

Growth vs. Profitable Growth

By Chris Burand

In an industry that prizes sales, it's no wonder so many sales programs and trade magazines advertise double-digit growth. You've probably seen the headlines: "Agency grows 20% annually for the last five years! Look inside and learn how!" Well, okay, maybe the headlines are not quite so loud, but this message does sell.

Readers enticed by these articles very often assume without question that all this growth is based on profitable sales. Readers easily make this big leap of faith because the insurance industry is plagued by the myth that all sales are profitable. Many agents believe this is a "cost-plus" industry where each sale costs an agency \$x dollars and the sales price always exceeds the cost. The urban insurance legend is that every sale has a 10% profit margin, for example, and therefore a 10% increase in revenue equals a 10% increase in profit. Nothing could be further from the truth. The industry is, unfortunately, much more like Detroit where the cost to manufacture a vehicle may exceed the sales price.

As an example, consider new business. Which is more profitable, writing new business or renewals? Is your agency's new business even profitable in the first year? If not, what happens to profit if a lot of new business is being written? Profit margins decrease, proving this is not a cost plus industry.

According to the *Growth and Performance Standards* published by the Academy of Producer Insurance Studies, the average agency with more than \$2,000,000 in commissions has \$3,908,000 in revenue, \$3,496,000 in expenses, and writes 7,668 accounts. This means the agency spends \$456 per account. How many accounts generating less than \$200 in commission does the average agency of this size write? Less than \$100 commission? If the average cost per account is \$456, is the \$100 commercial account going to be profitable?

It is easy to grow by writing unprofitable accounts and a lot of sales organizations are more than willing to do so, hoping to score a few big sales to subsidize all the unprofitable sales. In fact, a study cited by the *Wall Street Journal* several years ago showed 61% of all salespeople preferred to make a sale even if they lost money on the deal.

Does this problem infect your agency? It is a problem that has infected many agencies. One large broker hired a large number of producers to accomplish fast growth. Even if none of the producers generated enough sales to be individually profitable, top line revenue will increase substantially. But if the individual producers are not profitable, will the growth be profitable? How important is it to simply grow, if that growth is unprofitable?

I often ask audiences, "Do you want to make any sale or do you prefer profitable sales?" There is a big difference between sales that are profitable and those that are not. Much of the "fantastic" growth touted in our industry is not based on profitable growth, so when evaluating a sales program or even reading an article about an agency growing quickly, think in terms of profit.

For example, if you learn of an agency growing 15% annually and you find yourself getting that tight feeling in your chest making you want to grow faster too, consider whether that 15% is adequately profitable. Look for clues and read carefully to determine what it took to get that 15% growth. I recently worked backwards using the information in a magazine article and discovered the agency's rampant growth was powered by a 50%-75% reduction in commission rates. Is 15% annual growth still appealing at this point?

Fast, unprofitable growth might be appealing for certain strategies, such as loss leaders (tough to do in this industry), driving a competitor out of business, or selling out soon. If these strategies do not make sense for your agency though, then the key is to distinguish between all growth and profitable growth. This can be a tough but we have to bust the myth that all insurance sales are profitable. Agents that have learned the difference are now some of the most profitable agencies in the country.

The bottom line is all growth is not profitable. Many of the sales programs and high growth agencies making the news are not achieving profitable growth. Is your goal to grow at *any* cost or to grow profitably?

Chris Burand is president of Burand & Associates, LLC, an insurance agency consulting firm. Readers may contact Chris at (719) 485-3868 or by e-mail at chris@burand-associates.com.

NOTE: None of the materials in this article should be construed as offering legal advice, and the specific advice of legal counsel is recommended before acting on any matter discussed in this article. Regulated individuals/entities should also ensure that they comply with all applicable laws, rules, and regulations.

September 2006