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PlainsCapital to Buy First Southwest Co. Banking Firm Acquiring Dallas-Based FA

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By Richard Williamson and Jason Philyaw / The Bond Buyer

DALLAS - First Southwest Co., the third-largest financial adviser nationally and the largest in the Southwest, will be acquired by the Texas banking firm PlainsCapital Corp. in a private equity swap announced yesterday.

The acquisition of the 62-year-old First Southwest by the 20-year-old PlainsCapital, both Dallas-based, will add \$500 million to \$700 million to PlainsCapital's \$3.4 billion of assets, according to the two companies.

First Southwest will keep its name as a broker-dealer and a financial adviser operating as a subsidiary of PlainsCapital, the second-largest privately held bank in Texas. Total equity at the combined companies will be valued at \$400 million.

With regulatory and shareholder approval, the deal could close by the end of the year, the companies said.

On a smaller scale, the deal follows similar mergers or conversions to commercial banks. In September, Bank of America acquired Merrill Lynch & Co. in a \$50 billion deal, while Goldman, Sachs & Co. and Morgan Stanley announced plans in September to become commercial banks with a third of the 30-to-1 leverage permitted for investment banks.

Joining the ranks of commercial banks will be American Express Co., which this week also won approval to convert to the new business model. As a result of the change, the nation's largest credit card company by purchase volume could qualify for the Troubled Asset Relief Program for banking firms burdened by toxic assets.

With credit card defaults rising, October was the first month since 1993 that credit card companies were unable to sell bonds backed by customer receipts. So far this year, at least 42 regional banks have won preliminary approval or expressed interest in participating in TARP, funded by \$700 billion approved by Congress.

"The landscape for us has changed," said Hill Feinberg, chairman and chief executive officer of First Southwest. "With the consolidation of all the investment bankers with banks, we felt we were losing the ability to be competitive because the banks have a lot of things we don't have. The pluses are enhanced equity, enhanced funding, and enhanced profitability."

Feinberg will stay on with the new entity and will serve on the board of the merged companies. He will continue to have the same title and First Southwest management will remain in place, he said.

Alan White, chairman and CEO of PlainsCapital, said the deal gives his bank an additional line of business with national reach. He said First Southwest has served as an adviser for his bank for two years and that the idea of a merger came up after another investment banking firm approached him about a merger.

"It was not the right kind of deal, but it got us talking to First Southwest," White said. "This is a deal that we really should have been doing."

Through the first nine months of the year, First Southwest served as financial adviser on 410 deals worth \$16.7 billion.

Feinberg said both companies avoided toxic assets such as collateralized debt obligations that have wrecked the balance sheets of the large investment banks. First Southwest was not burdened by excessive debt, but needed a "level playing field" to compete in the new muni environment, Feinberg said.

A longtime Dallas investment banker familiar with the deal said he wouldn't be surprised if smaller, more regional firms follow First Southwest's lead and merge with more traditional banks, as "everyone in the industry is experiencing some sort of trouble right now."

"Some of these broker-dealer-type companies may be following the larger firms up on Wall Street and looking to consolidate operations," the banker said. "First Southwest, which works as a clearing house in addition to its financial advisory business, may now gain access to the Fed window and more easily access the central bank, which could lead to increased liquidity on very short notice."

Feinberg said that there are no plans for layoffs and that, in fact, he recently hired Richard Ramirez, a former vice president at Goldman Sachs, to run the Austin office. Ramirez was among some 30 Goldman executives laid off recently as the investment bank prepared to announce steep losses. Last week, however, First Southwest lost six key executives who left the company to start their own financial advisory services firm in Austin.

First Southwest is a dominant player in Texas whose former executives fill the numerous positions at other banking firms. The company typically plays a role in any major issue in the state and has advised or financed on landmark projects.

"You'll find that one time or another, just about everyone in the municipal bond business once worked for First Southwest," Feinberg once said.

In financial advisory services, First Southwest's volume in dollars fell 28% in the first nine months of 2008 to \$16.8 billion, compared to \$23.4 billion in the same period of 2007. The number of issues the firm worked on dropped by 100 to 415, and the company's ranking fell to number two in the Southwest from number three in the first nine months of 2007. Market share also fell to 5.3% from 7.3% in 2007.

As a senior manager, First Southwest managed an 8.5% increase in dollar volume to \$2.4 billion on 130 deals, 20 fewer than in the first nine months of 2007.

First Southwest has 22 offices in 10 states and the District of Columbia, employing nearly 370 people, including 220 registered sales representatives. The company has annual revenue of more than \$100 million.

PlainsCapital also owns mortgage lender PrimeLending and asset manager Hester Capital Management. Feinberg said that White's decision to keep those companies operating under their own names and management will also apply to First Southwest.

Founded in Lubbock in 1987, PlainsCapital specializes in middle-market companies and high-net-worth individuals, according to the company, which moved to Dallas in 1999. Earlier this year, it moved its headquarters to the Victory Park development in downtown Dallas.