

First Quarter 2019 Allstate Agency Value Index

Decline in Values Driven by ECP, 9% Commission & Split Book Sales

Allstate Agency Price to New/Renewal Commissions Ratio (National Average)						
	2017 4th QTR	2018 1st QTR	2018 2nd QTR	2018 3rd QTR	2018 4th QTR	2019 1st QTR
\$0 to \$100,000	1.60	1.43	N/A	2.07	2.18	N/A
\$100,001 to \$200,000	2.20	2.21	2.15	2.08	2.39	1.46
\$200,001 to \$300,000	2.29	2.35	2.41	2.35	2.49	2.47
\$300,001 and up	2.90	2.90	2.93	2.96	2.69	2.64
Simple Average	2.41	2.62	2.63	2.58	2.50	2.44
Low	1.6	1.35	1.6	1.82	1.84	1.4
High	3.62	3.26	3.65	3.13	3.21	3.21

Let's tackle the three items that had a measurable effect on agency values in the first quarter of 2019:

1. ECP AGENCIES

Recent start-up agencies under Allstate's lucrative Enhanced Commission Program (ECP) transitioned this quarter for an average sales multiple of right at 2.0 times. This not only caused a decrease in the simple average this quarter, it was also a driving factor in the larger-sized agencies seeing a drop in value. The burning question is why would a very large agency that was recently started sell for such a lower than average sales multiple?

- a. **Not a Proven Commodity** – Recently started agencies under the ECP contract that have realized rapid growth are lucrative to the owner. However, the long-term "stickiness" of the customer base is unproven.
- b. **Tenure Retention – 5+ Years** – A common metric looked at when analyzing the health of an Allstate agency is the "Tenure Retention – 5+ Years" listed on the agent's Business Metrics Report. Unfortunately for recently started agencies, there is no tenured retention ratio of 5+ years available for analysis.
- c. **Price over Service** – A significant part of the decision-making process for those shopping for a new insurance carrier to protect their home and auto is **price**. Given that all of the insured customers of an ECP agency are new, any upward change

in **price** will drive many of these customers to start shopping for a new insurance carrier. On the flip side, an Allstate agency that has been in business since 1982 is more likely to retain the overwhelming majority of its clients in the event of a premium increase. Long tenured customers tend to move away from price and make decisions based on their perceived level of **service**.

- d. **Where are the customers located?** ECP is a great opportunity for agents to cast a wide net to attract new clients to Allstate. The drawback with the wide net is that we are now seeing for the first-time large agencies whose clientele are often located a far distance from the primary agency location. This may be a non-issue, but traditionally speaking the majority of clients are located within a relatively tight geographic footprint from the agency location.

Prospective Allstate agency buyers going scratch instead of purchasing due to ECP opportunity?

The ECP start-up opportunity is so great, that it is driving approved buyers away from purchasing smaller sized agencies (typically those with \$2 million in earned premium or less). With approved agency purchasers viewing the ECP opportunity as far superior to purchasing a small agency, those Allstate agencies with Earned Premium of between \$1 million and \$2 million realized a significant drop in value this quarter.

2. 9% COMMISSION AGENCIES

If you aren't hitting baseline expectations to the point that your agency is receiving only a 9% commission, very few buyers are going to want to purchase your agency at full market value. And, if there are parties interested in purchasing your agency, these likely sophisticated buyers are unlikely to give you as a 9% commission selling agent the sale value they would for a better performing agency.

This quarter there were multiple agencies with 9% commission that drove down average values.

3. SPLIT BOOK SALES

Split books are great for Allstate as they bring in two outside buyers and allow for another store front location. However, it will be a rare occurrence where a seller receives the same or a higher sales multiple for his or her agency if the book is split. The only scenario I can see is if Allstate starts allowing small agencies to receive the full benefits of ECP.

Split book sales can have various outcomes – Increase in value, more cash at closing (since two buyers, two loans two down payments), but often the additional expense of two location, even though split by two separate owners, results in an overall lower value for the seller of an agency that becomes split at the time of sale.

Not All Agencies Created Equally

This quarter is a great reminder, that even though all agencies are selling a common product (home auto and life insurance), they are all very different. These differences will drive buyers to pay very different values, depending on various attributes of a specific agency.

If your agency is receiving 10% commission and was not a recent start-up you should feel very good about the value of your agency, especially if you have reached scale and have a great customer retention ratio.

Sellers call me all the time – usually to tell me that they are planning on selling their business for the average multiple listed on my report. My response is always the same: the Allstate Agency Value Index is a great place to start when trying to set a price on your agency. From there, you have to decide if the various attributes of your business make it worth more or less than the average. If you are selling, take the time to list out the strengths and weaknesses of your business. If you want to sell for more than they average, be prepared to validate your expectations.

\$0 to \$100,000 in New/Renewal Commission

No agencies were financed in this size group by PPCLOAN in the First Quarter of 2019.

\$100,000 to \$200,000 in New/Renewal Commission

On the surface, the ECP program appears to be making these sized books unattractive if the agency being sold is not part of a merger transaction.

The average sales multiple for this size group decreased from 2.39 times the previous quarter (driven by merger activity), to 1.46 times this quarter. Additionally, hurting this size group is the presence of agencies being sold that were receiving 9% commission.

\$200,000 to \$300,000 in New/Renewal Commission

Agencies in this size group maintained a healthy multiple of 2.47 times, which is favorable compared to 2.49 times in the final quarter of 2018. Assisting in maintaining this relatively strong value for this size group was a healthy mix of outside buyer and existing agents serving as agency purchaser. In fact, 50% of the agencies sold in this size group were to an existing agency owner.

\$300,000+ in New/Renewal Commission

After a sizeable decrease in value in the final quarter of 2018, it was expected that this largest size group would realize an increase in value as we entered 2019. However, this size group experienced all three of the initial talking points in this memo – ECP agency sale, 9% commission

agency sale, and split book sale. Despite this, the value of the largest sized agencies only saw a nominal drop in their average value.

It is important to note that excluding ECP agencies, split books, and 9% commission agencies, the multiple for this size group was a very healthy 2.86 times for the first quarter of 2019.

Percentage of Agency Sales by Size Group						
	2017 4th QTR	2018 1st QTR	2018 2nd QTR	2018 3rd QTR	2018 4th QTR	2019 1st QTR
\$0 to \$100,000	4 %	11 %	0 %	5 %	4 %	0 %
\$100,001 to \$200,000	24 %	17 %	20 %	16 %	32 %	11 %
\$200,001 to \$300,000	44 %	11 %	28 %	32 %	36 %	33 %
\$300,001 and up	28 %	61 %	52 %	47 %	28 %	56 %

The Allstate buy/sell market in the first quarter of 2019 was dominated by agencies with over \$2 million in earned premium. These represented 89% of the agencies financed by PPCLOAN. The split between the three largest sized groups was very even, resulting in very reliable sales multiple results for each.

Allstate Agency Value Ratios						
	2017 4th QTR	2018 1st QTR	2018 2nd QTR	2018 3rd QTR	2018 4th QTR	2019 1st QTR
Agency Price to New/Renewal Commissions	2.41	2.62	2.63	2.58	2.50	2.44
Agency Price to Total Revenues	2.22	2.40	2.35	2.21	2.34	2.16

For those agency owners residing in a state where a good portion of the homeowner's insurance is written through a third-party brokerage company (primarily coastal counties), looking at the multiple of revenues may be your best measuring stick for agency value as it takes into consideration both Allstate and brokered (i.e. non-Allstate) revenues. Certainly, the brokerage book is a reliable source of renewal income and has a level of value that is not presented in the traditional multiple applicable to Allstate commissions.