BRP Group, Inc.

Fourth Quarter 2023 Earnings Conference Call

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CORPORATE PARTICIPANTS

Bonnie Bishop, *Executive Director, Investor Relations*

Trevor Baldwin, *Chief Executive Officer*

Brad Hale, *Chief Financial Officer*

CONFERENCE CALL PARTICIPANTS

Sid for Greg Peters, *Raymond James*

Josh Shanker, *Bank of America*

Meyer Shields, *KBW*

Pablo Singzon, *JPMorgan*

Elyse Greenspan, *Wells Fargo*

PRESENTATION

Operator

Greetings and welcome to BRP Group Inc. Fourth Quarter 2023 Earnings Call.

At this time, all participants are in a listen-only mode. A brief question-and-answer session will follow the formal presentation. (Operator Instructions)

As a reminder, this conference is being recorded.

It is now my pleasure to introduce your host, Bonnie Bishop. Thank you. You may begin.

Bonnie Bishop

Thank you, Operator. Welcome to the BRP Group's Fourth Quarter 2023 Earnings Call. Today's call is being recorded.

Fourth quarter and full year financial results, supplemental information and Form 10-K were issued earlier this afternoon and are available on the Company's website at ir.baldwinriskpartners.com.

Please note that remarks made today may include forward-looking statements subject to various assumptions, risks and uncertainties. The Company's actual results may differ materially from those contemplated by such statements. For a more detailed discussion, please refer to the note regarding forward-looking statements in the Company's earnings release and to our most recent Form 10-K, both of which are available on the BRP website.

During the call today, the Company may also discuss certain non-GAAP financial measures. For a more detailed discussion of these non-GAAP financial measures and historical reconciliation to the most closely comparable GAAP measures, please refer to the Company's earnings release and supplemental information, both of which have been posted on the Company's website at ir.baldwinriskpartners.com.

I will now turn the call over to Trevor Baldwin, Chief Executive Officer of BRP Group.

Trevor Baldwin

Good afternoon and thank you for joining us to discuss our fourth quarter results reported earlier today. I am joined this afternoon by Brad Hale, our Chief Financial Officer, and Bonnie Bishop, Executive Director of Investor Relations.

For the fourth quarter, the contributions from the significant investments we made in 2021 and 2022 continued to manifest themselves in a meaningful way, as we generated organic growth of 15%, our 15th straight quarter of double-digit organic growth as a public company.

For the year, we achieved industry-pacing organic growth of 19%, including double-digit organic growth across all three of our segments, grew Adjusted EBITDA by $54 million, a 27% year over year increase, and expanded our margin by approximately 50 basis points. As a result of the investments we have made over the past few years, our business remains well positioned to continue delivering double-digit organic growth, ongoing margin expansion, rapid growth of free cash flow from operations, and continued strengthening of our balance sheet.

In IAS, we generated organic growth of 9% in the fourth quarter, in line with expectations we previewed on our third quarter earnings call. As forecasted, while growth was robust in most areas of our IAS platform, we saw select weakness in profit sharing revenue and project-based work in sectors such as construction, where increased client sensitivity to continued higher interest rates and insurance rate increases had an impact in Q4. Despite the headwinds in Q3 and Q4, IAS organic growth for the full year was 12%, in line with our long-term target of 10% to 15%. There will always be puts and takes to the underlying momentum of our end client industry sectors, but early signs are pointing to an ebbing of these negative impacts that persisted during the second half of 2023. Job starts in our construction practice are seeing a normalization as we start the year, and our clients in general across the IAS business are exhibiting resiliency, consistent with the continued growth seen in the broader U.S. economy.

Our UCTS segment grew organic revenue 22% in the fourth quarter, due to continued strength in our multifamily, homeowners and commercial umbrella programs, which has persisted into the first quarter, and the commercial property and high net worth homeowners products we launched in late 2023 continue to gain momentum. UCTS organic revenue growth for the year was 31% thanks to broad-based strength across our platform, and due to the significant growth in our homeowners platform in 2023.

Our MIS segment grew revenue 21% organically for the quarter and 23% for the year, thanks to continued strength from Westwood and a growing contribution from our National Mortgage and Real Estate operation. Additionally, investments in our sales and distribution capabilities at Westwood have led to three more Top 35 builders signing with us in the last six months. We expect sustained strength in new business, along with higher attachment rates and meaningful insurance rates to continue to drive momentum for Westwood in 2024.

As a part of our efforts to streamline operations, increase margin, and focus on our core businesses, we have executed a definitive agreement for the sale of our wholesale brokerage platform, Connected Risk Solutions, to Amwins. We expect the transaction to close on March 1, generating cash proceeds of approximately $59 million. In addition, this transaction is expected to be neutral to 2024 adjusted EPS, and accretive to both 2024 organic growth and Adjusted EBITDA margin. As the nation's largest independent wholesale broker, Amwins has been one of our trusted and preferred trading partners for many years and they will be an outstanding home for Connected's clients and colleagues. Brad will cover the anticipated financial impact of this transaction in a few moments.

As we move forward with our strategic roadmap, we are deepening our focus on efficiency in execution through our recent work to simplify and optimize our operating model and business operations. To that end, in January, we announced the promotions of Dan Galbraith, formerly Chief Operating Officer, and Jim Roche, formerly Chief Insurance Innovation Officer, to co-Presidents of BRP Group, with shared firmwide responsibility for BRP's continued performance and operations. Dan will also serve as CEO of Retail Brokerage Operations, which includes the Insurance Advisory Solutions segment and the Medicare and Mainstreet personal insurance businesses in the Mainstreet Insurance Solutions segment. Jim will also serve as CEO of the businesses in the Underwriting, Capacity and Technology Solutions segment, as well as of Westwood, which resides in the Mainstreet Insurance Solutions segment. Dan and Jim have delivered exceptional results and made significant contributions to BRP's growth and evolution since joining the firm. I am excited for their contributions in these roles as they broaden their responsibilities to drive our continued success as we build the transcendent broker of the future.

In summary, we are proud of the strong results we delivered in 2023. We are executing daily on numerous strategies to drive continued industry-leading organic growth, expanding margin, and growth of our free cash flow, all while building on our unique culture and status as a destination for our industry's most talented professionals.

I want to thank our nearly 4,000 colleagues for their unwavering dedication to all our stakeholders during a challenging year in the insurance marketplace. While growth across the economy still appears resilient, dislocation persists in large portions of the insurance marketplace, impacting many of our clients. I extend my gratitude to our clients for their continued trust in our ability to help them navigate these conditions and deliver innovative and thoughtful solutions.

With that, I will turn it over to Brad who will detail our financial results.

Brad Hale

Thanks Trevor, and good afternoon everyone.

For the fourth quarter, we generated organic revenue growth of 15% and total revenue of $285 million. For the full year, organic revenue growth was 19% and total revenue was $1.2 billion. We generated organic growth in the quarter of 9% at IAS, 22% at UCTS, and 21% at MIS.

We recorded a GAAP net loss for the fourth quarter of $62.5 million, or GAAP diluted loss per share of $0.56. GAAP net loss for the full year was $164 million, or $1.50 per fully diluted share. Adjusted net income for the fourth quarter, which excludes share-based compensation, amortization and other one-time expenses, was $16.2 million, or $0.14 per fully diluted share. For the full year, adjusted net income was $131.1 million or $1.12 per fully diluted share. A table reconciling GAAP net loss to adjusted net income can be found in our earnings release and our 10-K filed with the SEC.

Adjusted EBITDA for the fourth quarter rose 16% to $45.6 million compared to $39.2 million in the prior year period. Adjusted EBITDA margin was 16% for the quarter, flat versus the prior year period. Adjusted

EBITDA for the full year grew 27% over the prior year to $250 million. Adjusted EBITDA margin was 21% for the full year, an expansion of 50 basis points.

Net cash provided by operating activities in our statement of cash flows was $44.6 million for the full year 2023 compared to negative $2.5 million in 2022. Free cash flow from operations was $60.6 million for the full year, an increase of 6% from the prior year, even in the face of a 68% or $42.7 million increase in cash paid for interest. For the fourth quarter, free cash flow from operations was negative $15.4 million compared to negative $2 million in the prior year period. We incurred $15 million of severance expense in the fourth quarter and took meaningful steps around selling and operating expense management to achieve the $10 million of run rate savings for 2024 that we highlighted on the third quarter earnings call. We expect these expense management efforts, our continued growth of the business coupled with a decrease in one-time integration costs and flattening interest expense to yield greater than a 100% expansion of free cash flow from operations in 2024.

As a result of our strong organic growth and the absorption of prior year investments, our business is well positioned to accelerate the realization of significant operating leverage in 2024. As a reminder, we absorbed significant expense headwinds in Q1 and Q2 2023 from the roughly 1,000 net new colleagues that joined BRP in 2022. The absence of this headwind, as well as the cost savings initiatives we executed in the fourth quarter to align the growth services support structure with our go-to-market approach and integrated platform, will continue to have a positive impact on margin in 2024 and beyond. In addition, we have completed a substantial portion of our partnership integrations, as a result of which we anticipate meaningfully lower one-time expenses in 2024, which should drive increased free cash flow conversion.

In the fourth quarter we paid $2.8 million in earnouts, and our remaining estimated undiscounted earnout obligations total approximately $309 million as of December 31, 2023. As discussed on the Q3 earnings call, several agreements pursuant to which we executed on partnerships contain provisions related to earnouts that permit the former selling shareholders to allocate portions of the earnout proceeds to partner colleagues who were not selling shareholders but who meaningfully contributed to the partnered firm's achievement of the earnout. When this determination is made, it results in compensation expense being recorded as an offset to the change in contingent consideration, which is net neutral to net income. As a result of this practice, we added back $8 million of compensation expense in Q4 associated with colleague earnout pools and expect to add back approximately $7 million in Q1 2024 for earnouts coming due. The vast majority of the earnouts will be paid by the end of the first quarter of 2025. Thereafter, we expect to generate significantly higher free cash flow.

We expect our net leverage will continue to decline through the end of 2024, and our goal is to de-lever to approximately 4x or lower by the end of the year. This target includes 2024 estimated earnout payments of approximately $135 million, of which roughly $80 million will be paid in the first quarter. As a reminder, last quarter we revised down our target net leverage range to 3x to 4x from 3.5x to 4.5x.

Also, a few incremental details with respect to our sale of Connected Risk Solutions, our wholesale brokerage business. Connected finished 2023 at approximately $34 million of gross revenue and $5 million of Adjusted EBITDA. As Trevor mentioned, we expect cash proceeds from the transaction to be approximately $59 million. We anticipate the transaction will be neutral to 2024 adjusted EPS, and accretive to both 2024 organic growth and Adjusted EBITDA margin.

For the first quarter of 2024, we expect revenue of $370 to $380 million, and organic revenue growth at the high-end of our long-term range of 10% to 15%. We anticipate Adjusted EBITDA between $95 million to $100 million, and adjusted EPS of $0.51 to $0.55 per share.

As we project 2024 results, I'd like to reiterate our guidance from the third quarter earnings call but make an adjustment for the divestiture of Connected Risk Solutions. For full year 2024, we expect revenue of

$1.35 billion to $1.40 billion, which implies organic growth towards the upper end of our long-term range of 10% to 15%, Adjusted EBITDA of $315 million to $330 million, and expected free cash flow from operations of $165 million to $195 million.

In closing, we are very pleased with our results for the fourth quarter and full year of 2023, are immensely proud of our colleagues for their grit in a year of continued difficulty in the insurance environment, and grateful to our clients for their continued trust and confidence.

We will now take questions. Operator?

Operator

Thank you. We will now be conducting a question-and-answer session. (Operator Instructions)

The first question we have is from Greg Peters of Raymond James. Please go ahead.

Sid

Hey, good afternoon. This is Sid on for Greg.

Trevor Baldwin

Hey, good afternoon Sid.

Sid

Hey. I know you guys called out some headwinds on the IAS segment after the last couple of quarters. Just curious if your 2024 guidance assumes those headwinds persist or if you're expecting some improvements there.

Trevor Baldwin

Hey Sid, this is Trevor. A few things. One, specific to the 2024 guidance, it incorporates our expectation for a normalization of the impact of rate and exposure, which is where we see those headwinds show up relative to some of the project revenues mentioned earlier in my prepared remarks.

I think to contextualize the underlying performance of the IAS segment it's important to run through a handful of stats.

When we look at the impact of rate and exposure on our organic growth in the IAS segment for the first half of 2023, it was a 6.6% tailwind. And when we look at the impact of rate and exposure on the IAS segment in the second half of 2023, it was a negative 0.5% headwind. In the fourth quarter specifically, it was a negative 2% headwind. So if you look at the underlying organic growth and you normalize for the amount of transition we saw impact from rate and exposure, the organic growth from the IAS segment apples-to-apples would have been mid teens for the second half of the year and the fourth quarter.

When you look at the underlying momentum that we're seeing in that segment, I would tell you that it's growing. We track a metric called sales velocity which is how we measure new business revenue being generated or won from new clients as a measure of prior year commission and fee revenue. For the full year of 2023 IAS sales velocity was 17%. And more specifically, for the fourth quarter, IAS sales velocity was 21%, a notable uptick as we saw the growth in momentum and new client wins as a result of the investments we've made in talent and capabilities. As that compares to industry average, there's a consulting firm in the industry, Reagan Consulting. They perform a quarterly called the Growth & Profitability Study. For the full year 2023, the industry median sales velocity was 11.6% and to be in the 75th percentile, it was 15.7%.

So, a long-winded way of saying we feel like momentum in the IAS business continues to be very strong. We had some idiosyncratic drivers of rate and exposure compression in the back half of 2023 tied to some specific dynamics with particular clients and in client industry sectors, and we believe that's largely behind us. We've seen that as through January with a return or more normalization of rate and exposure in that part of the business.

Sid

Okay. Thanks, I appreciate it. Then I was hoping maybe—I know this was touched on in the prepared remarks, but hoping you can discuss a little bit more in detail the drivers of the margin expansion embedded in your guidance. I think last quarter Trevor, you mentioned Juniper Re is expected to be negative Adjusted EBITDA in 2024, and hoping maybe you could quantify that and confirm if it's still expected to be EPS accretive in 2025.

Trevor Baldwin

Yes. Let me just take those kind of one by one.

From a margin accretion standpoint, it's driven by broad-based discipline and operating effectiveness around payroll, operating expenses and travel and entertainment expense. But, notably, it's driven by us kind of growing into and normalizing the investments that were very significant that we made into talent in our business in 2021 and 2022.

If you look at the magnitude of that difference, when we started 2023, we added 1,000 net colleagues to the business in 2022 and had over $40 million or payroll that did not yet earn through our P&L that was going to be running through the 2023 P&L that we fully absorbed. When we look at the net hiring into the business, in 2023 we net added just a hair over 40 colleagues into the business while still adding over $187 million of revenue on an organic basis. That's not because we stopped investing in the client facing and talent side of the business; it's because we were able to rationalize our footprint and talent investments as we wrapped up the integration work across the vast majority of the partnerships we've completed over the past few years.

Specific to Juniper, we're very pleased with the progress we're making there. Jeff has recruited in a fantastic team and we fully built out capabilities across reinsurance brokering, actuarial services, cat modeling and operations. We expect that business to begin contributing to revenues in the first quarter.

We do expect that business to have a net loss for the fiscal year 2024, and our base plan is that that business will be EBITDA and EPS positive in 2025, however we continue to evaluate talent investments and opportunities.

In summary, I'd say we have a lot of trust and confidence in Jeff and the team that he's been able to assemble and we're super excited for the contributions they're going to make, both this year and beyond.

Thanks, Sid. Next question from the next analyst, please.

Operator

The next question we have is from Josh Shanker of Bank of America. Please go ahead.

Josh Shanker

Thank you for taking my question. Good afternoon everybody. At higher end of 10% to 15% long term organic revenue guidance is very strong, but it's also lower than it's been in the past. Can you talk about some of the drivers of your outsized organic growth and in retrospect, and what's changing about the outlook to the broader economy that makes you a little more conservative looking forward?

Trevor Baldwin

Hey Josh, this is Trevor. As we've talked about in the past, we view there really to be four building blocks to organic growth and it starts with how much of the prior year revenue did you retain, what's the impact from rate and exposure on either expansion or compression of that prior year revenue that renews? Then most importantly, how much new revenue do you win from new clients that you're bringing into the organization?

What's been consistent from us is that the preponderance of our organic growth is driven by our new business generation. Our retention tends to be in line to slightly better than industry average. The impact we have from rate and exposure actually tends to be a bit lower than the industry average. And our new business generation, our sales velocity tends to be significantly higher.

As we think about those metrics for 2024, we're not expecting any kind of material degradation; if anything, I'd say slight improvements in overall revenue retention and client retention. I would say we do anticipate an ebbing of kind of the impacts we've seen from rate overall in our businesses. And I'd say just in general coming off another year where we've had multiple segments with organic growth in excess of 20%, we're not going to plan for kind of hugely outlier performances like that. We expect really strong performance out of all three of our segments. We expect double-digit organic growth out of all three of our segments, but I would say that there is some characteristic conservatism that we're just not going to forecast for 20-plus percent organic growth.

Josh Shanker

That's understandable. One other question. I was just curious what kind of success have you had onboarding other lines of business besides renters on the MGA of the Future platform?

Trevor Baldwin

Josh, a tremendous success. The MGA of the Future platform continues to be just a significant growth driver for us overall with organic growth for 2023 in excess of 30%. And while our renters platform, which is a mature and scaled business continues to perform exceptionally well with growth in excess of 20%, and candidly we're seeing growing momentum there as we head into 2024 with a number of new initiatives relative to expansions into Canada and a number of software providers we expect to bring online this year, I'd say a significant part of that growth has been driven by the new products that we've been able to develop and rollout. Homeowners and flood in particular have been a huge success, generating over $360 million of premium and over $65 million of revenue for the MGA in 2023 alone. We now have over 12 unique products that we've built and launched off the MGA platform and an expectation that we'll launch another four to five this year.

As we've talked about in the past, when we looked at the lens through which we evaluate new product opportunities, it's where we do we have unique and differentiated distribution? Is there an opportunity to build a product that brings kind of unique end client fit and utility? And importantly, can we see a path to scaling that product line up in excess of $100 million over a reasonable timeframe?

And so we could not be more excited about the momentum that we have and the success that we're seeing across the MGA.

Josh Shanker

Thank you for the answers.

Operator

The new question we have is from Meyer Shields of KBW. Please go ahead.

Meyer Shields

Thanks and good evening or afternoon everyone.

A quick question to begin with. Is there any distinct seasonality in the revenues for earnings of the business being sold to Amwins?

Brad Hale

No, not really, Meyer. It's relative. They have some seasonality month-to-month but if you look quarter-to-quarter it's relatively flat.

Meyer Shields

Okay. Perfect. I know this obviously isn't going to take care of the entire debt program but are there specific plans for the proceeds?

Trevor Baldwin

It provides continued and better financial flexibility, Meyer, and we'll continue to thoughtfully manage our balance sheet to optimize returns.

Meyer Shields

Okay. Then one last one. If I can follow-up on Josh's question, it seems that there's increasing comfort with Florida's reforms with regard to people being (inaudible) and maybe depopulating citizens or whatever. I was hoping you could take us through what the implications of that are for Westwood, for the MGA of the Future?

Trevor Baldwin

Yes. Those implications are all positive, Meyer. Westwood continues to perform exceptionally well with organic growth in excess of 20%. We added three new Top 35 builders over the past few months as new distribution partners in to the Westwood business. As you know, a big volume of the new homes being built across the U.S. are build in Florida, and so to the extent that more capacity opens up, that creates more optionality and puts us in a position to provide more and better choice to our ultimate clients.

The opening up of the market will be a very good thing for us and should translate into our ability to kind of bring in further capacity into the MGA to continue to kind of meet the needs of our clients.

Meyer Shields

Okay. Fantastic. Thanks so much.

Trevor Baldwin

Thanks, Meyer.

Operator

(Operator Instructions)

The next question we have is from Pablo Singzon of JPMorgan. Please go ahead.

Pablo Singzon

Hi. Good evening. Just a question on margins. If you go by the guidance that you're giving that implied EBITDA margin expansion is the largest on (inaudible)—would be the largest EBITDA expansion that you would have done on an annual basis. Call it, 300 points. It seems like you can explain 80 bps of that from the $10 million of cost saves. Would the remainder just be natural operating leverage, and is there reason to think that that kind of cadence continues beyond '24?

Trevor Baldwin

Hey Pablo, this is Trevor. I'd say that the answer to your question that you surmised is accurate in that that margin accretion is coming from operating leverage. We're coming out of a couple of years in '21 and '22 where we invested significantly into the business. And as you know, roughly 80% of the expense base in this industry is payroll and so we've done most of the hard work around that as a result of how we managed headcount in 2023 for 2024.

We're not going to provide an outlook on what kind of margin accretion to expect in '25 or beyond, but what I will reiterate is, consistent with what we've said in the past is the margin profile of this business is not any different than that of our peers that operate in the high 20s, low 30s EBITDA margin. If anything, as a result of the utilization of technology and proprietary systems that we have, the hard work that we've done over the past few years to fully integrate our platform, I would suggest that over time our margin profile will be superior to that of our peers.

As a result, we do expect margin accretion for the foreseeable future year in year out; some years that will be more than others. We'll continue to invest in the business and invest in talent in a thoughtful and meaningful way that enables us to continue to remain on the vanguard for our clients and continues to allow us to cultivate our status and reputation as a true destination for the most talented professionals in our industry.

We're incredibly excited about how this business is positioned heading into 2024 and while '23 was a fantastic year, it was also a year that had some challenges and required some tough decisions. We've made those decisions and executed on those actions and positioned our business to really drive very strong and profitable growth in 2024 and beyond.

Pablo Singzon

Okay. Thank you.

Trevor Baldwin

Thanks, Pablo.

Operator

The next question we have is from Elyse Greenspan of Wells Fargo. Please go ahead.

Elyse Greenspan

Hi. Thanks. Good evening. My first question, does your organic guidance for ’24, are you assuming double-digit organic growth in all your segments? Then within IAS, I know you discussed earlier about some of what caused the slowdown in the second half of the year. Can you give us a sense of how that business is trending in the first quarter, two months into the first quarter from an organic basis?

Trevor Baldwin

Hey Elyse, so, one, we are expecting double-digit organic growth across all three of our segments in 2024. Relative to kind of early trends in the first quarter for the IAS business, through January we have seen a, what I would call normalization of the impact of rate and exposure and continued strength in new business momentum as I shared on the momentum we saw in sales velocity in the fourth quarter.

Elyse Greenspan

Can you just provide some thoughts, I guess, for ’24 and ’25 as you guys think about a return to M&A. Obviously interest rates have come down. Just give us an update on the pipeline and how you’re thinking about return to M&A activity.

Trevor Baldwin

Yes. We continue to have active dialogues and traffic in the opportunities that exist across the industry. We believe that M&A will continue to be an important value creation lever for us as evidenced—if you’ve seen our financial supplement that’s posted to the IR portion of our website, you’ll see that we added some new disclosure this quarter that details the success of our first large cohort of partnerships, the transactions we completed in 2020. You’ll see the significant multiple buydown that occurred as a result of both top and bottom line growth across that cohort.

M&A we do believe will be an ongoing and important part of our story. Consistent with our view last quarter, we don’t expect any material M&A in 2024 as we focus primarily on de-levering into our stated target leverage range of 3x to 4x. And after we pay the last of the large earnouts in the first quarter of 2025, I think we would expect that M&A becomes a more prevalent part of our story again, but importantly will be more episodic in nature than it was in the first few years of our life as a public company.

We’re incredibly fortunate as a business to have a platform that knows how to grow organically double digits year in year out throughout market and economic cycles. That enables us to be very thoughtful about when and how to deploy capital for M&A. We don’t need M&A to create value or to grow our business. As I articulated earlier, we grew organically our business by $190 million of revenue this past year. And so when there’s opportunities to align with high quality businesses that have terrific talent and brings us unique end client industry sector capabilities, expertise and risk competency centers of excellence, then those are opportunities we will pursue and execute on, but what you will not see us do is M&A just for the sake of driving growth or trying to create merger arbitrage. It’s purely about creating value, enhancing capabilities and driving long-term sustainability into our operating model.

Elyse Greenspan

Thank you.

Trevor Baldwin

Thank you, Elyse.

Operator

Thank you. There are no further questions at this time. I would like to turn the floor back over to Trevor Baldwin for closing comment.

Trevor Baldwin

I want to thank you all for joining us on the call this evening. In closing, I wanted to thank our colleagues for their hard work and dedication to our clients and each other. I also want to thank our clients for their continued trust and confidence.

Thank you all very much and we look forward to speaking with you again next quarter.

Operator

This concludes today's conference. Thank you for joining us. You may now disconnect your lines.