

# Customer Demand Spurs Collection Field M&A

ARM and customer service firms hunt for deals to expand and spread technology costs

By Martin Sikora

**T**he debt collection industry is huge, fragmented, highly profitable, and in the throes of classic systemic change that drives brisk consolidation through mergers and acquisitions.

Growth alone is a grabber for ambitious players. As consumer debt rises and more credit is granted, the industry expands in virtual lock step simply because there are more bills to collect and more clients to collect them for. But that's only one of the forces prompting key competitors to either bulk up or enter the field via acquisition, says Mike Ginsberg of Kaulkin Ginsberg, a Bethesda, Md.-based M&A adviser and consultant to debt collection firms.

On top of obvious growth, he says, M&A is being sparkplugged in what is now known as the asset receivable management industry (ARM) by these factors:

- Credit granters and billers, ranging from banks to utilities to hospitals, are increasingly farming out debt collection to specialized agencies because it's considered a non-core function;
- Mergers in client industries have resulted in fewer but larger customers that are demanding that their collectors get bigger, reduce costs, and become more technologically sophisticated;
- Collection units have found that they can leverage the same infrastructures for diversifying and cross-selling services in such allied areas as purchase of mature and hard-to-collect debt and programs to cultivate

and retain customers of clients; and

- New clients are coming on board consistently, with state and local taxing agencies signing on most recently and federal agencies, including the IRS, expected to deliver another growth kicker in the near future.

"The growth opportunity is tremendous and it's very identifiable," Ginsberg says, synthesizing the rich mixture of strategic drivers. "The industry is large. It's an industry that's generating north of \$15 billion a year in revenues. It's a growth industry in several different areas and it's diversified. It is a very profitable industry and it lends itself to M&A activity for a variety of buyers."

The combination paced a banner dealmaking year in 2004 with Kaulkin Ginsberg estimating that there were 55 ARM deals with combined prices at a record level above \$1.5 billion.

Ginsberg sees three different categories of buyers trying to get a piece of the action through acquisitions — ARM specialists trying to bulk up or settle into closely related niches; customer relationship management (CRM) businesses, call center operatives, and financial firms adding collection capabilities; and private equity groups, some of which are doing buildups.

**NCO Group Inc.**, based in Horsham, Pa., is considered the largest ARM specialist and is one of the industry's most active buyers. In its latest deal, regarded as a large transaction by industry standards, NCO

agreed to buy rival debt collector and ARM manager **Risk Management Alternatives Inc.**, headquartered in Duluth, Ga., for \$118.8 million.

The second category includes a potpourri of firms penetrating the ARM space, such as **West Corp.** and **Convergys Corp.**, both best known for CRM and call center operations, and student loan giant **Sallie Mae**.

West's acquisition log includes the \$178 purchase of **Worldwide Asset Management LLC** in August 2004 while Convergys bought **Encore Receivable Management Inc.** for \$68 million the previous April. Sallie Mae has bagged three acquisitions in firms collecting student loans and buying debt.

Ginsberg says that private equity firms are attracted by ARM firms' growth prospects and profitability. Among the financial buyers active in the field are **GTCR**, **Parthenon Capital**, and **Harvest Partners**, but the slate includes many other smaller players.

Parthenon led a \$167 recap of **Diversified Collection Services Inc.** in January 2004 and Harvest spearheaded a \$127.5 million recap of **Intellirisk Management Corp.** the following May.

Given the strong rate of M&A activity in the industry, opportunities for cashing out through sales to strategic players are good while there are also prospects for picking up smaller stand-alones as add-ons.

"There is continued interest by buyers of all shapes and sizes," Ginsberg notes. ■