Reagan Consulting

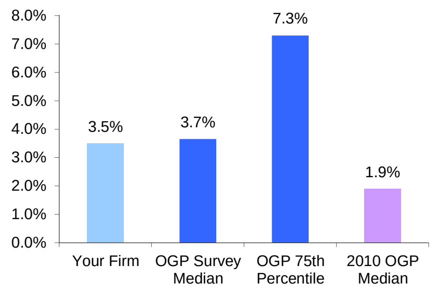
Year-End 2011
OGP ID: 9999

Organic Growth & Profitability Survey (OGP) - Year-End 2011

- Median annualized revenue for surveyed firms is approximately $14 million, average is approximately $24 million. All U.S. geographies represented.
- In this Year-End survey, we have provided a comparison to 2010 OGP results in lieu of public broker results, as not all public broker results have been released.

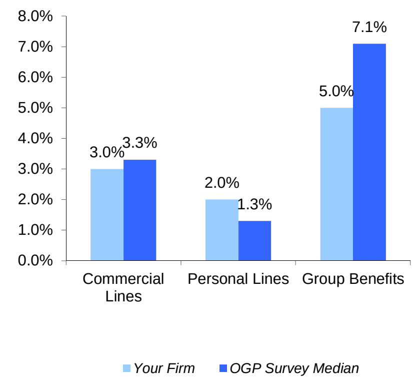
Organic Growth

Total Agency Organic Growth



Your organic growth rank:	40th - 50th percentile

Organic Growth by Product Line

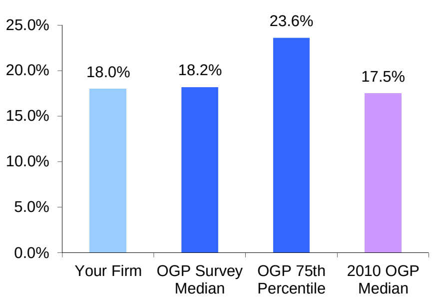


Reagan Consulting Observations

- Median organic growth for the year was 3.7%, the highest annual figure in the four-year history of the OGP survey
- Median organic growth in 2011 of 3.7% almost doubled last year's 1.9% mark
- Despite the positive news, brokers missed their projected growth of 4.2% by 0.5% - and growth for the full-year (3.7%) was slightly lower than growth through the first three quarters (3.8%)
- **OGP Projected 2012 Growth: 5.0%** Brokers are optimistic about 2012, projecting a median organic growth rate of 5.0% for the coming year

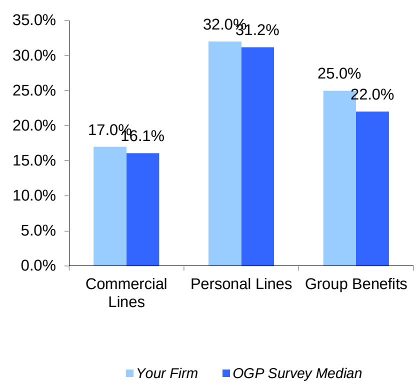
Profitability

Total Agency EBITDA Margin



Your profitability rank:	40th - 50th percentile

EBITDA Margin by Product Line

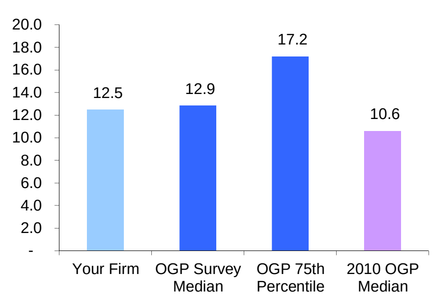


Reagan Consulting Observations

- Median EBITDA margin improved slightly in 2011, marking the second straight year of margin improvement
- From a profitability perspective, brokers slightly exceeded their projections, posting an 18.2% margin versus a projected 18.0%
- Contingent income, an important driver of profitability, was up 2.7% for the median firm in 2011
- **OGP Projected 2012 Margin: 18.0%** OGP firms are projecting consistent margins in 2012, despite a strong growth projection

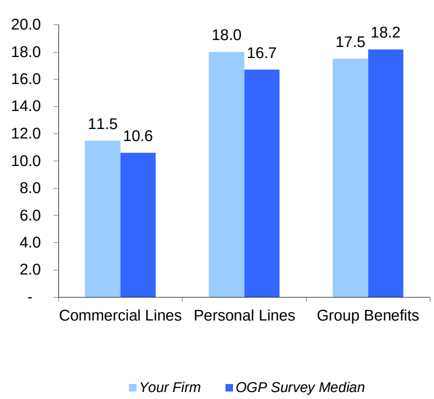
The Rule of 20 [(1)]

Total Agency Rule of 20



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

Rule of 20 by Product Line



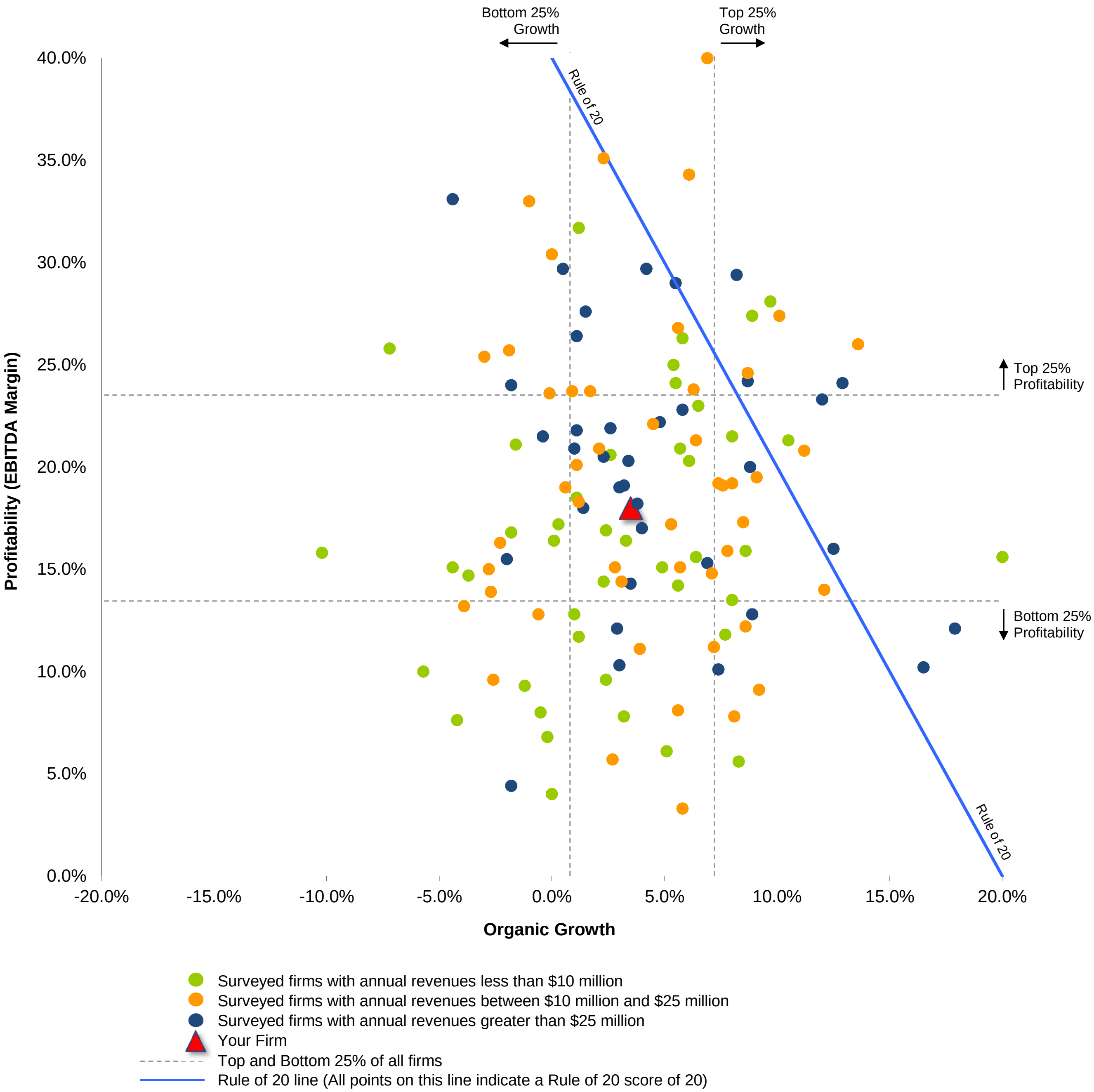
Reagan Consulting Observations

- Rule of 20 results, and thus shareholder returns, continue to rise - the 12.9 Rule of 20 score recorded this year is almost double 2009's score of 7.0
- 14% of all OGP firms recorded a Rule of 20 score of 20 or better in 2011, versus 10% in 2010
- All lines of business posted double-digit Rule of 20 scores, with group benefits leading the way at 18.2
- **OGP Projected 2012 Score: 14.0** Continued improvement in shareholder returns projected by brokers in 2012

(1) 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 distributions and / or share appreciation, a shareholder return of approximately 15% - 17%, which is a typical agency / brokerage return under normal market conditions. Given current market conditions, however, few firms are achieving a score of 20 or better.

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

Agency Organic Growth & Profitability Scatter Plot



About the Scatter Plot

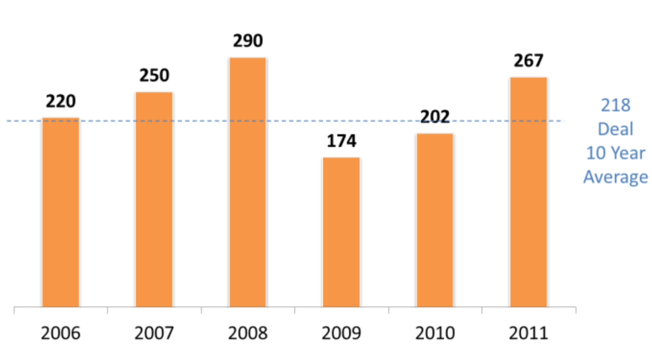
In the chart above, we've plotted every firm in the survey that completed both the total agency organic growth section and the total agency profitability section. Each firm's organic growth is plotted along the x-axis, and each firm's profitability is plotted along the y-axis. We've included a couple 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.

M&A Activity Was Strong in 2011. Will it Continue in 2012?

by Kevin Stipe

Merger & Acquisition activity rebounded sharply in 2011. In fact, the 267 deals announced in 2011 nearly reached the record of 290 deals consummated in 2008. So after the relatively quiet years of 2009 and 2010, the industry just experienced the second heaviest year on record.

Number of Deals (2007 - 2011)



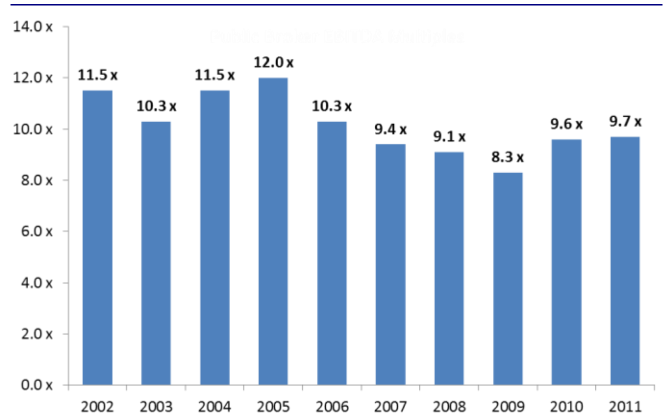
Source: SNL

Will this pace continue? Understanding the factors that drove 2011 activity can help answer this question. There were four factors that drove the heightened pace in 2011. If they continue into 2012, there is no reason to believe that we won't see another year of rapid consolidation.

1. *The return of sellers*. In last year's M&A commentary, we noted that the wild-card for 2011 would be the return of the seller. Would an extension of the economic rebound result in stronger valuations and also more optimism about the ability to receive substantial earn-out money in deals? Would the optimism pull would-be sellers off the sidelines and into the game? The answer turned out to be a very strong yes! And today, with OGP participants forecasting another acceleration of organic growth to 5% in 2012, there is no reason to believe that deal activity will slow. If anything, we anticipate the pace will likely accelerate once again.

2. *Public broker valuation multiple expansion*. Over the last two years, public broker valuations have risen significantly, outpacing their growth in earnings. This is important because it means the brokers have an increasingly powerful currency with which to acquire others. Today, public brokers are trading at nearly 10 times their reported EBITDA, which is the highest level since 2006. With their own higher valuations, there is a greater incentive to buy private agencies and leverage the difference between the multiples of private firms (typically 6-8 times EBITDA) and their own valuations at 10 times EBITDA.

Public Broker Valuation Multiples (2002 - 2011)



Source: Public Filings and Press Releases

3. *Land grab by new buyers.* In 2009 Marsh launched its middle market strategy with the creation of Marsh & McLennan Agency. Within its first two years, Marsh & McLennan Agency acquired over $300 million of middle market revenue by acquiring several marquee agencies. In 2011, it was AssuredPartners' turn. This upstart, launched by

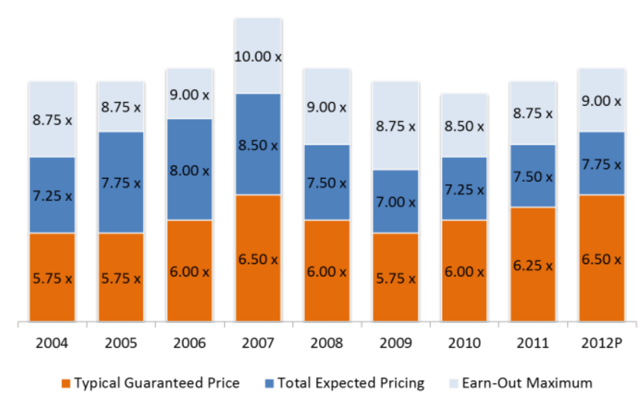
two former Brown & Brown executives, has closed four deals totaling over $160 million during the past five months. These firms turned an already crowded field of buyers upside down by aggressively acquiring some of the largest private players in the industry.

4. *Acquisition imperative caused by continued low organic growth*. The resumption of organic growth in 2010 and 2011 has been fantastic news for the industry after the disastrous contraction of 2009. At the same time, the 3.7% achieved by OGP firms in 2011 is still weak by historic standards, and is certainly not enough to satisfy industry investors or provide opportunities for profit margin expansion. As Arthur J. Gallagher CEO J. Patrick Gallagher noted in AJG's earnings call, "If organic is over 3%, you'll see a bit of margin expansion assuming a low inflationary environment. But below 3%, don't expect margin expansion." At 3.7%, there isn't much room for margin expansion, so many firms turn to acquisitions, which accelerate growth and allow for greater profitability.

VALUATION TRENDS

Valuation multiples increased in 2011 for the second straight year. We believe, in light of continued strong buyer demand, multiples will likely push slightly higher in 2012, as shown in the chart below.

Deal Valuations (2004 - 2011)



Source: Reagan Consulting Analysis

We believe that for mid-size and large healthy agencies, average guaranteed pricing (the multiple delivered to the seller regardless of post-closing performance) will hit 6.5 times EBITDA, another quarter point above the 2011 level. Expected and maximum earn-outs will likely trend slightly higher as well, as sellers feel more confident about their future results and negotiate with buyers over larger earn-outs if superior results are actually achieved.

Of course, average deal multiples can paint a misleading picture of how buyers actually price their deals. EBITDA multiples vary greatly from one deal to another, depending on the unique characteristics of the firm being purchased. What firms are receiving the highest valuations in today's marketplace? We see five attributes that tempt buyers to relax their pricing discipline.

1. *Strong sales culture.* Over the long-run, consistent growth is the key to driving shareholder returns. The most valuable agencies in the industry are those that build a dynamic team of well-trained and well-equipped producers who are free to focus their attention on continually expanding their customer base.

2. *Operational excellence.* Execution, discipline, productivity and efficiency. These are words frequently used to describe agencies that are extremely well managed. Buyers are more comfortable aggressively pricing a deal for an agency that has consistently demonstrated good management and high profit margins. The post-closing performance risk is perceived to be low.

3. *Specialization.* Agencies that specialize tend to have higher new business closing ratios, better account retention, and better profit margins than most generalists. As a result of their faster growth and higher profitability, specialists are worth more – often 50% or higher – than a similar-sized generalist. With buyers aggressively trying to build specialty practices within their own organizations,

valuations of specialist agencies have soared in recent years.

4. *Large account expertise in Employee Benefits.* A huge number of large benefits accounts (those over 100 lives) are still handed by small benefits brokers. This is partly because benefits carriers haven't forced consolidation like P&C carriers have. As acquirers are themselves scrambling to focus on the over 100 life segment, they have engaged in an arms race of investments in value added resources. The acquirers are then seeking to leverage these investments by buying agencies with large accounts and with producers trained to sell value added resources.

5. *M&A experience and relationships.* Today's acquirers are more commonly constrained by a lack of quality acquisition candidates than they are a lack of capital. As such, an acquisition that immediately expands the field of quality candidates can be extremely valuable. An agency leadership team with deep and successful experience in acquiring and integrating other agencies can be especially valuable to a private equity player.

There is actually a sixth attribute, but it is so important and all-encompassing that it can't be confined to our list. Every buyer talks about it. All seek to find it. It is the quality of an agency's people. As professional services businesses, it is axiomatic that an agency is only as good as its people, and that the very best agencies are simply collections of the best people. So while financial and operational due diligence are important, getting to know an agency's people is the most important aspect of any acquisition.

Absent an economic calamity, 2012 should be another banner year for acquisitions, with deal activity and pricing continuing to rise. This is exciting news for an industry that has weathered the challenges of the past decade as well as any.

Reagan Consulting has a singular focus on the insurance distribution system. We have advised many firms – including over half of the top 100 brokers – on strategy, valuation and mergers & acquisitions. With our M&A practice, we are active participants in the deal marketplace for agents and brokers, working on sell-side, buy-side and merger transactions. Since 2007, we have advised on almost 60 transactions with a total deal value over $1 billion. Selected transactions from 2010 and 2011 are presented below.

The Gleason Agency, Inc. and Gleason Financial, Ltd.

Have been acquired by

Arthur J. Gallagher & Co.

Reagan Consulting advised Gleason

2011

Potter Holden & Company

Has been acquired by

Arthur J. Gallagher & Co.

Reagan Consulting advised Potter Holden

2011

LaMair Mulock Condon

Has merged with

Molyneaux Insurance

Reagan Consulting advised LMC

2011

Plumhoff & Associates

Has been acquired by

USI Insurance Services

Reagan Consulting advised Plumhoff

2011

RJF Agencies

Has been acquired by

Marsh & McLennan Agency

Reagan Consulting advised RJF

2011

Brown & Riding

Has merged with

Alexander, Moorford & Woo

Reagan Consulting advised Brown & Riding

2010

Haake Companies

Has been acquired by

Marsh & McLennan Agency

Reagan Consulting advised Haake

2010

Thomas Rutherfoord, Inc.

Has been acquired by

Marsh & McLennan Agency

Reagan Consulting advised Rutherfoord

2010