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Need For Tech Emerging As Banking M&A Influencer

By **Chelsea Naso**

Law360 (March 14, 2019, 1:33 PM EDT) -- Mergers and acquisitions activity in the banking sector is still largely driven by continuing consolidation and a shifting regulatory environment, but the need for technology is increasingly influencing financial institutions' deal-making.

The hunt for helpful technology is causing banks to consider merger partners' technology offerings when consolidating and is also prompting banks to either acquire or invest in budding technology platforms, especially as they try to court new customers or better serve existing ones with digital services.

"Banks of all sizes are increasing their focus on technology and technological advantages to stay competitive," said Sara Lenet, a Hogan Lovells financial institutions and M&A counsel.

That means inking a merger with a fellow bank to create the scale needed to invest in the type of technology needed to remain competitive, which ranges from payment services and mobile banking to platforms that enhance back-office efficiency.

"It's expensive and the costs are significant to build those sort of technology platforms and improve systems to keep them current and relevant. A lot of banks have found that scale is attractive. The resources that a combined bank can pour into increasing focus on and advancement of technology are better than either bank can do alone," Lenet said.

The ability to increase investment in technology was a key theme in the blockbuster tie-up of SunTrust Banks Inc. and BB&T Corp. SunTrust CEO William H. Rogers Jr. said the $28 billion merger "will accelerate our capacity to invest in transformational technologies" and BB&T Chairman and CEO Kelly S. King described the combined bank as "the premier financial institution of the future."

Banks with the potential to merge with others are seeing their technology offerings under the spotlight. In addition to creating scale for future investment in the space, a merger can give the combined bank a better technological starting point.

"Bigger is better from that perspective," said Omar Pringle, a Freshfields Bruckhaus Deringer LLP corporate and M&A partner.

Some are also skipping mergers with fellow banks entirely in favor of acquiring or investing in technology companies that may help give them a leg up on the competition.

In an analysis of the digital- or technology-focused acquisition activity of the S&P Global 1200 in 2009 through 2017 published in November, Freshfields found that the broader financials industry was the most active acquirer after the tech industry itself in terms of deal count. The industry accounted for 11.1 percent of tech deal volume, according to the report.

Investing in tech companies directly can shift some of the costs and risks associated with trying to develop those capabilities in-house.

"Banks are interested in exploring how to provide new and innovative services to their customers by acquiring or entering into strategic transactions with early-stage technology companies. It's in some ways less risky for banks to do that than trying to divert resources of their own," said Daniel Kahan, a Morrison & Foerster LLP corporate associate.

With that idea in mind, some financial institutions are taking more of a corporate venture capital approach to technology investing and getting behind startups whose offerings could be game-changers.

It highlights a changing perception among some banks that financial institutions will be better positioned in the future if they shift the way they regard themselves.

"It sounds like a little bit of a cliche, but I think the way a lot of banks have developed organizationally is that they are thinking of themselves as being very innovative companies — in some cases, even technology companies — that provide financial services, rather than financial services companies that use technology," Kahan said.

That blending of financial services and financial technology was prominent in the headline-making combination of Fiserv Inc. and First Data Corp. Wisconsin-based financial services technology company Fiserv in January inked a $22 billion all-stock deal for financial services company First Data. Fiserv President and CEO Jeffery Yabuki said he expects the combination "to redefine the manner in which people and institutions move money and information."

Smaller banks are also looking to partnerships with fintech or other technology companies, Lenet noted. This could include joining forces with an online loan provider to underwrite loans that fit into the bank's qualifications or other mobile platforms that can bring in more customers than traditional methods.

"We're seeing increased partnerships between banks and fintech, sometimes even more at the regional and community bank level. These are maybe banks that don't have the resources or don't desire to spend the same amount of money to build really sophisticated mobile or online technology or automated technology, so they partner with fintechs that offer some of that so it's a new revenue stream," Lenet said.

While technology is a key consideration in banking M&A, it's still not the main impetus for deal-making in the industry.

Much of that can be tied to a lessening of regulatory burdens for regional banks as well as the desire to have an attractive level of deposits.

"I think that when they raised the stress test ceiling, banks now aren't going to be afraid to go over the $50 billion level. I think there's going to be more, larger midmarket mergers and potentially more

mergers of equal transactions because of the regulatory market," said Michael Rave, a Day Pitney LLP partner who advises financial services companies.

"Another driver is deposits. I think the deposit market is very competitive these days. I think if you're a bank with very solid, low-cost deposits, that will remain a very attractive target for M&A," Rave said.

--Editing by Katherine Rautenberg and Marygrace Murphy.
