

Valuation Risk

There is a misconception in the marketplace that insurance agency valuations are strictly based on an agency's current financial statements. The reality is that two agencies with the same revenue volume and EBITDA margin (Earnings Before Interest Taxes Depreciation and Amortization) may generate very different values. Current revenue and earnings are imperative when calculating value, but even more important are the sustainability, predictability and potential growth of the earnings stream going forward.

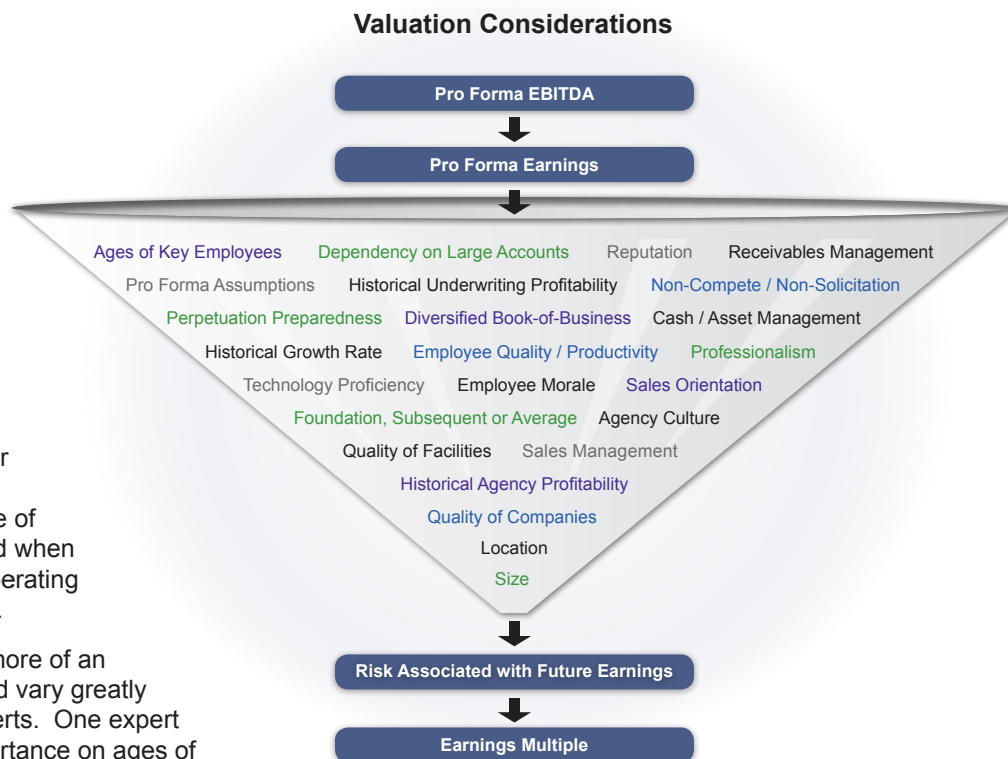
The sustainability and predictability of the financial performance is inherent in the valuation multiples used to calculate value. The harder it is to predict an agency's future earnings, the lower the valuation multiple will be. On the other hand, agencies with predictable earnings as demonstrated by fewer operating risks and strong consistent historical profit margins will generate higher valuation multiples. The funnel chart illustrates some of the areas that are examined when determining an agency's operating risk and valuation multiples.

The assessment of risk is more of an art than a science and could vary greatly between two valuation experts. One expert may place a very high importance on ages of key employees or perpetuation preparedness, while another may be more concerned with technology proficiency or producer non-compete agreements. In our valuation practice, we review all the risk factors from a standpoint of a hypothetical buyer on a stand-alone basis. From our transaction experience, it is clear that buyers assess risk and establish valuation multiples based on the anticipated post-closing structure.

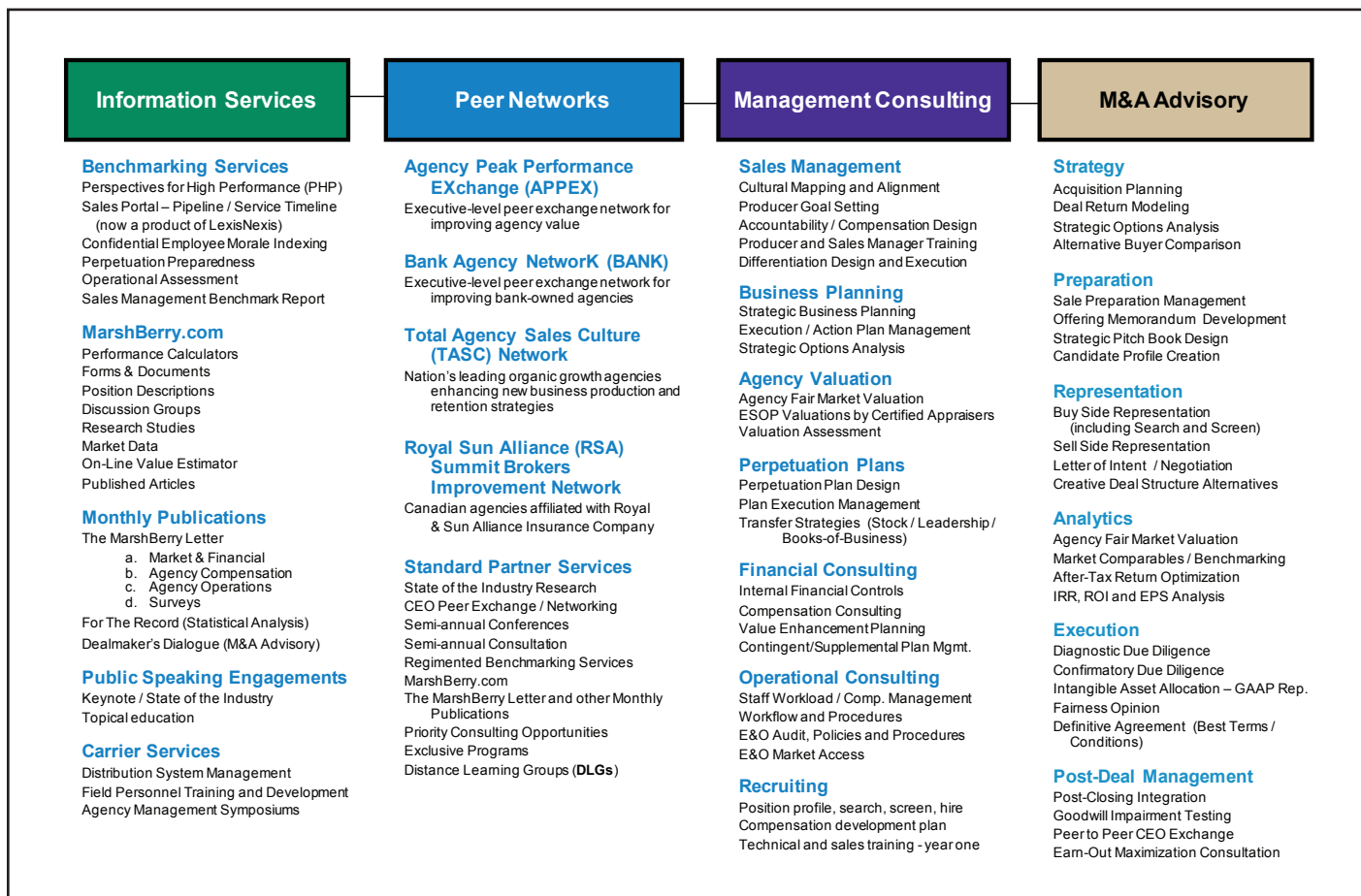
Revenue and profits are not created equal. Agencies that consistently achieve the highest valuations are those that demonstrate a history of strong financial performance and leave little doubt about their ability to achieve similar results in the future.

March's issue of The MarshBerry Letter will explore the topic of valuation risk in more depth.

Authored by Chris Darst, Senior Vice President, 949-234-9648



MarshBerry Solutions



MarshBerry's core focus is helping its clients realize their fullest potential with respect to growth, profit, survival and maximization of shareholder value. MarshBerry's agent, broker, bank and carrier clientele engage the firm to achieve goals within the retail and wholesale channels of the insurance distribution system. The firm's unparalleled industry-specific services include consulting, performance benchmarking, peer-to-peer exchange networks, merger and acquisition intermediation and producer recruiting.

