Covid-19, Agency Value, and Insurance M&A

The changes to our way of life have substantially changed (at least temporarily) due to Covid-19. But how does that affect agency value and your plans to buy or sell an agency? While the insurance industry is relatively recession proof, Covid-19 can and will have an impact on insurance industry M&A in addition to how we currently run our agencies.

Buyer's Perspective

Interest rates are about as low as they can get which means the cost of borrowing is low for people with good credit.

The large, private equity buyers would rather put their money is something relatively stable compared to the wild gyrations of the stock market. Even smaller buyers would rather invest in something they can control rather than the stock market.

For smaller borrowers, the Small Business Administration is a common source of loans for insurance agency acquisitions. The SBA is now contemplating changes to stimulate the economy. These changes include:

1) Reducing or eliminating the SBA guarantee fee charged to borrowers, which will significantly reduce closing costs on SBA loans. The current SBA guarantee fee on a $2 million loan is over $50,000.
2) Increasing the loan guarantee amount from 75% to 90%. This will help entice lenders/financial institutions to want to lend rather than hold on to cash.

Seller's Perspective

Many sellers believe a hard market is coming and that will increase premiums, commissions, and therefore the profitability (and value of their agency). This may be true, but there are several offsetting issues that need to be addressed.

Commercial lines focused agencies will probably be seeing clients with return premium audits due to below expected revenues and payrolls. This will result in return / reduced commissions, thereby reducing agency profitability.

Depending on how long this virus persists and its long-term effects, many small (and even larger) businesses may go out of business. This is especially true of agencies that have a market niche of restaurants and hotel/motel, etc. How will those agencies make up the lost commission income?

Personal lines focused agencies should be relatively unaffected unless the country enters a longer recessionary period. During a recession, people are trying to save money whenever possible. This could result in more homeowners and auto clients shopping their business. Agencies will have to work harder to retain this business.

Assuming a recession persists for a long period of time, this could result in people abandoning their homes (and related home loans) and allowing them to go into foreclosure. This could result in lost accounts for an agency.

Taxes

Prior to the Covid-19 crisis, many agency owners nearing retirement were concerned about the 2020 election. Assuming a democrat would win the Presidency, there was a greater likelihood of taxes increasing. This would result in the "cash in pocket" after selling the agency and paying taxes being less.

With the dramatic drop in the stock market and the concern over Covid-19, the chances of President Trump being re-elected has gone down. Even if Trump is re-elected, Congress is spending trillions of dollars to support the economy. Sooner or later that bill will come due and taxes will have to increase for everyone.

The Changing Agency Environment

With Covid-19 and even beforehand, agencies are learning they don't need to be face-to-face with clients. Phones, email and videoconferencing works just fine in communicating with clients. Agencies that are paperless and automated can allow employees to work from home a little easier in this new environment. However, this means the agency owner needs to learn how to manage remote employees, handle IT issues, cyber liability concerns, workflow, etc. Agencies that aren't as automated may still need to have employees come into the office. Is this feasible if you have employees with children while schools are closed? And what if one of your employees catches the virus from another employee? Now you are looking at a potential workers compensation claim. These are only a few issues to consider. Many other issues will surface as we move through time with life in this "new normal."

The Future

In our ever-changing world, with people flying all over the planet, odds are that this may not be the only pandemic we will face. For insurance agency owners nearing retirement, perhaps now is the time to seriously consider retirement options. For buyers, interest rates are very low, and money is readily available. This pandemic could result in a significant increase in insurance industry M&A activity.

Whether you are in agency leadership and/or want to consider agency ownership in the future, now is the time to consider and evaluate ALL your options. Plan for your agency's future – both strategically (3-5 years out) as well as handling current operational workflow challenges that you will be facing. Whether you have employees working from home or at an office, every agency should have a disaster plan for now and the future.

NOW is the time to work ON your agency's future, not just IN your agency. Do this not just to survive the Coronavirus, but to maximize your agency's value!

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