Will CIBC Capture This $3 Billion Prize?

Description

Sometimes it's easier to take a giant leap than a bunch of baby steps. That now seems to be the attitude of **CIBC** (TSX: CM)(NYSE: CM) as it pursues wealth manager Russell Investments. According to a Reuters report, CIBC is facing competition from two private equity consortia for Russell, which could fetch a price tag of up to $3 billion.

Seattle-based Russell is perhaps best known for its indices, but also has $259 billion in assets under management. In addition, the company provides pension consulting and transition management services.

Ideal for CIBC

Ever since the financial crisis, which hurt CIBC more than any of Canada's other big banks, the company has been in retreat mode, focusing on financial services in Canada. While that has allowed the bank to generate high returns, it makes growth harder to come by. Shareholders are always wondering how CIBC plans to reinvest its earnings – dividend hikes are not enough. One only has to look at CIBC's 10.4x price to earnings ratio, well below the Canadian bank average.

CEO Gerry McCaughey has identified wealth management as a key area of growth for the bank. He eventually wants to see the division reach 15% of earnings. In 2013, that number was 11.4%.

While wealth management is a great business, with high returns and little capital requirements, it can be difficult to pick up market share without acquisitions. CIBC has already made a few in the past five years, most recently its $210 million acquisition of Atlantic Trust. Other deals have included an $848 million purchase of a 41% stake in American Century Investments in 2011, as well as a deal for McLean Budden's private wealth business.

A common theme for the banks

Since the financial crisis, many banks around the world have been selling wealth management businesses to raise money. And Canadian banks have been happy to scoop them up. A perfect example occurred back in 2012, when **Royal Bank of Canada** (TSX: RY)(NYSE: RY) acquired the emerging markets business of Coutts, the wealth division of the Royal Bank of Scotland (RBS was one of the worst-hit banks during the financial crisis).

This situation seems a little bit different. Northwestern Mutual, which owns Russell, has simply stated that wealth management is "not a core part of its business". And there seems to be plenty of interest in Russell. CIBC should be careful it does not overpay for a wealth manager like Russell, no matter how much it is trying to grow its wealth management division.

Foolish bottom line

CIBC's shareholders should generally be pleased that the company is pursuing wealth management targets; it seems like a very good use of its money. But CIBC has to be careful not to overpay; wealth managers are surely not as cheap as they used to be. Time will tell if CIBC ends up taking that giant leap.

CATEGORY

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