September 4, 2020

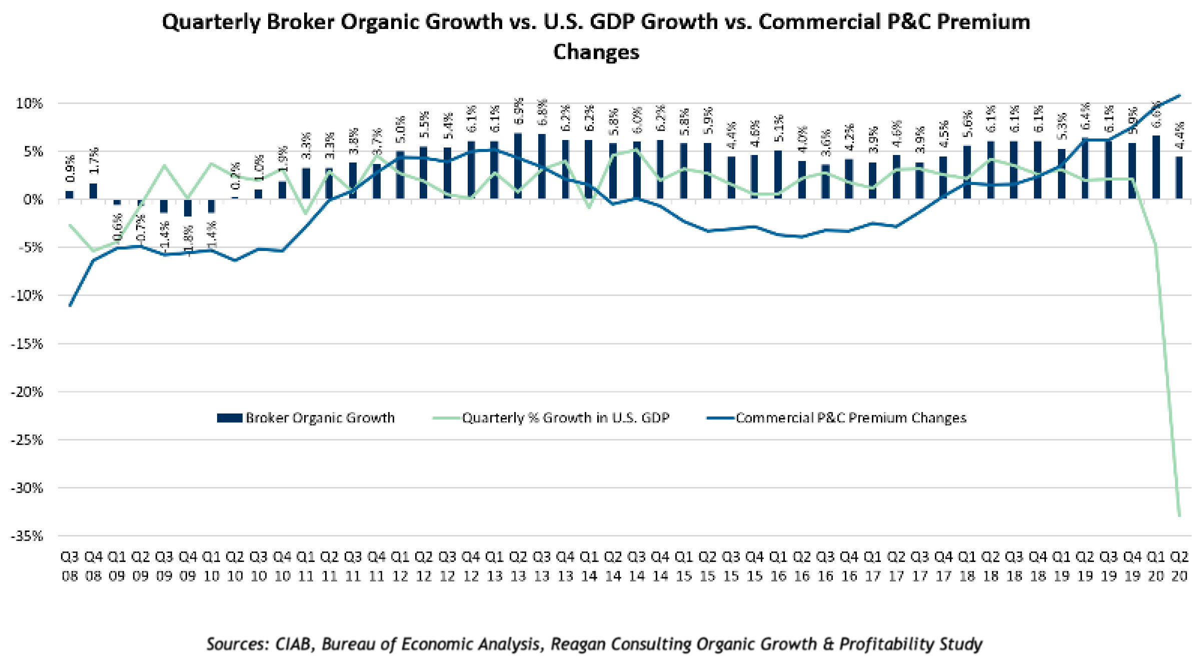
Brokers optimistic that the worst may be behind us.

To our friends and clients,

Despite the tumultuous arrival of the COVID-19 pandemic, its associated mandatory and stringent lockdowns, and the corresponding GDP collapse, brokers remain surprisingly optimistic about their near-term growth prospects. At the end of Q2, brokers reported median year-to-date organic growth of 4.4% while projecting full-year 2020 organic growth of 5.0%. This is positive news on two fronts. First, the insurance distribution industry is performing well when compared to many other industries' declining growth trends. Second, the full-year organic growth projections imply that the second half of the year will be *better* than the first half of the year from a growth perspective.

What's the cause for this uncommon positivity? The answer lies in understanding the two most important factors driving broker growth: U.S. GDP growth and P&C premium pricing. History has shown that if either U.S. GDP growth or P&C pricing change is positive, brokers have been able to generate positive organic growth

As can be seen in the chart below, the only time that brokers experienced negative organic growth in the past twelve years was the great recession, when dealing with both a soft P&C pricing market and a shrinking economy. Notice, though, that broker growth performance trailed the economic decline. Historically, there is a six-to-nine-month lag between U.S. GDP changes and the corresponding effects on brokers. Economic and exposure declines take time to work their way through policy renewals, audits, and then broker commissions.



If the lag effect works similarly this time around — and given the magnitude of the Q2 GDP decline —shouldn't we be bracing ourselves for a rough period from Q3 2020 through Q1 2021? Instead of preparing to take a hit in the second half of the year, though, brokers are preparing for a slight improvement in growth.

That optimism – cautious as it might be – is fueled primarily by the continued rise in P&C pricing. In Q2 2020, the CIAB reported that the average commercial pricing increase was 10.8%. This was the strongest quarterly result since Q1 2003 when an average of 14.0% was reported. And to date, this pricing increase has been enough to cover any exposure declines resulting from poor U.S. GDP growth.

Yet, what happens in the remainder of 2020 remains to be seen. We simply don't have a good precedent for understanding the effects of a 33% drop in GDP on broker performance. Can a favorable P&C pricing environment cover that kind of decline? Will government stimulus prevent our industry – and others – from feeling the full brunt of the shutdowns? The next two to three quarters will be critical in determining the ultimate impact of the pandemic on brokers. How will and 2020 forecasts, the worst could be behind us.

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