



## **Got The Urge To Merge?**

Posted by [Sam Friedman, NU Editor in Chief](#) in [Sam's Views](#)



Many independent agencies struggling to survive in this anemic economy are eager to sell or merge with a bigger operation to bolster their leverage with carriers, gain access to new markets and achieve economies of scale. But even though the credit crunch is not necessarily dampening buyer appetites, pulling off a deal is far from a slam dunk these days, principals are being warned.

I moderated a panel of some of the biggest buyers in the business yesterday, presented by Hales & Company and sponsored by the folks over at FC&S Bulletins—a National Underwriter Company subsidiary. They offered some very keen insights into the hurdles agencies must clear to attract a buyer and earn top dollar on a sale in this capital-starved market.

Among the major points cited by the buyers is that it's hard to value an independent agency these days, given the fact that with the bottom falling out of the economy, even achieving a 100 percent renewal rate will normally mean lower revenue for agents, since so many clients are cutting back operations and laying off staff that insurable risks are down considerably.

I also raised the issue that any agency with a substantial book of group benefit business is similarly hard to price, since health care reform might cut premiums or profitability or pull the rug out from them altogether if a government plan is part of the package.

Buyers on the panel—including representatives from the prolific Brown & Brown (which buys almost an agency per week), Hub International, Alliant, Ascension, Wells Fargo and Digital Insurance (a benefits broker buying small group books)—estimated that on average, they closed about one out of five deals they seriously explored. That means about 80 percent of sellers come up empty.

One sure deal-breaker appears to be having too much invested in any one client. One buyer reported coming across an agency for sale drawing 25 percent of its revenue from a single account. Talk about putting all your eggs in one basket!

The buyers also wanted to make sure the seller's top producers were on board, as defections could seriously undermine the agency's value, even with non-compete clauses. Indeed, one of the panelists noted that while "all buyers run the same numbers—they are formulaic and objective—they don't drive a deal. There has to be chemistry within the selling agency and with the buyer. There has to be harmony among the top sales people," or else the buyer is likely to walk away.

One of the buyers goes so far as to survey key clients via a third party to check on satisfaction with and loyalty to the seller, although a fellow panelist was skeptical about such a move. "That could be a two-edged sword. Most don't want word getting out about a sale until the deal is done. You don't want to make clients nervous about their agent's future."

The buyers also seemed more interested in keeping key agency principals on board long after a sale, rather than just serving as an exit strategy for a seller looking to pack it in. The buyers were especially enthusiastic about working with a seller who wants incentive compensation as part of the deal, based on their future production. "We like sellers who are looking to make more money for themselves by making more money for us by paying them like a producer," quipped one panelist.

The good news is that money seemed to be no object for these buyers, in terms of accessing capital even in the current credit crunch. Brown & Brown, for example, noted that it generated a lot of cash given its operating margin, and while it has a line of credit available, prefers to finance deals internally. Others have private equity capital at their disposal.

One potential buyer conspicuous by their absence was the Marsh & McLennan Agency launched last October by mega-broker Marsh as a separate entity to serve the middle-market. Ambitious plans were announced to build a new, national network of independent agencies via acquisitions, but here we are more than six months later, and I haven't heard of a single purchase to date.

Just like having the banks buying more insurance agencies to diversify their revenue stream pushed sales prices higher for sellers, having a behemoth like Marsh enter the market gobbling up agencies like a modern Pac-Man to build their new subsidiary should have the same effect. But for the moment, it's been all talk, no action.

Although fewer deals are getting done in this economy, the panelists agreed, the fact is that sales and mergers are being executed with regularity. All it takes is finding the right dancing partner. That was music to the ears of the sellers in the audience.

What do you folks think of the M&A market? Feel free to share your hopes, fears and experiences here.