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Why more banks are launching IPOs

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By Jackie Stewart

A bullish outlook on the financial sector encouraged more banks to go public this year.

A number of banks were eager to take advantage of investor optimism after last year's presidential election. Several had compelling stories built around high-flying niches, while others were looking to provide liquidity for investors or create a currency for acquisitions.

Eleven banks have held initial public offerings this year, excluding mutual conversions, or almost double the number that took place in 2016, based on data from Sandler O'Neill. Though down from the 15 IPOs conducted in 2014, a year when post-crisis investors pursued exit strategies, momentum could continue if bank stocks remain hot.

"I think the stock market is a factor, but also which banks will have a good earnings growth story," said Vincent Hui, a senior director at Cornerstone Advisors who oversees the firm's risk management and M&A practices. "People will buy into you if you have a good earnings growth story. But we will have some headwinds."

The KBW Nasdaq bank stock index is up about 16% this year, which has spurred more investors to pump more money into bank stocks, industry experts said.

Banks also have cleaner balance sheets and stronger operations compared to the post-crisis years, said Brian Sterling, co-head of investment banking at Sandler O'Neill.

“If you put together good stories, you’ll get increased activity,” Sterling added. “I do think you have some unusual business models [of banks that have gone public] and different approaches with good management teams.”

Banks with unique business models are also appealing to investors.

Esquire Financial looked at the IPOs at Triumph Bancorp in Dallas and Live Oak Bancshares in Wilmington, N.C., as it was preparing to go public, said Andrew Sagliocca, the Jericho, N.Y., company’s president and CEO.

Triumph, which focuses on factoring and other nontraditional businesses, held its IPO in 2014; Live Oak, a major small business lender and technology innovator, went public the following year. Triumph’s stock is up more than 25% this year, while Live Oak’s shares have increased by roughly 35%.

Executives and directors at Esquire, which has a specialization in offering services to law firms, began mulling an IPO in early 2016 to create liquidity for shareholders and allow employees to take an ownership stake in the company. A publicly traded stock also allows the company to access capital markets more efficiently, Sagliocca said.

“We were in a true inflection point,” Sagliocca added. “There were a lot of institutional investors that wanted to invest in a unique business model. The market conditions were stronger than in the past.”

An increasing number of banks with less than $1 billion in assets are bucking conventional wisdom by going public, said Rory McKinney, managing director and head of investment banking at D.A. Davidson. Such institutions can make the leap if they have strong management teams and returns that are beating out larger rivals.

“Investors are always looking to invest in different types of new stories,” McKinney said. “There is interest in the sector as a whole … because of the bright lights economically across the country, tax reform, reg relief. Those things come into play from an investor perspective in connection with an IPO.”

Esquire, with $480 million in assets, was familiar with the view that banks of its size may be too small to go public, Sagliocca said. Investors, however, seemed more concerned about the company’s business model and performance metrics.

Esquire's stock price has increased by more than 25% since its June IPO.

"The proof is we have been successful," Sagliocca said. "Based on the stock price, there's interest I would assume."

M&A is another factor. Aspiring acquirers can benefit from having a stock to offer a target.

"Banks need a currency to do deals," Tom Michaud, president and CEO of Keefe, Bruyette & Woods, said during a recent panel discussion at the University of Mississippi. "Cash can't compete with a bank that can offer stock trading at 2.5x tangible book."

While there is an expectation that IPO activity can remain steady next year, some constraints exist. The number of banks is down 7% from the end of 2015, providing fewer candidates for public offerings. At the same time, there are only so many management teams that have want to go public and have a constructive use for extra capital.

Earnings stories could also be challenged for executive teams that relied heavily on cost cutting to boost the bottom line, Hui said. Some institutions, which have run into concentration limits in areas such as commercial real estate, could face challenges as they try to diversify their portfolios.

Investors could also turn bearish based on a domestic or international shock, noted James Cassel, chairman and co-founder of investment bank Cassel Salpeter. "There's no reason next year shouldn't be good for bank IPOs — but with an asterisk," he said.

"My view in general is that time is never your friend with an IPO because so many things are outside of your control," Cassel added. "If you want to raise capital in the third quarter of next year, you might want to have your head examined as to why not now."