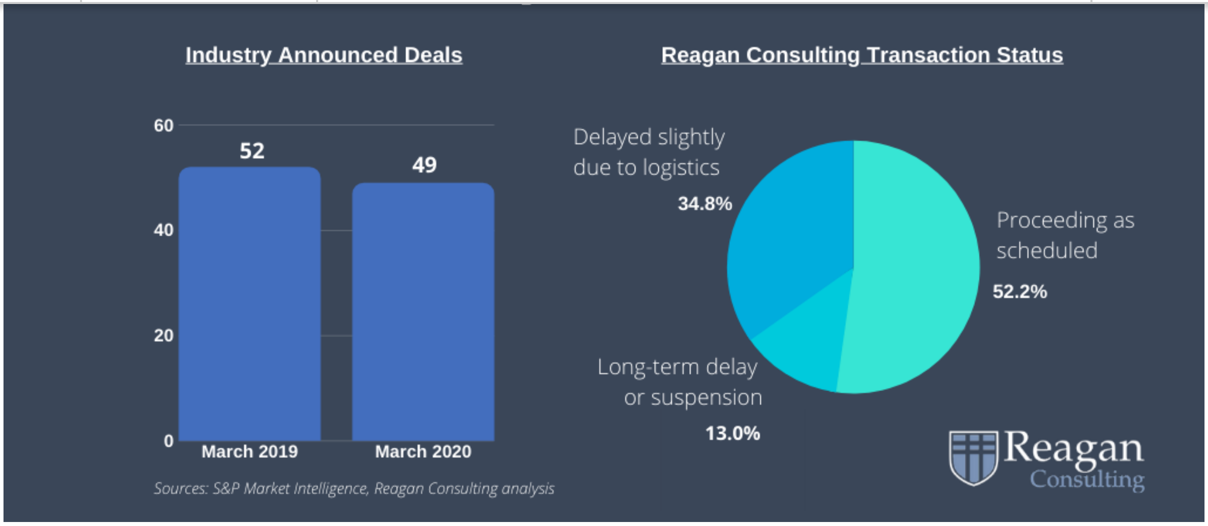
An Early Reaction from the M&A Marketplace

To our friends and clients,

The Dow Jones Industrial Average dropped over 2,000 points on Monday, March 9, signaling that the market was officially very worried about the impact of the novel Coronavirus. In the subsequent four weeks, Americans have been staying at home, social distancing, and focusing on staying healthy. While many features of ordinary and business life have been paused, the M&A market for insurance agents and brokers has carried on. Certainly, the M&A market has not completely escaped the reaches of the Coronavirus, but it is still open and active.

In March of 2019, per S&P Market Intelligence, there were 52 announced transactions in the M&A market for agents and brokers. And in March of this year, despite the reality of Coronavirus taking hold early in the month, there were 49 announced transactions (see chart below). We believe that number would have been higher if not for deals that have been delayed – not pulled – due to logistics reasons (rescheduling due diligence sessions, managing transitions to a work-from-home environment, etc.).



Further, at Reagan, we recently did a status check on all of the deals that we have in process and found that only 13% of our active buy-side or sell-side transactions have been delayed long-term or suspended (see chart above). The remaining 87% of deals are proceeding as scheduled or have been slightly delayed for logistics reasons. While we have had transactions suspended, the largest portion of our deals – over half – are proceeding as scheduled with no delay at all.

Our observations on the early reaction from the M&A market are as follows:

- Deals that were priced and that went under LOI prior to the Coronavirus outbreak are largely closing without significant revisions to terms or pricing. Some of these deals are delayed for a couple of weeks as the parties adjust mechanics in a work-from-home world, but we have not seen a mass suspension or renegotiation of these transactions.
- Acquirers with the strongest balance sheets are best positioned to compete. Perhaps the most noticeable effect of the current crisis is the drying up of the lending markets. Debt has become scarce and more expensive. While this is unlikely to last, obtaining funding in the very near term is challenging.
- The M&A market is likely to experience a flight to quality. High-quality firms are likely to command premiums while lower quality firms are likely to see bigger discounts.
- Buyers are taking a deeper look into a seller's client list, trying to identify if there are client concentrations in industries hardest hit by the Coronavirus. Moving forward, sellers should expect that this will become

slowdown will be more valuable. Conversely, clients in the hospitality and entertainment industries, for example, will be considered as higher risk.

- Sellers need to be realistic about the implications this slowdown may have on their ability to meet earn-out targets. Because most transactions have 1–3 year earn-outs, it may be difficult to recover completely from even a short-term revenue dip.
- Long-term investors are still focused on the long term. We have heard from many acquirers that if they thought a firm was an attractive partner in February, they still view that firm as an attractive partner now. A temporary revenue dip won't meaningfully alter long-term economics. Industry players are also optimistic that the recovery from the current slowdown will present a favorable environment for brokers – potentially with hardening markets.

Keep in mind, however, that we are still early in understanding the full impact of the Coronavirus on the M&A market. Yet, the early reaction is largely positive as the industry understands that M&A transactions are long-term investments. Deals in process are getting closed, buyers are open to looking at new opportunities, and sellers are initiating new processes even now. As we press forward, we'll maintain our monitoring of how the risk-sharing between buyers and sellers continues to evolve.

Brian Deitz
Partner, Reagan Consulting
Email Brian directly >>>

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