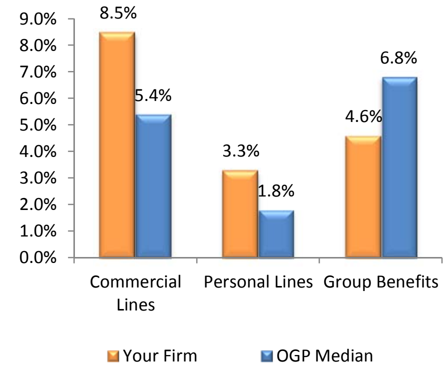
Organic Growth

Total Agency Organic Growth

Your organic growth rank:	**50th - 60th percentile**

Organic Growth by Product Line

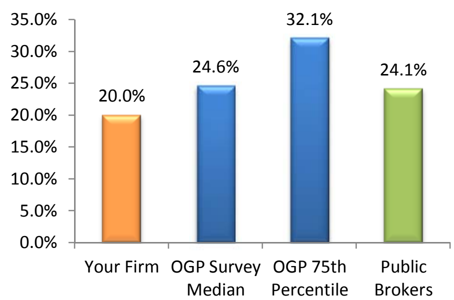


Reagan Consulting Observations

- Median organic growth was 5.9%, a slight increase over the first quarter and slightly higher than a year ago
- For the first time in four years, group benefits outgrew commercial lines, increasing by 6.8% versus 5.4%
- Softening pricing is clearly taking a toll on commercial lines, as its growth slowed for the second consecutive year
- **OGP Projected 2015 Growth: 6.7%**
  Brokers continue to project a second half rebound, resulting in full-year growth of 6.7%

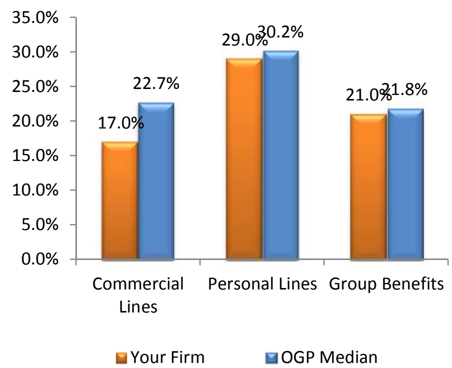
Profitability

Total Agency EBITDA Margin



Your profitability rank:	**30th - 40th percentile**

EBITDA Margin by Product Line



Reagan Consulting Observations

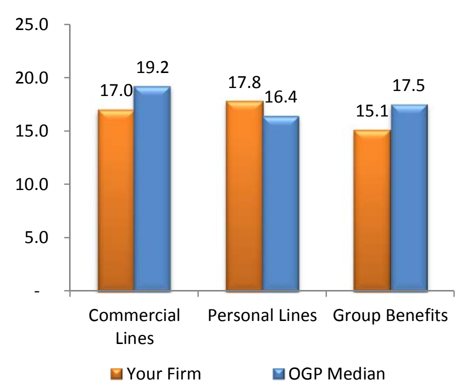
- EBITDA margin increased to 24.6% in Q2 2015, which represents a new record for Q2 profitability
- Median EBITDA figures are inflated by the cash-basis recognition of contingent income, which is largely received in the first half. Thus, as in past years, EBITDA margins will decline throughout the course of 2015.
- While commercial lines margins were identical to Q2 2014, employee benefits margins dropped 230 basis points, possibly reflecting an employee benefits "arms race"
- **OGP Projected 2015 Margin: 20.0%**
  Brokers project a 20% full-year EBITDA margin, which would fall just below the record mark of 21% from 2014

The Rule of 20 (see note below)

Total Agency Rule of 20

Your Rule of 20 rank:	**40th - 50th percentile**

Rule of 20 by Product Line



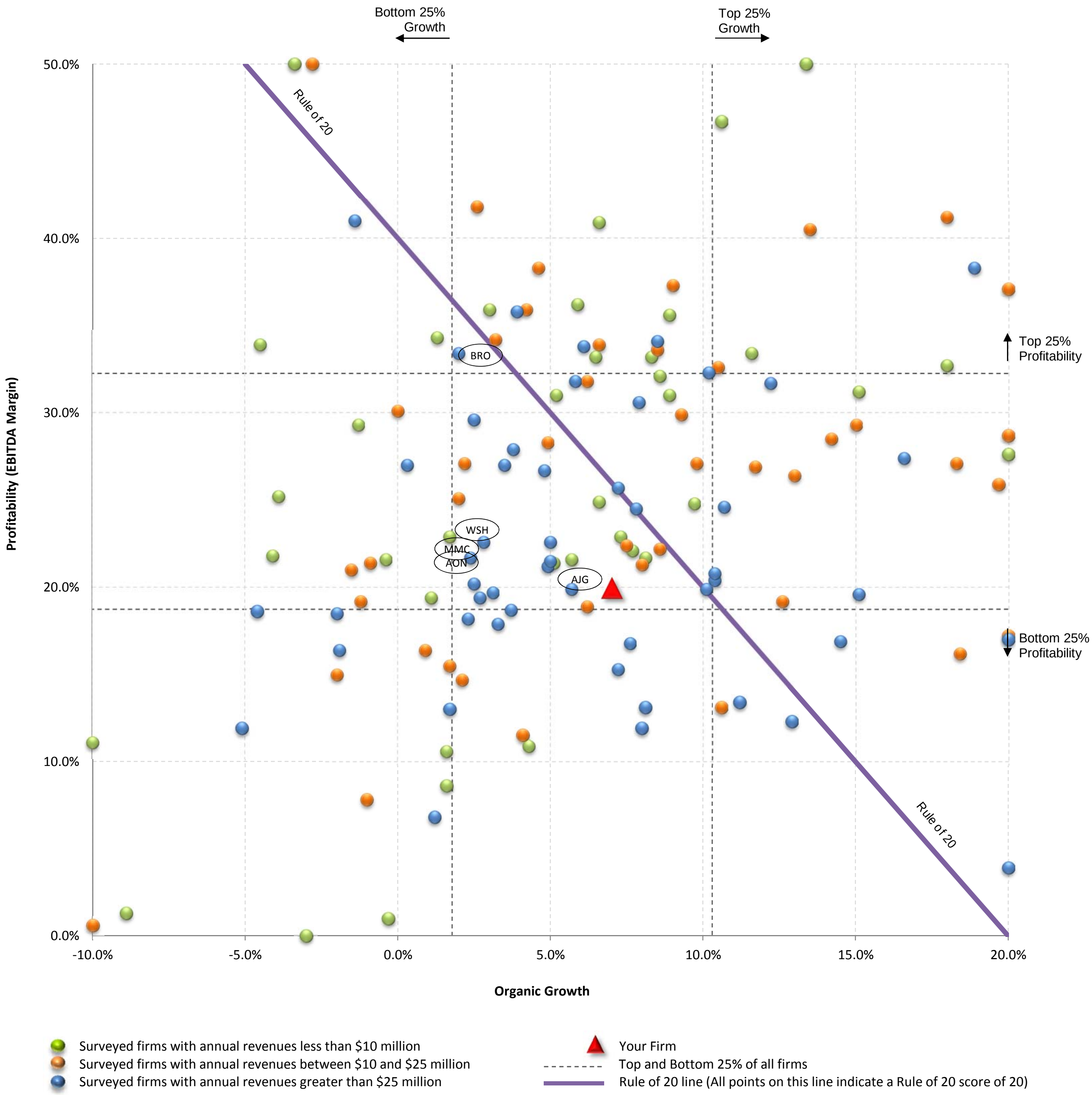
Reagan Consulting Observations

- The 19.0 median Rule of 20 score is the highest second quarter mark in the seven years of the OGP
- Rule of 20 scores, like EBITDA margins, are inflated by cash-basis contingent income and will decline throughout the year
- Rule of 20 scores by line of business were mixed compared to 2014. Commercial lines was flat while group benefits declined due to a material decline in profit margins
- **OGP Projected 2015 Score: 17.5**

About the Rule of 20

Reagan Consulting has developed a metric called the “Rule of 20” to provide a quick means of benchmarking an agency's shareholder returns. The Rule of 20 is calculated by adding half of an agency's EBITDA margin to its organic revenue growth rate. An outcome of 20 or higher means an agency is likely generating, through profit distributions and / or share price appreciation, a shareholder return of approximately 15% - 17%, which is a typical agency / brokerage return under normal market conditions.

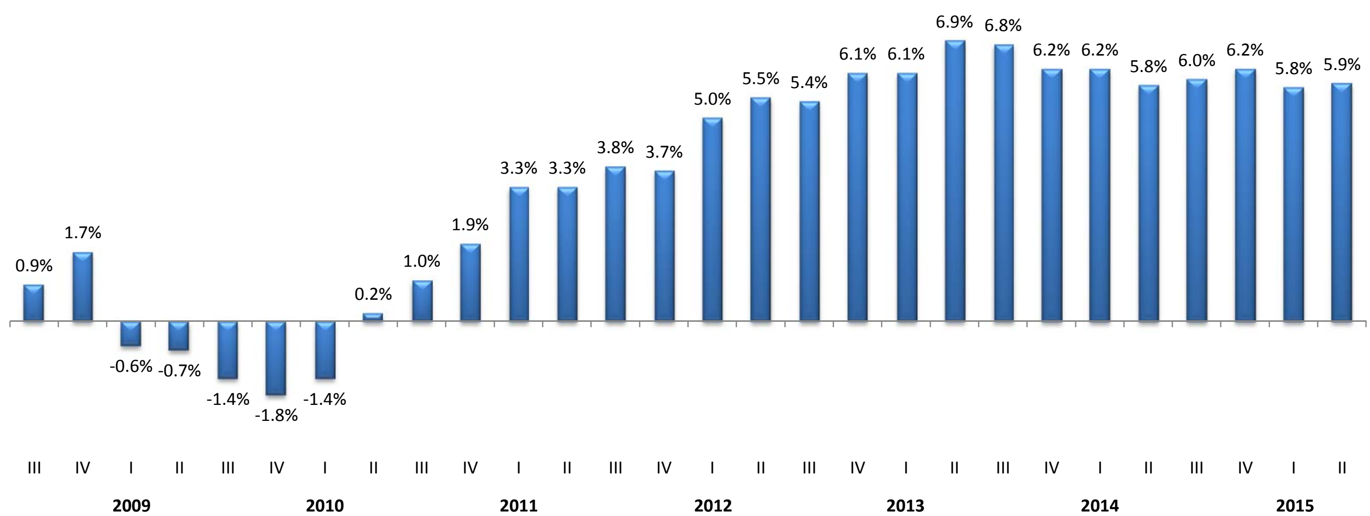
Note: If data for your firm reads "0.0%" or "0.0" it may mean that no data was submitted for that metric.



About the Scatter Plot

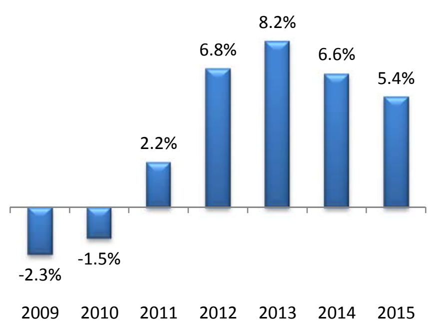
In the chart above, we've plotted every firm in the survey that completed both the total agency organic growth section and the total agency profitability section. Each firm's organic growth is plotted along the x-axis, and each firm's profitability is plotted along the y-axis. We've included a couple of guidelines on the graph to help in interpreting the data. The grey dotted lines show the top and bottom 25% of firms in organic growth and profitability. The solid blue line represents all combinations of organic growth and EBITDA margin that result in a Rule of 20 score of 20. Finally, we've broken the firms into groups based on revenue size, as distinguished by the different colored dots. The goal of this scatter plot is to show the wide range of organic growth and profitability results in the industry and to benchmark where your firm falls.

Quarterly Organic Growth - Total Agency Median (Q3 2008 - Present)

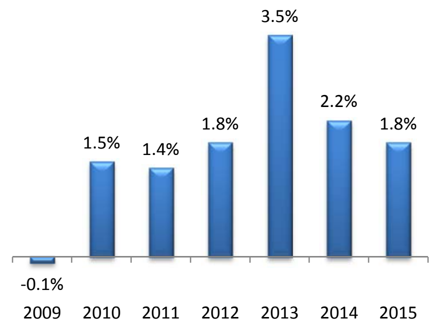


Comparative Median Organic Growth by Product Line (Second Quarter Numbers, 2009 - Present)

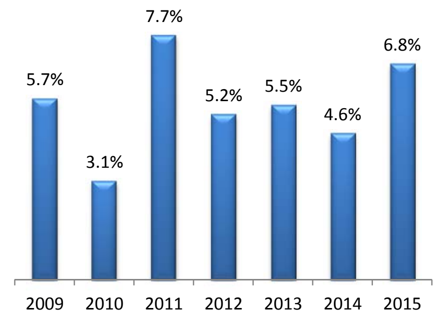
Commercial Lines



Personal Lines

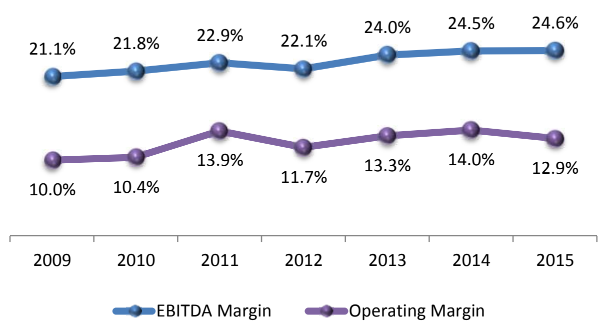


Group Benefits

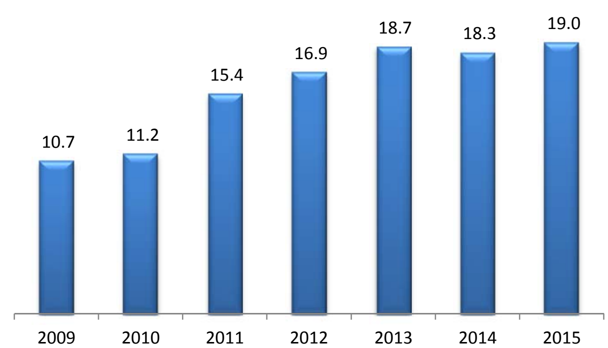


Comparative Median Profitability and Rule of 20 Analysis (Second Quarter Numbers, 2009 - Present)

EBITDA Margin and Operating Margin



Rule of 20



About EBITDA Margin and Operating Margin

EBITDA Margin is calculated by dividing a firm's pro-forma EBITDA (Earnings Before Interest, Taxes, Depreciation and Amortization) by the firm's pro-forma net revenues. Operating Margin is calculated as EBITDA less contingent income, divided by pro-forma net revenues less contingent income.

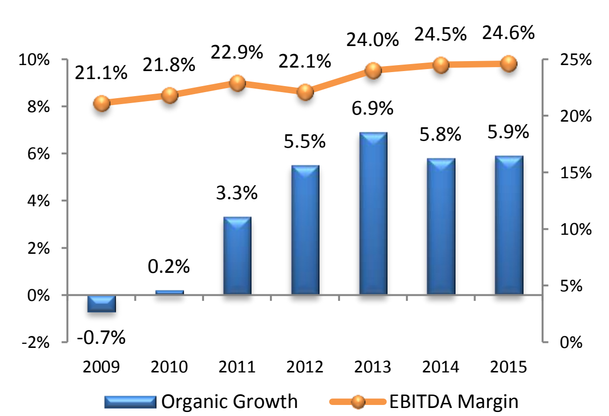
Industry Fundamentals Remain Strong While Consolidation Accelerates

by Kevin Stipe

Times are good for insurance brokers. Organic growth rebounded slightly to 5.9% in the 2nd quarter, up from 5.8% in the 1st quarter. The 5.9% organic growth rate was also slightly higher than the 2nd quarter 2014 figure of 5.8%. Industry organic growth has now been in a relatively tight band of 5% to 7% for fourteen consecutive quarters.

The bump in organic growth helped push Q2 profit margins to 24.6%, which is the highest 2nd quarter margin since the OGP Survey was launched in 2008.

Q2 Organic Growth & EBITDA Margins



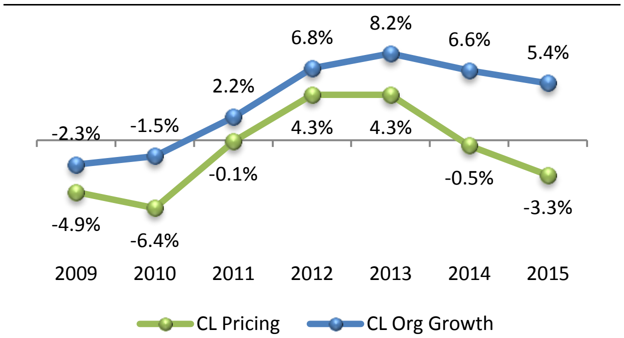
Note: Profit margins will likely decrease during the 3rd and 4th quarters due to the fact that they are inflated by cash-basis contingent income recognition during the first half of the year. Nevertheless, OGP Survey participants are projecting another strong year for industry profitability with a forecast of 20% for the full year.

While the overall results look healthy, there are some interesting trends developing that will need to be monitored going forward.

Commercial Lines

Commercial lines, weighed by softening P&C pricing, is growing more slowly than group benefits for the first time since 2011. The soft pricing trend has accelerated in recent quarters and shows no sign of abating. With the ISO recently reporting that P&C insurers posted their largest quarterly net income in 30 years during Q1 2015, it appears more (and potentially deeper) softening is on the way. If this happens, commercial lines growth will likely decelerate further, and will pull agency-wide organic growth down with it, since commercial lines represents over 2/3rds of the typical OGP firm's revenue.

Commercial Lines Pricing vs. Organic Growth



CL Pricing Source: CIAB

Group Benefits

It is no secret that the group benefits business is undergoing a transformation. This began prior to the passage of Obama's healthcare reform bill in March 2010, and has accelerated further as the implications of the law have come into focus. The U.S. Supreme Court's recent ruling in King v. Burwell seemed to sweep away the last major roadblock to the bill's implementation.

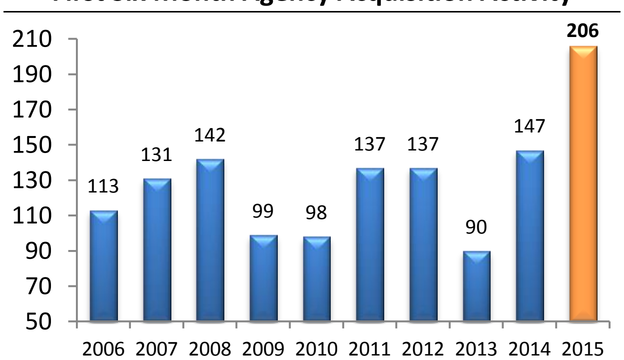
For a while after the bill's passage, OGP benefits growth decreased. This likely occurred for a variety of reasons, including downward pressure on broker compensation and the need for brokers to spend an unusually large amount of time educating clients about the law, rather than producing new business. The most recent quarter showed a significant jump in group benefits growth rates. Whether that growth will continue is anybody's guess.

One thing is sure, though. The Group Benefits Practice Leader role may be the toughest job in the industry. Managing the normal stresses of leading a business segment, while also trying to stay ahead of the game in one of the most rapidly-changing insurance markets in our lifetime is not for the faint-of-heart. Leaders must determine which client segments to pursue, what services to provide for them, and how those services will be paid for. Today's group benefits marketplace resembles an arms race where brokers must make tough choices about which new "weapons" systems to invest in. It is both costly and risky, requiring capital and vision.

Consolidation Continues

The first half of 2015 saw the fastest pace of consolidation in our industry's history, with over 200 announced deals. At this pace the industry will smash the record of 328 deals set in 2012.

First Six Month Agency Acquisition Activity

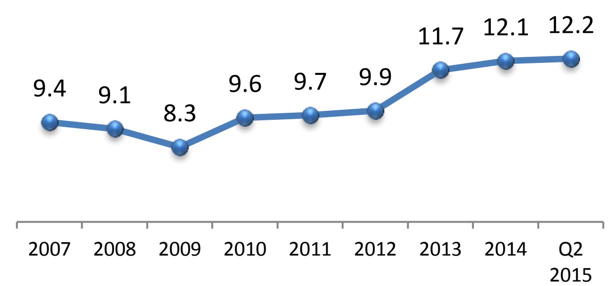


Source: SNL Financial

What is going on? Deal activity is at extremely high levels across a wide swath of the economy, not simply in the insurance brokerage business. It is driven by several factors: companies with record levels of cash are looking for investment returns; firms with relatively low organic growth are being pushed by investors to improve top-line growth; low interest rates are making it very attractive to borrow and use leverage to do acquisitions and supercharge returns.

Finally, despite some recent volatility, the stock market has maintained its strength and publicly-traded broker multiples have inched even higher in 2015, giving buyers an even stronger acquisition currency.

Public Broker EBITDA Multiples



Source: SEC Filings

As a result, a wide variety of publicly traded, private-equity funded and employee-owned brokers are all vying for deals and in many cases paying record levels to try to entice firms to join them. It is turning the industry on its ear. During just the first two quarters of 2015, five firms on the *Business Insurance* Top 100 list were acquired. More will inevitably follow.

Perpetuation Planning

Many of the industry's most successful firms are firmly committed to long-term independence, believing that a key to their success is the ability to offer meaningful ownership to high performers while remaining in control of their destiny. Reagan

Consulting's valuation data confirms that it is tough to beat the employee ownership model. Over the past 20 years, ownership of even a modestly-performing agency has been an outstanding investment. Will this continue? We expect that it will.

But today's acquisition activity and high valuations are testing the resolve of independents. Long-term private ownership doesn't happen by accident. It requires careful planning and monitoring.

To assist agency principals in remaining independent, in 2010 Reagan Consulting published *The Private Ownership Study.* In the study, we found that long-term independence depends on an agency's ability to build and maintain the Four Pillars of Perpetuation.

Of the four pillars, the greatest struggle for most agencies today is building a team of Able Buyers with the capability and interest in purchasing the company from the current owners. To address this, in 2014 Reagan Consulting published the *Producer Recruiting and Development Study*.

The Four Pillars of Perpetuation

Leading firms that participated in both studies have shown that with leadership's resolve and the proper focus and execution, long-term private ownership is as attractive today as it has ever been.


Reagan Consulting
Strategy • Valuation • M&A
Top 100 - 2015 Transactions
WGA WILLIAM GALLAGHER ASSOCIATES
Boston, MA
was acquired by
Arthur J. Gallagher & Co.
MHBT
Dallas, TX
was acquired by
MARSH & McLENNAN COMPANIES
COOK MARAN & ASSOCIATES
Trust Is Our Policy
East Hampton, NY
was acquired by
Prime
J.W.TERRILL
St. Louis, MO
was acquired by
MARSH & McLENNAN COMPANIES
HDH GROUP
Pittsburgh, PA
was acquired by
HUB International
Reagan Consulting congratulates these outstanding companies on the completion of highly successful transactions. It was our privilege to have been engaged by the sellers, all among the top 100 largest brokers, in each of these transactions.
If you are considering a sale or acquisition, or if you want to remain privately held, call us to see how our experience can work for you.
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