insuranceage

Opinion: The broker beauty parade

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Morphose Capital Partners' Nick Atherton reveals how brokers can make the most of a post-pandemic uptick in M&A activity

It's never 'the' time for a brokerage to sell. That choice and the circumstances behind it are as individual as you are. But once the decision to sell has been made, it's time to look at what needs to be done to get your business shipshape and sale ready. That means understanding buyer motivation, who makes the best suitor and what you need to do to be the belle of the buyout ball.

What's in it for buyers? The benefits of snapping up a healthy brokerage are clear. For example, instant access to new geographies or sectors where the target's existing brand value and market penetration mean an easy route to expansion. According to Deloitte, expanding existing distribution channels is the top M&A reason for European insurers, while adding new ones is the third highest priority. The new breed of digitally-native start-ups are ripe for acquisition, injecting tech savviness that legacy organisations struggle to grow themselves which Deloitte notes is a particular aim of North American insurers.

Despite the pandemic, insurance M&A activity continues, although down a little on previous years. Research by the Cass business school shows that, compared to 2019 when there were 774 deals, in 2020 there were only 674 deals valued at more than $100m, the lowest number since 2009. But, this trend is reversing. In the last quarter of 2020, 246 deals were completed globally, compared to 210 in the same period the previous year. *The Insurance Broker M&A Outlook 2020* also showed that 2019 saw a particular increase in activity from PIB, Ethos Broking and Global Risk Partners. In the UK, 48% of M&A deals were consolidations and a substantial 71% involved private equity (PE) firms.

Finding funding

Why so much focus on PE? While insurance undoubtedly took a hit from the pandemic, it's an industry in much more robust health than, say, travel. Pandemic-resistant business lines such as healthcare, grocery or logistics are attractive, as are organisations with high levels of recurring premiums. These are compelling targets for equity firms with pent up funds and reduced opportunities for investment elsewhere.

PE may well be the catapult brokerages need to access new markets or broader customer segments but it's not necessarily a long-term financial relationship. PE is often more an affair than a marriage. Investors would typically be looking to cash out within three to five years.

The perfect deal depends largely on the brokerage and its aims. The management buyout, for example, is ideal for leveraging in-house expertise to sustain growth. It keeps continuity, meaning it's largely business as usual.

Culture is important. Even if the aim is to acquire territory or channels, personnel matter. When we acted as adviser to Borland Insurance on its recent acquisition by US broking firm AssuredPartners, it wasn't just details of the agreement that counted. AssuredPartners were also a great cultural fit. Without it, the deal wouldn't have left the starting blocks.

Earnouts commonly feature in M&A deals. A post-closing purchase price payment, contingent on the business meeting defined goals over a timeframe agreed in advance. They're useful for ironing out differences in opinion on purchase price and offer the buyer surety, only paying some of the sale price upfront and the remainder based on its future performance. Often the seller stays on for a period to keep continuity and help meet goals so, more than ever, the partnership needs to be right.

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What am I worth? That's the million-dollar question and the answer is frustrating: it depends what you're selling. A valuation in the high single digit multiples of Ebitda is realistic for insurance brokers but the structure of the
deal matters. Getting that right – earnout versus all cash, for example – is a delicate but crucial negotiation. It pays to appoint a specialist M&A adviser to secure the best outcome.

There is much a broker can do to get in shape for the big deal: streamline operations, make sure earlier acquisitions are fully integrated, collect in aged debt and get corporate documentation up to date. Also, define and refine your USPs. Understand and promote your business, explore trends and forecasts so your buyer knows exactly what they're getting and has confidence.

Equally, anticipate and resolve problems that could be thrown up during due diligence, like previous irregularities or disputes. Buyers don't like surprises. Deals have come undone simply by failing to comply with FCA capital adequacy rules.

Green shoots of recovery are all around. Pent-up demand in PE combined with large brokers hungry for acquisitions spell a fertile time for M&A activity. Now's the time to take advantage.

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