Market Availability

By Chris Burand

Right now is a great time to start an insurance agency and I have seen several start-ups achieve far more success than I expected. Some are outperforming their peers who have a twenty-year head start.

Start-ups are enjoying a favorable environment right now because the market is soft and because new agencies can access carriers relatively easily. Even if a start-up cannot get a direct carrier contract, new agents can access virtually every single national carrier without getting a direct contract and the commission rates are very reasonable. Many wholesalers offer carrier access, several brokerage web sites offer access, carriers are being lax about their agents brokering business for other agents, and company appointments are easier to obtain.

This great access to carriers is not limited to start-ups. Every agency has this same opportunity, making it a great time for agencies to re-evaluate their stable of carriers and implement pro-active carrier management.

Industry averages show that roughly 60% of an agency's business is usually placed with its top three carriers. My research shows 85%-90% of most agencies' business is placed with their top ten carriers. This means that an agency with $20,000,000 premium averages at least $17,000,000 with its top ten carriers and divides the remainder between five to ten carriers and probably fifty brokers. No agency needs to split $3,000,000 premium between five to ten carriers and fifty brokers. That is the epitome of bad carrier relationship management.

Even if the agency consolidated all their brokers into one, they are still splitting $3,000,000 between, say, eight entities. That is only $375,000 each, which is nothing. In reality, the average relationship is probably closer to $100,000–and $100,000 is a rounding error to most carriers and major brokers.

Moreover, $100,000 premium is insignificant to this size of an agency. It is only $12,000 commission. "Only $12,000!" many agency owners are exclaiming. "It's $12,000 we wouldn't otherwise have!" But consider the actual profit behind that number. If an agency's profit margin is 25%, then the pertinent number is $3,000. In all probability, the profit margin is less because the average commission rate is less on much of this business and the agency is not receiving any contingencies. Using a 15% profit margin then, the pertinent number is $1,800. Now, count the number of accounts that generate that $1,800. I bet there is between twenty-five and fifty accounts involved. How profitable is it to service twenty-five accounts generating $72 profit each? I believe even these numbers are very optimistic, so the reality for most agencies is they are <u>losing</u> <u>money</u> on these relationships.

A main street agency of this size probably needs a maximum of twenty-five P&C carrier relationships. Fifteen is probably very doable today for the same reason start-ups are easier today: the number of wholesalers providing access to key markets is greater than ever before.

Instead of keeping a carrier just because it writes an agency's two largest but hard to place accounts, which forces the agency to place many accounts with that carrier to maintain the relationship, an agency can keep the two key accounts with the carrier through a broker, place the other accounts where they fit better, and increase the agency's profitability with the other carriers more than enough to offset the slightly less commission the brokers pay for those two accounts.

Some owners may believe the current carrier environment is short-term, but I don't see this situation changing any time soon. The larger national carriers are very desperate for more volume and simultaneously, they have dug themselves into a very deep pit by demanding too much volume from good agencies. As a result, they have become dependent on big agencies, consolidators, and big clusters who may now be demanding more compensation. The big carriers cannot go back now and reduce volume commitments or create enough new agencies fast enough to offset these forces. Nor can they break up with the big guys. Therefore, offering their wares through every available resource is their best option. With profits so high, especially with some convinced they do not need up-front agency underwriting anymore, they really are not concerned that this distribution method will result in poor loss ratios.

Additionally, some very good carriers that usually do not make direct agency contracts have developed very good products aimed at attracting more retail business. This includes reinsurers and carriers that are probably exploring ways to bypass brokers and make direct agency appointments.

The result is a great opportunity for agencies because gaining access to important carriers is easy–if an agency manages their carrier relationships well. Joining a cluster, as many agencies do to "improve" their position with carriers, usually just dilutes their carrier relations even further. In today's environment, there is little need to join a cluster to gain access to carriers. Additionally, agencies that manage their company relationships better are much more likely to get paid more for their efforts. This is a fact.

I know agencies can thrive in this soft market with fewer company relationships if they improve the quality of their carrier relationships. I know agencies can successfully start from scratch in this market because carrier access is so easy. The key for both is practicing solid carrier management and maintaining the self-discipline required to not chase a new appointment to make $200 profit.

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**.

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