief Felix Rohatyn, on the AT&T-BellSouth deal. About one quarter of deals now feature multiple banks on at least one side. Such arrangements represent a logical symbiosis. CEOs often seek advisers that can provide financing — and banks like Citi that are striving to build their M&A bona fides are happy to accommodate them — but also may want to tap a putatively more objective adviser.

Boutiques may be booming now, but what will happen when the deal-making cycle turns and fees fade? Their senior-most bankers, who are typically already rather well-off, may simply retire or do something else. In an industry so dependent on relationships, such departures can be devastating.

A few boutiques have sought to address the longevity issue by diversifying. Perella’s group plans to make strategic investments in companies and hedge funds. In the last down cycle, Greenhill added a unit that helps restructure troubled companies. The firm raked in \$253 million from that business in 2003, versus \$34 million during the 2000 merger boom. Last month Evercore hired a batch of Sanford C. Bernstein & Co. portfolio managers to start an asset management division.

Another potential fix is to go public. Evercore reportedly was considering an IPO last summer, but it has yet to file a registration statement with regulators. (Evercore officials won’t comment on the possibility of an offering.) Of course, boutiques that go public and embark on new businesses may find themselves caught up in the same conflicts and shareholder-driven fixation on profit for which they criticize their bulge-bracket rivals.

Yet if boutiques prove to have staying power, the merger advisory business could end up being dominated on one end by deal-making powers like Citi that are able to muster capital as well as expertise, and on the other by boutiques proffering concentrated brainpower. Those in the middle — notably, regional banks and brokerages entertaining national M&A ambitions — could fall by the wayside. Bulge-bracket firms like Goldman and Morgan Stanley, which lack the universal banks’ balance sheets, may have the most to lose if talent and clients continue to flee.

In a recent report Bear, Stearns & Co. analyst Daniel Goldberg raised concerns that senior-level defections at Morgan Stanley have damaged client relationships and could hurt the firm’s banking business over the long term. M&A has a drawn-out processing cycle: Mandates don’t result in paid fees until the deals close, often six to 12 months later. And CEOs frequently make one big buy only to disappear for years. The true impact of the defections thus will be felt over the next two to three years.

Morgan Stanley and Goldman executives argue that generations of senior bankers have left without causing permanent damage. Goldman has long been known for its deep bench. And Morgan Stanley CFO David Sidwell assured analysts in January that the firm’s pipeline of impending deals is full to bursting. The execs also point to their ability to connect M&A clients with their capital markets groups as an advantage. A buyer of an energy company, for example, may want to hedge against oil-price swings; Goldman and Morgan Stanley, with top-tier commodities and derivatives groups, can do that in the blink of a monitor.

“Clients want integrated solutions,” says a Goldman spokeswoman. Morgan Stanley won’t comment on the boutique boom.

The most probable scenario for the future: Some boutiques will thrive as companies seek independent advisers to avoid conflicts or to complement the merger financing services of big banks; and the best M&A departments of bulge-bracket firms will also flourish. CEOs will still turn to firms that can provide debt financing along with merger advice, particularly during economic troughs. Despite all the attention paid to trading, M&A is still critical to how bulge-bracket firms define themselves. CEOs seeking an extra measure of security may well decide to pay a bit more to have multiple firms run their deals.

At least one old master, who has seen both sides of the Street, isn’t counting out the old-line M&A houses. “I don’t think these boutiques will supplant Goldman Sachs or Morgan Stanley,” says Perella. “The big firms will cry all the way to the bank.” ■