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Contents

Private Equity in the European Insurance Sector

Analysing PE deal trends and strategies in insurance brokers

Key takeaways

- The insurance subsector has accounted for the bulk of European PE financial services deal activity over the past decade, especially insurance brokers. PE deal volume for insurance brokers has increased around 8.5 times from 10 years ago and hit a new record in 2021.

- Factors driving PE deal activity with insurance brokers include robust recurring revenues, sticky and long-term customer relationships, asset-light business models, heavily fragmented markets, and light regulation. However, some key risks to PE deal activity include high levels of competition pushing valuations higher, squeezing margins due to pricing compression, increased threat of further regulation, and more direct-to-consumer sales from insurance companies.

- The PE buy-and-build playbook is the dominant value creation strategy when acquiring insurance brokers, with an astounding 84.0% of deal activity coming from add-ons in 2021, as sponsors seek to pursue multiple arbitrage, and revenue growth for platform companies.

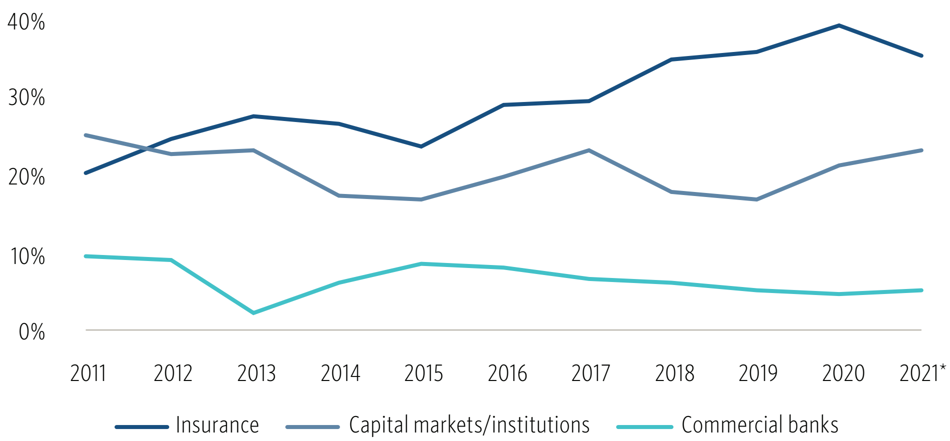
- As incomes and life expectancy increases, deglobalization strengthens, and more unexpected events hit, insurance broker PE deal activity will continue to grow as the demand for having tailored insurance coverage becomes more pronounced. This dynamic will propel additional niche brokers in underserved regions and product lines to pop up, thus increasing sponsors' investable universe.

- A few emerging technology trends are poised to transform the insurance broking space, in driving cost savings, efficiencies, and productivity across the entire insurance broker value chain. These include the heightened adoption of AI, data and analytics, IoT, and automation. These technologies are anticipated to foster more personalized and frequent communications with customers, largely through mobile devices, and will streamline the customer acquisition, onboarding, claims, and renewals processes in becoming policyholder-centric.

Introduction

Across the European private equity (PE) ecosystem, new peaks have been set in the deals and exits landscapes in 2021, as the pandemic-induced stimulus created the most favourable dealmaking environment ever. The financial services sector saw outsized activity in 2021, with insurance deal activity accounting for more than one in three financial services deals since 2018, especially insurance brokers. With an unprecedented amount of capital available and several successful exits, sponsors' appetite for insurance brokers intensified. In the past two years, over 70.0% of closed European PE insurance deals have been in the insurance broker space. The extremely fragmented insurance broker market has thousands of smaller, privately owned businesses, which are lightly regulated and require low capital intensiveness. These business characteristics make insurance brokers favourable for a classic PE buy-and-build strategy, as sponsors leverage multiple arbitrage to drive stronger returns.

Financial services subsector deals as a share of all financial services deals



Source: PitchBook | Geography: Europe
*As of December 31, 2021

This new research will serve as an introduction to PE investing in the insurance brokerage space. We will explore what an insurance broker is, evaluate key risks and factors driving PE deal activity, provide a market map, and end with commentary on one emerging opportunity in the sector. This report will serve as a primer for deal teams, LPs, and advisors seeking to understand the key elements of investing in European-headquartered insurance brokers.

What is an insurance broker?

An insurance broker (broker) is an intermediary between a client (policyholder) and an insurance company, who solicits, sells, and negotiates insurance on behalf of the policyholder. Brokers have a deep understanding of insurance products, risk management, prices, terms, and insurance companies. Brokers work to identify what clients should insure, how much to insure, and how to manage risk effectively.

Policyholder

Businesses, individuals, or organisations looking to purchase insurance products, from home insurance to more complex products such as public liability.

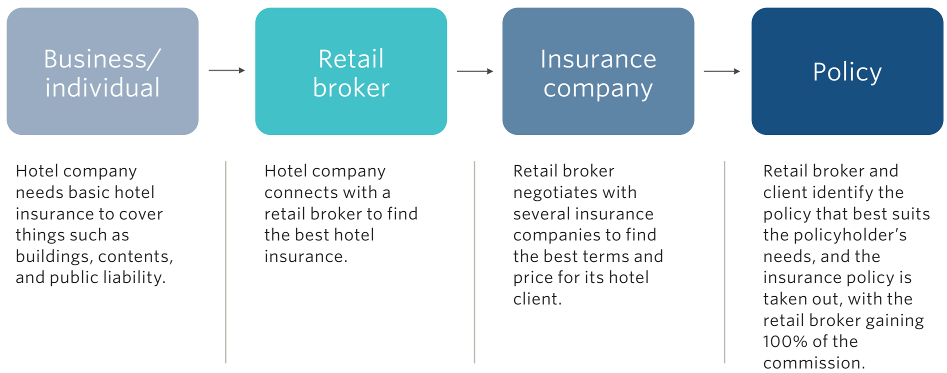
Brokers are usually independent from insurance companies and act in the best interests of their policyholders by negotiating with several insurance companies for the best terms and lowest premiums.

London Lloyd's market
Located in London, Lloyd's is the world's leading insurance marketplace, allowing insurance companies to sell specialty, unique, and complex insurance products to policyholders via wholesale brokers (Lloyd's broker). These products include kidnap & ransom, sports & entertainment, and terrorism & political violence insurance.

The insurance broker market is split up via insurance products, brokerage type, and region. This analysis will focus on retail and wholesale brokers, as well as managing general agents (MGAs) in the European region. In terms of insurance products, we will keep the analysis broad as PE investors tend to invest across the spectrum.

Types of insurance brokers

Retail broker



Underwriter
Individuals who work for insurance companies to set prices and terms for a particular insurance product. Underwriters work with wholesale brokers in drawing up policies for their clients through the Lloyd's market.

Retail brokers are typically privately owned brokers, operating in local markets where the underlying client is based, and are usually the first point of contact for a policyholder. They act as an intermediary between the policyholder and the insurance company or wholesale broker and will decide whether local or Lloyd's markets are more suitable to place the desired insurance. The bulk of PE deal flow sees sponsors acquire retail brokers due to fragmented markets and a long tail of companies. While some will define retail brokers as only serving individuals, and commercial brokers as serving businesses and organisations, for the purposes of this analysis, retail brokers will serve individuals, organisations, and businesses. Retail brokers can place rudimentary home, auto, or business insurance for policyholders through local markets, to more complex products such as yacht, cyber, and financial insurance through their wholesale broker relationships in the Lloyd's market. Retail brokers are paid a commission by the policyholder which is typically baked into the insurance policy premium.

Wholesale broker

Company X →	Retail broker →	Wholesale broker →	Lloyd's market →	Policy
Company X needs specialty cyber risk insurance to protect its products and services.	Company X connects with retail broker to find the best cyber risk insurance.	Because cyber insurance is complex and niche, the retail broker contacts a wholesale broker to place the insurance through the Lloyd's market, as domestic markets will not facilitate such complex insurance products.	Wholesale broker negotiates with several Lloyd's underwriters or syndicates to find the best terms and price for the underlying policyholder (company X).	Insurance policy is taken out by the underlying policyholder, and commissions are split between the wholesale and retail broker.

Wholesale brokers are companies who act as an intermediary between retail broker(s) and an underwriter or syndicate, placing complex lines of insurance through the Lloyd's market, while having no contact with the underlying policyholder. Wholesale brokers work on the policyholder's behalf, negotiating with underwriters to create a tailored policy to insure the risk of retail brokers' clients.[1] Wholesale brokers have specialized expertise in particular complex line(s) of insurance coverage. They place 5% to 100% insurance for assets that have difficult-to-place risks, such as political or product recall risk, through their Lloyd's underwriter relationships. The wholesale broker market is consolidated, meaning it's difficult for PE firms to buy these entities, as they rarely come up for sale. That said, in Q1 2021, Cinven and GIC acquired the London-headquartered wholesale broker Miller Insurance. To operate in the Lloyd's market, the broker must have an approved license, which is costly, complex, and time-consuming to attain. A retail broker will use a wholesale broker when a client is looking to gain insurance for a specialized type of risk, such as cyber, which is hard to place in local markets. Through the wholesale broker's Lloyd's license, deep expertise, and relationships with Lloyd's underwriters, they will obtain a policy and split commissions with the retail broker if the policy is taken out by the underlying client.

Managing General Agent (MGA)

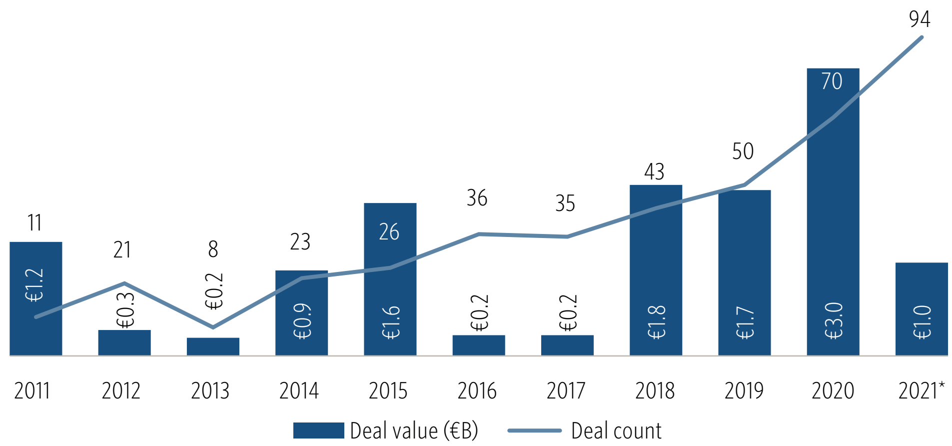
Policyholder/ retail broker/ wholesale broker →	MGA →	Policy
A policyholder, retail broker, or wholesale broker can contact an MGA to discuss their client's insurance demands or individual insurance needs.	Subject to the situation, the MGA can underwrite, price, and bind insurance coverage. In other circumstances, the MGA will discuss prices and terms with insurance companies in seeking the best policy for the underlying client.	Insurance policy is taken out by the client, and commissions are split between all parties involved.

1. "How the Market Works," Lloyd's, n.d.

MGAs are a specialised type of insurance agent or broker. Making them unique, MGAs are granted underwriting authority by an insurer. MGA functions include underwriting and pricing, binding coverage, and settling claims. MGAs can manage all or part of the insurance business of an insurer, act as an insurance agent or broker for the insurer, while also working as an intermediary between insurers and agents, clients, or brokers.[2]

Overview

Insurance broker PE deal activity



Source: PitchBook | Geography: Europe
*As of December 31, 2021

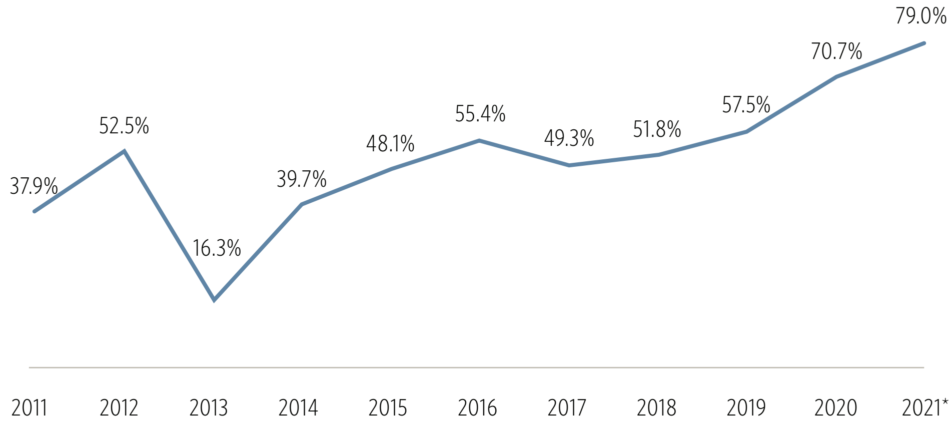
European PE insurance broker deal volume has been on an upward trend over the past decade and hit a new record of 94 closed transactions in 2021. PE insurance broker deal volume has increased around 8.5 times from 10 years ago and contributed a new high of just under 80% of all insurance deals in 2021. Some key drivers of PE deal activity in the space include fragmented markets driven by light and local regulations in many European countries and a high volume of insurance brokers due to low barriers to entry. Other factors powering PE deal activity in the space consist of strong business fundamentals, recurring revenues, and low risk business models, which we will dive into later.

For the first time in over a decade, the last two years has seen sponsors overtake corporates as the dominant acquirer of European-based insurance brokers via deal count, driven by growing and record dry powder levels. Insurance brokers such as UK-based Specialist Risk Group, Newstead Insurance Brokers, and PIB Group were all acquired by sponsors in 2021. The buy-and-build playbook is the dominant value creation strategy when purchasing insurance brokers, with an astounding 84.0% of deals coming from bolt-ons in 2021, up from 27.3% in 2011. For example, AnaCap Financial Partners' portfolio company MRH Trowe (MRH) made 11 Germany-based

2. "What is an MGA?" Insurance Business UK, Alicja Grzadkowska, September 21, 2021.

bolt-ons in 2021 as it seeks to become the one-stop-shop insurance solution in the country. MRH aims to diversify its platform through product and geography via the acquisition of niche brokers serving the DACH region in areas and products that the MRH platform lacks. Acquisitions have included a mix of rudimentary and specialty brokers such as Helmig & Partner specializing in bakery chains, Sportvers specializing in motorsport, and Kolb & Bär Versicherungs und Finanzmakler specializing in health & life. Bolt-ons are mainly used to drive three areas of value creation for PE platform companies—revenue growth, margin expansion, and multiple expansion. According to Nicholas Montoute from AnaCap Financial Partners, building scale through acquisitions is critical to develop successful insurance broker PE platforms, as brokers lend themselves well to buy-and-build models.[3]

Insurance broker PE deals as a share of all insurance PE deals



Source: PitchBook | Geography: Europe
*As of December 31, 2021

The UK is the largest European PE insurance broker market, accounting for 63.8% of closed PE deals in 2021. The region's huge international reach—which can insure virtually any type of risk in most locations because of the Lloyd's market, wide addressable market, and sophisticated infrastructure—contributed to its heightened PE activity. In addition, the region has high levels of expertise, deep reserves of capital, and developed local markets. It is the only country where the world's 20 largest insurers have set up offices,[4] and some of the largest insurance brokers are headquartered in the region, including Aon (NYSE: AON), Willis Towers Watson (NASDAQ: WTW), and PE-backed Miller Insurance. According to recent reports, globally the London Lloyd's market provides 60.0% of aviation insurance, 52.0% of energy insurance, and 33.0% of shipping insurance,[5] highlighting the region's importance within the insurance sector.

3. Nicholas Montoute, phone interview by Dominick Mondesir, December 9, 2021.
4. "UK Insurance Brokerage Market - Forecast (2020 - 2025)," Research and Markets, IndustryARC, March 2020.
5. "The UK: A Global Centre of Excellence for Insurance," The Global City, March 2021.

Top PE investors in European-based insurance brokers since 2016*

Source: PitchBook | Geography: Europe
*As of December 31, 2021

Looking ahead, we expect PE deal activity in the insurance broker space to climb as insurance further cements itself as an integral part of the global economy. According to the PitchBook Q3 2021 Insurtech Report, total direct written premiums (DWPs) are estimated to have reached €5.5 trillion ($6.1 trillion) in 2020, or 7.2% of global GDP. Further, as European PE dry powder grows, fragmentation intensifies, and low industry growth rates of around 7.3% over the next five years are expected,[6] greater activity is anticipated in the space. This will mainly be propelled by increasing demand for insurance policies and greater reliance on brokers from insurance companies and policyholders. As incomes and life expectancy rises, deglobalization strengthens, more unexpected events hit, and the volume of European small and medium-sized enterprises (SMEs) expands, the demand for having the correct insurance coverage will become more pronounced. Additional niche retail brokers will continue to pop up in underserved regions such as Central & Eastern Europe (CEE), Southern Europe, and the Benelux, as well as in product lines such as cyber risk according to Julian Addo of Miller.[7] These trends will foster a greater number of investable targets for PE platforms, while diversifying and increasing revenue streams.

- **Global life expectancies on the rise:** According to studies led by Imperial College London in collaboration with the World Health Organization (WHO), life expectancies are expected to increase in many countries by 2030, and will exceed 90 years in South Korea, and 85 years in the UK, therefore increasing the demand for long-term life and health insurance products.[8]

- **Acceleration of unexpected events:** The past 24 months has taught the world to expect the unexpected, which will drive demand for tailored insurance products. Rapid climate change has caused devastating wildfires, extreme flooding, and record heat waves in 2021. The COVID-19 pandemic caused global lockdowns, event cancellations, and significant business interruption which will heighten demand for numerous types of insurance, including communicable disease

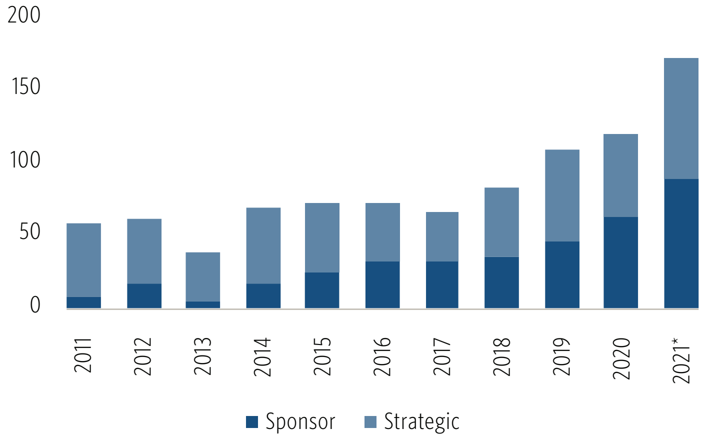
6. "Insurance Brokerage Market Outlook - 2027," Allied Market Research, Vaibhav Modi, Monica Chhabra and Vineet Kumar, February 2021.
7. Julian Addo, phone interview by Dominick Mondesir, December 1, 2021.
8. "Average Life Expectancy Set to Increase by 2030," Imperial College London, Kate Wighton, February 21, 2017.

insurance. Ransomware attacks are on the up, as seen from the €4.5 million ($5.0 million) demanded from Colonial Pipeline in 2021, which will push cyber insurance north. And European geopolitical tensions currently stand at decade highs, propelled by the invasion of Ukraine, which is driving protectionism, the need for local supply chains, and better tailored insurance products to insure against these rare risks.

- **Quickening global innovation:** As global innovation in fintech, the metaverse, cryptocurrencies, digital payments, and buy-now-pay-later platforms accelerates, the demand to insure these unique and complex risks will rise globally. For instance, digital payments are expected to increase by 73.0% in Latin America by 2025, which will push the need for customized insurance coverage among its SMEs and greater dependence on brokers to educate and distribute products to consumers.

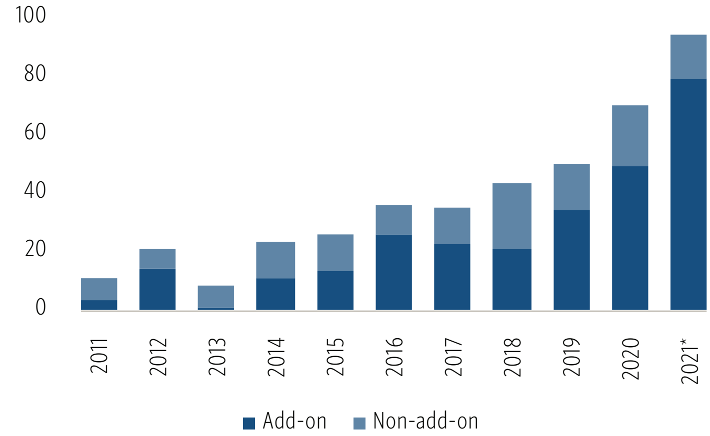
PE activity

Insurance broker deal count by buyer type



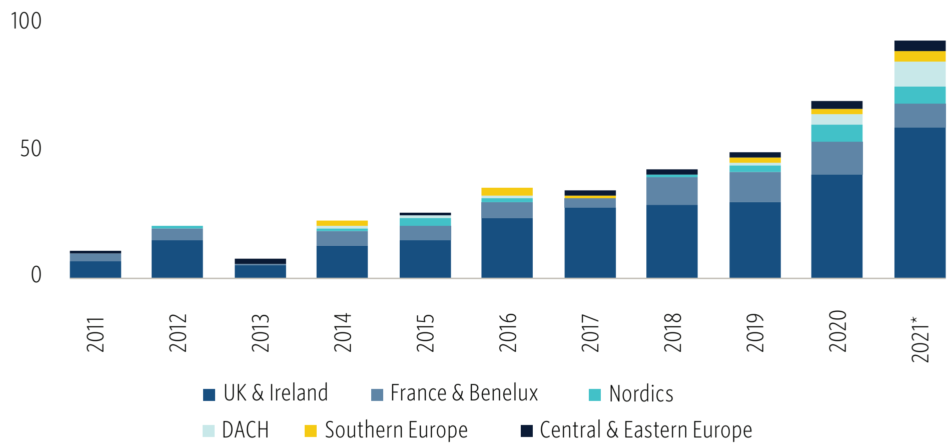
Source: PitchBook | Geography: Europe
*As of December 31, 2021

Insurance broker PE deal count by type



Source: PitchBook | Geography: Europe
*As of December 31, 2021

Insurance broker PE deal count by region



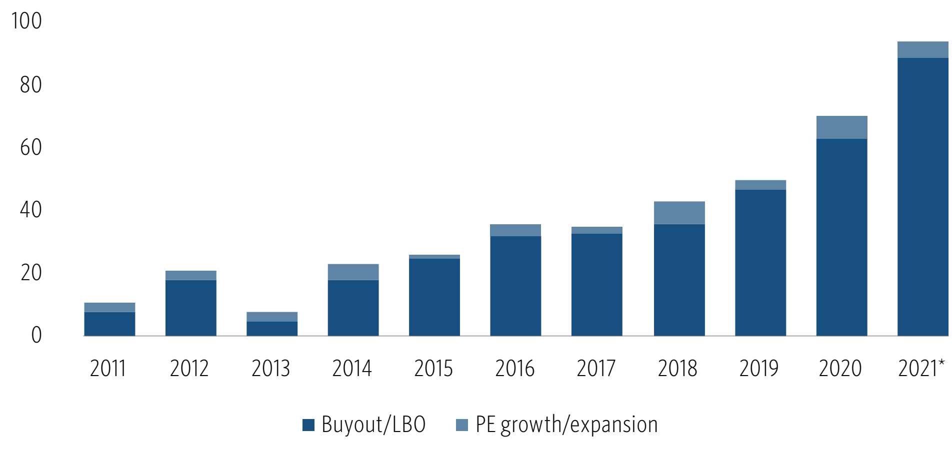
Source: PitchBook | Geography: Europe
*As of December 31, 2021

Notable insurance broker PE deals in 2021*

Insurance broker	Acquirer(s)	Bolt-on sponsor(s)	Close quarter	Region	Broker type
Miller Insurance	Cinven, GIC	Cinven, GIC	Q1	UK	Wholesale/Lloyd's broker
PIB Group	Apax Partners, Carlyle Group	Apax Partners, Carlyle Group	Q1	UK	Wholesale/commercial/retail broker
CRS Yachts	Aston Lark	Bowmark Capital	Q1	UK	Wholesale/Lloyd's broker
Five Insurance Brokers	Global Risk Partners	Ares Capital Europe, Penta Capital, Searchlight Capital Partners	Q1	UK	Commercial/retail broker
Anderson White Insurance Brokers	Clear Insurance Management	ECI Partners	Q2	UK	Commercial/retail broker
Town & Country Insurance Services	Partners&	Capital Z Partners	Q2	UK	Commercial/retail broker
Aiken Insurance Limited	NFP	HPS Investment Partners, Madison Dearborn Partners, Stone Point Capital	Q3	Ireland	Wholesale/commercial/retail broker
Usay Compare	Ardonagh Group	HPS Investment Partners, Madison Dearborn Partners	Q3	UK	Commercial/retail broker
P.E. Kelly Insurances	INNOVU Insurance	MML Growth Capital Partners Ireland	Q4	Ireland	Commercial/retail broker
Channing Lucas and Partners	Inflexion	Inflexion	Q4	UK	Wholesale/Lloyd's broker

Source: PitchBook | Geography: Europe
*As of December 31, 2021

Insurance broker PE deal count by type



Source: PitchBook | Geography: Europe
*As of December 31, 2021

Top strategic acquirers of European-headquartered insurance brokers since 2016*

Source: PitchBook | Geography: Europe
*As of December 31, 2021

Factors driving PE deal activity

Strong business fundamentals

PE investors' collective appetite for insurance brokers continues to grow mainly due to their strong business fundamentals. Robust recurring revenues of around 90% to 95%, sticky, long-term customer relationships, high cash conversion cycles, and asset-light business models allow PE investors to drive higher returns through a mix of elevated leverage, organic, and M&A growth measures. Furthermore, low operating expenses and high margins also contribute to brokers' strong business fundamentals.

In the following example, a retail broker's business model illustrates its strong business characteristics: Retail broker 1 (RB1) specialises in placing hotel liability insurance for UK SMEs and has built relationships with several insurance companies that underwrite this type of insurance, including Insurer A. Insurer A agrees to provide up to £1 million in insurance premium capacity for RB1's hotel clients, insisting they must make £100 per policy. RB1 is then free to set a price over and above the £100 per policy to their policyholders. Usually, RB1 will seek to earn around 10% to 20% commission per policy, so they will charge the underlying policyholder anywhere from £110 to £120 per policy. RB1 has now managed to scale the business to 1,000 paying hotel customers, earning 10% to 20% commission per policy annually, thus creating a platform of strong recurring revenues. Because purchasing insurance is a compulsory cost rather than a discretionary cost, RB1's hotel clients are sticky and long-term, as policyholders will renew their hotel insurance for the lifetime of their businesses. RB1 will incrementally increase prices each year, which could boost margins to as high as 30%. The policyholder will pay their hotel insurance premium to RB1 either in one upfront annual payment or in monthly installments, and RB1 will then distribute Insurer A's cut of the £100 per policy. This translates into a high cash conversion cycle due to RB1's high volume of paying clients and low operating expenses, which sees the bulk of cash made retained.

Scale, fragmented markets, and multiple arbitrage

Growth through M&A is a key part of the PE playbook for insurance brokers, as sponsors target revenue growth, margin expansion, and multiple expansion in driving returns on assets. Due to high fragmentation levels, single-digit organic growth rates, and scale exponentially benefitting brokers, buy-and-build strategies work well in the space. GPs will look to add specialty retail brokers, wholesale brokers, and MGAs with a quality insurance book characterised by low claims and high renewal rates onto an existing PE platform. In our view, these add-ons should foster enhanced product and regional coverage, higher market share, and more customers in becoming a one-stop-shop insurance solution. For example, Aston Lark, which is backed by PE sponsor Bowmark Capital, made 18 add-ons in 2021 in a variety of specialty retail and wholesale brokers. These acquisitions tended to be lower risk and cheaper, thus making multiple arbitrage possible. Aston Lark is aiming to become a one-stop-shop UK insurance broker, having built extensive product coverage across business, personal, and employee benefit insurance lines through M&A. According to Tassillio Arnhold of AnaCap Financial Partners, sponsors will try to achieve a blended entry multiple in the mid- to high-single-digit range and then look to sell the combined group for a double-digit exit multiple, thereby creating multiple arbitrage.[9]

Buy-and-build example: Bowmark Capital with Aston Lark

PE sponsor		Platform company		2021 insurance broker bolt-ons	Insurance lines
Bowmark Capital	Acquires	Aston Lark	Acquires	Haven Knox-Johnston	Automotive
				CRS Yachts	Yachts
				Spring Guernsey	Multi-lines
				Right to Health	Health
				Sennocke International Insurance Services	Commercial & personal lines
				Denmark Green & Associates	Business
				Bruce Stevenson Insurance Brokers	Multi-lines
				Magenta Insurance	Home
				Venture Insurance Brokers	Multi-lines
				DNA Insurance Services	Motor trade
				Linkscover	Golf clubs
				Plester Group	Life & health
				Essex insurance Brokers	Film & visual arts
				The Health Insurance Co.	Life & health
				S.Johnson & Co.	Property
				Bainbridge Collins	Multi-lines
				Innovation Broking	Multi-lines
				Choice Benefits	Multi-lines

Source: PitchBook | **Geography:** UK

9. Tassillio Arnhold, phone interview by Dominick Mondesir, December 14, 2021.

Low risk and lightly regulated

Relative to other companies in financial services, insurance brokers are lightly regulated and offer low risk business models. While regulatory practices of insurance brokers vary across Europe, most of the insurance risk and burdensome regulation lies with the underlying insurance company. For example, in the UK, insurance companies must follow tight Solvency II regulations, while retail brokers follow more lenient rules. The light touch regulatory approach fosters higher free cash flows for brokers, as little cash is spent on regulatory compliance, which may change in the future. In addition, insurance companies must keep a certain amount of cash or cash equivalents on hand for regulatory purposes, while brokers are able to invest all free cash flows into fast-growing areas of the business.

Wide addressable market

The global insurance brokerage market is expected to reach €465.9 billion ($515.3 billion) by 2028, up from €287.5 billion ($317.9 billion) in 2020,[10] while the retail brokerage market is anticipated to grow at a CAGR of 8.4% between 2020 and 2027—the fastest of any broker type.[11] With low insurance penetration rates in certain parts of Eastern and Southern Europe such as Estonia and Greece, which recorded insurance premiums of 1.3% and 2.2%, respectively,[12] as a share of GDP in 2019, insurance brokers have a significant amount of market share to attack in underserved regions both domestically and internationally. These numbers were more than 75% lower than proportions in the UK and Finland, where insurance coverage is robust. Further, as global innovation accelerates, the need for specialty insurance product lines in areas such as technology, sports, and energy will continue to drive the total addressable market (TAM) in the insurance broker industry.

Key risks

High levels of competition pushing valuations higher

Full valuations and hot PE deal activity indicates this trade could potentially be overdone. The buy-and-build strategy with insurance brokers is not a new concept, and many sponsors and strategics are actively pursuing the strategy, thereby intensifying competition and pushing valuations higher. For instance, strategic deal volume has jumped over 100% over the past five years, while the jump on the sponsor side was more aggressive, at around 2.8 times. According to industry sources, larger quality platform investments command EV/EBITDA multiples ranging from 13x to 15x, while smaller brokers trade around 8x to 10x. With elevated multiples, it becomes increasingly difficult for sponsors to achieve price arbitrage and leaves little room for error during the holding period. In Q2 2020, Searchlight Capital Partners acquired UK-based Global Risk Partners for €839.2 million at a

10. "Insurance Brokerage Market by Insurance Type (Life Insurance and Property & Casualty Insurance), Brokerage Type (Retail Brokerage and Wholesale Brokerage), and Regional Analysis (North America, Europe, Asia-Pacific, and LAMEA): Global Opportunity Analysis and Industry Forecast, 2021-2028," ResearchDive, June 2021.
11. "Insurance Brokerage Market by Insurance Type (Life Insurance and Property & Casualty Insurance), and Brokerage Type (Retail Brokerage and Wholesale Brokerage): Global Opportunity Analysis and Industry Forecast, 2020-2027," Allied Market Research, Vaibhav Modi, Monica Chhabra, and Vineet Kumar, February 2021.
12. "Value of Domestic Market Insurance Premiums to GDP in Europe in 2019, by Country," Statista, August 2021.

whopping 27.3x EV/EBITDA multiple. Moreover, while not an apples-to-apples comparison, Aon PLC (NYSE: AON), one of the largest Europe-headquartered insurance brokers, currently trades at a 28.2x EV/EBITDA multiple,[13] which is considerably higher than the European median EV/EBITDA buyout multiple of 11.9x. This highlights the lofty prices for quality insurance broker platforms.

Squeezing margins due to pricing compression

Sponsors help insurance brokers execute pricing management, which is a major organic growth measure. Annually, insurers' prices invariably either stay flat or increase due to tougher market conditions such as higher long-term inflation and rising claims. Despite rising prices, a popular strategy among brokers is to offer large upfront discounts to win new customers, which squeezes margins and profitability. In some instances, brokers break even or lose money in the first year of a client's policy. Brokers will focus on the lifetime value of a customer and prioritise renewals, which should push the broker into profitability in later years as they incrementally increase prices. On the wholesale side, according to Hafeez Akbar, a senior broker at Lockton, some brokers have seen large portions of their international business move away from London as some domestic insurers are able to offer considerably lower prices than London's Lloyd's market, thereby pressuring margins and revenues.[14]

Increased threat of further regulation

The Insurance Distribution Directive (IDD) and the implementation of commission caps from regulators could hurt the cash flow profiles of brokers, as the bulk of brokers' revenues comes from commissions sold on policies. The IDD replaced the Insurance Mediation Directive (IMD) in 2018 and aims to ensure consistent distribution standards across insurance products by insurance companies and insurance intermediaries, including brokers, to ameliorate consumer protection and promote fair competition. Key areas covered by the regulation include conflict of interest disclosures, customer demands and needs requirements, and remuneration disclosure requirements. These extra compliance rules will likely eat into brokers' margins as less time is spent on acquiring or maintaining customers and more resources are deployed into compliance.

Extending broker commission caps to more insurance products is a real threat to broker profitability levels. Commission caps have been applied to private health insurance products, and the German regulator BaFin has proposed a commission cap on life insurance policies of around 25% of the gross premium.[15] The Dutch government is also reportedly considering banning insurance companies from paying ransom payments to cyber hackers.[16] If approved, this will likely reduce broker commissions in cyber products. The evolving regulatory landscape, which could tighten across a range of insurance product lines and European countries, will undoubtedly reduce broker profitability.

13. "Aon PLC (AON)," Yahoo! Finance, March 22, 2022.
14. Hafeez Akbar, phone interview by Dominick Mondesir, January 13, 2022.
15. "Insurance Sales: Commission Cap Requires Adjustment of Existing Renumeration Models in Sales Renumeration," Q_PERIOR, n.d.
16. "Dutch Government Considering Ban on Ransom Payments by Insurers," Pinsent Masons, Out-Law News, Sari van Grondelle and Wouter Seinen, September 28, 2021.

Enabler

An acquisition that accelerates the digitisation journey of a company via adopting tech-driven capabilities that the company previously did not have.

More direct-to-consumer sales from insurers and the increase of disruptors

Another major challenge for insurance brokers is the direct purchase of insurance policies by policyholders from insurance companies, as well as the rise of alternative platforms from insurtech disruptors, including US-based Lemonade (NYSE: LMND) and Germany-based wefox. Continued tech innovation is making purchasing insurance—especially rudimentary products from insurance companies or alternative platforms—easier, faster, and, in some instances, cheaper than the traditional broker model. Some incumbent insurers are either launching digital models or partnering with/acquiring insurtech enablers to heighten their share of direct business, bypass broker-led models, and accelerate their digitisation journeys.

Key-person risk and high customer concentration

Insurance brokers—especially wholesale brokers—often have key person risk, as they have high customer concentration rates. A key person within an insurance broker refers to an employee who has client relationships that produce an outsized amount of company revenue. Despite noncompete agreements, the general practice of a key person taking clients should they move on to another brokerage is not unusual. It's not uncommon for around three wholesale broker employees to manage five to 10 clients that produce over 75% of a wholesale broker's revenues. In the event these three key persons leave the company, the broker's earnings would likely be materially affected.

Insurance broker market map

Notable European-headquartered insurance brokers that have received PE capital through either a buyout or growth equity investment.

Major PE-backed insurance broker platforms by region

Source: PitchBook | **Geography:** Europe

Emerging opportunity

The increased integration and adoption of technology

A few emerging technology trends are poised to transform the insurance broking space by driving cost savings, efficiencies, and productivity across the entire insurance broker value chain, including product development, distribution, administration, claims, and renewals. The pandemic-led disruption substantially accelerated the digitalisation journey for insurance brokers—especially incumbents using legacy technologies in an industry that's been slow to embrace digital transformation. In an industry characterized by in-person meetings, brokers had to upgrade online channels, expand digital capabilities to support sales, and accommodate remote workforces. Furthermore, the rise of disruptors through the steep acceleration of insurtech startups has forced brokers to be laser-focused on the digitalisation mega-trend. If brokers are too slow to adopt new technologies, they could be left behind. The following emerging technologies are expected to be at the heart of the seismic tech-driven shifts that will reduce operating costs and increase profitability: artificial intelligence (AI), data and analytics, Internet of Things (IoT), and automation. These technologies are anticipated to foster more personalized and frequent communications with customers, largely through mobile devices, and will streamline the customer acquisition, onboarding, claims, and renewals processes in becoming more customer-centric through online channels.

Many brokers have yet to realize the full potential of their datasets, but with the increased application of IoT, AI, and blockchain, brokers will be on a path to developing actionable, deeper, and more predictive insights from the millions of datapoints around consumer behaviours. A data-driven and analytics-led approach will unearth hidden patterns and allow for more-accurate risk management and pricing practices, as well as better product development from brokers. The identification of such habits through connected devices will help brokers create bespoke, timely, and usage-based insurance packages for individual customers. This process should lead to improved customer acquisition numbers, renewals, and greater profitability. For example, several insurance brokers offer auto products that track and incentivise safe driving behaviour through connected devices, which helps in offering more personalized and real-time pricing.

Automation is another key area wherein insurance brokers are accelerating integration. The moment of truth for many brokers comes when policyholders file a claim. Slow, time-consuming, and cumbersome claims processes ultimately lead to client churn, while automating large portions of this process in a way that clearly outlines benefits, ensures fast payouts, and simplifies filing claims will likely lead to big upticks in broker renewal rates and margins.

These technological changes will likely win new customers, reduce costs, and drive market share. In an effort towards being more proactive as opposed to reactive, brokers should be assessing whether to build, acquire, or partner with new technologies in growing their business intelligence capabilities. In contrast with the current model of “identify and repair,” future models will focus on “predicting and preventing” events driven by AI, IoT, and automation. The insurance brokers that embrace these disruptive technologies will be the winners in the next decade, while incumbents that view the technological developments as a threat could be setting themselves up for failure.

Conclusion

Over the past five years, investing in European-headquartered insurance brokers has been a core private equity investment area within the financial services ecosystem. Robust recurring revenues, fragmented markets, light regulation, low-risk business models, and wide addressable markets have driven PE deal activity. On the other hand, the increased threat of regulation, squeezing margins, and intense competition pose the biggest risks to PE dealmakers. The trend of investing in brokers will continue as insurance becomes more entrenched in everyday life and as reliance on quality intermediaries such as brokers expands. As more PE capital floods into the sector, prices will remain elevated, which will leave little room for error during the holding period. Sponsors will get more creative with their consolidation plays by building platforms in underserved regions, including parts of Southern Europe, DACH, CEE, and Benelux geographies, as well as by shifting aggressively into product areas such as cyber and gig economy product lines, wherein incumbents have historically been slow to serve. Bolt-ons will remain at the heart of value creation, with acquisitions of tech-focused enablers likely to increase as brokers embrace the digital transformation. In addition, management teams and bankers are marketing insurance broker platforms with ready-made acquisitions upon which sponsors can execute. Exit opportunities will also continue to build, with liquidity events to trade and financial buyers being the most popular. Further, as platforms grow in both size and prominence, exits via the public markets through IPOs or SPACs shouldn't come as a surprise. Over the next decade, the insurance brokers that incorporate disruptive technologies, as well as environmental, social, and governance (ESG) practices in line with the EU taxonomy, will command the greatest exit multiples and market share. Cost-efficiently gathering extensive customer learning insights from robust data sources, creating more personalized products through greater AI integration, and automating further processes will shift profit pools and dramatically reshape the industry from top to bottom.