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9. Brown & Brown Inc.

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Brown & Brown Inc.

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Brown & Brown Inc.'s appetite for acquisitions is as voracious as ever, at a time when the pace of its organic growth has slowed.

In 2003, the Daytona Beach, Fla.-based brokerage continued its breakneck acquisition pace, gobbling up 23 agencies with around $46 million in total annual revenues. Through mid-July of this year, Brown & Brown had acquired another 21 firms, representing annual revenues of nearly $86 million.

Last year's acquisitions helped push Brown & Brown's 2003 brokerage revenues to $545.3 million, up 20.6% over its 2002 brokerage revenues, earning it the No. 9 spot in Business Insurance's ranking of the world's largest brokers. Last year, Brown & Brown ranked at No. 8.

The company's total gross revenues, which include investment income and miscellaneous other revenues, rose 20.9% to $551.0 million.

Brown & Brown's slower rate of organic growth in 2003-about 5.9%, compared with around 12.0% in 2002-was perhaps the only blemish on an otherwise strong 2003 performance, analysts say.

J. Hyatt Brown, chairman and chief executive officer of Brown & Brown, explained that organic growth is affected by the jettisoning of slow-growing accounts that come with mergers and acquisitions. "When we find there are accounts that don't make our margins, we don't continue to write those," he said.

A softening marketplace in some lines didn't help, either.

"During the year, we did find that pricing-particularly in the second half, particularly in property-started to soften," Mr. Brown said. Large accounts were getting price breaks of as much as 30% to 35%, he noted, "and still are."

The decline in Brown & Brown's organic growth rate is not a big concern, but it is "meaningful," said Nick Pirsos, managing director of investment banking firm Sandler O'Neill & Partners L.P. in New York. The real question, he said, is: "Where do they go from here? If (organic growth) declines from here, we would put it in the significant category."

"It's a function of property/casualty pricing, which a broker doesn't have control over," said Mr. Pirsos. "If the industry remains on a soft path, it would be a concern for everyone, not just Brown & Brown," he added.

The slowdown internally doesn't diminish Brown & Brown's revenue gains or successes in 2003, though, executives say.

Net income, for example, rose 32.7% to $110.3 million.

And, Brown & Brown moved closer to one of its major goals: $1 billion in revenue and a 40% pretax operating margin. The company is now more than halfway to that revenue goal and, at 36.3% last year, is knocking on the door of its targeted operating margin, which it calculates by adding interest expense and amortization back in to its pretax profits.

With that operating margin and a $100 million increase in revenue in 2003, "we really did very, very well," said Mr. Brown.

While the 40% operating margin is in sight, the $1 billion revenue threshold remains some distance away. Mr. Brown said projections are that the brokerage probably will record that revenue figure around the first quarter of 2008.

Brown & Brown's overall growth continued during the first half of 2004. Brokerage revenues for the six-month period totaled $321.0 million, up 14.0% from the year-earlier period. Net income, meanwhile, rose 17.2% to $68.5 million.

Mr. Brown said Brown & Brown would continue to search for acquisitions that will help fuel additional growth.

Generally, agencies targeted by Brown & Brown serve the middle market and generate annual revenues of $1 million to $10 million. This year, though, two acquisitions have been larger-one produces around $18 million and another about $24 million in annual revenue.

Mr. Pirsos said he thinks the brokerage is capable of staying the course with its acquisition strategy. "Their goal is 5% to 10% in acquisition growth per year. I would think that is still achievable for the foreseeable future."

Brown & Brown tends to do well in a "market environment like today's, where they have merger and acquisition opportunities," said Nikolai D. Fisken, managing director at Stephens Inc., an investment banking firm in Little Rock, Ark. "They have more time to take market share" through acquisitions, because they need less time to look for clients' coverage in the current softening marketplace, he noted.

Brown & Brown generates most of its revenues through its Retail Division. That division produced $400 million in revenue last year, up 14.8% from the year before. The division provides a range of property/casualty products to commercial and personal lines buyers.

Mr. Brown said the brokerage's most difficult competitors are agencies with long ties to a town, those "who are part of the fabric of the community. Since we are in a broad array of small and midsize communities, we often find a broker that has been there forever and has very strong relationships with clients." Sometimes, though, Brown & Brown has that upper hand itself, with an operation staffed by the town's "mothers and fathers," he acknowledged.

A 2002 acquisition is paying off for Brown & Brown's National Programs Division. CalSurance Associates Inc., which provides professional liability coverage for niche markets from its Orange, Calif., office, generated $26 million in 2003 during its first full year of operation under the Brown & Brown banner. That was all but around $3.1 million of the increase in revenues last year for the division, which saw revenues jump by 49.8% to $87.7 million.

The Brokerage Division, which markets excess and surplus lines commercial insurance and reinsurance, contributed $32.7 million in revenues, a 34.3% jump from 2002. Most of that increase was due to new business rather than from the addition of commissions and fees from acquired firms.

Brown & Brown's Services Division provides third-party administration and managed health services. It produced revenues of $29.4 million, up 3% over 2002. Unlike other segments of the brokerage, the division's revenues are nearly all fee based, meaning market conditions don't have as much influence over its performance.

Part of Brown & Brown's success has been the decentralized, merit-based culture the brokerage has developed, according to Mr. Pirsos. The environment encourages employees who will work hard to produce business and provide leadership, with the promise of advancement for those who stand out.

"If you want to put your shoulder to the wheel, you can flat rise," Mr. Brown explained. "There are no ceilings."

Brown & Brown operates in eight regions that are not strictly geographical. Four of the regions report to Mr. Brown and four to Jim W. Henderson, the brokerage's president.

When looking for new hires who can produce in an environment that demands results and rewards them, Brown & Brown has found that national accounting firms have produced "very good prospects for us," said Mr. Brown. "Obviously, we're still recruiting people from other sales type businesses, and from insurance carriers."

Brown & Brown occasionally hires a producer from another brokerage, but typically the company doesn't recruit from competitors, Mr. Brown said.

"Our culture is why we have been able for 45 consecutive quarters to post a 15% earnings increase," said Mr. Brown, who illustrated the company's strategy with a football metaphor: "Our game plan is pretty doggone boring-three yards and a cloud of dust. Ad infinitum."

Brown & Brown's shares, traded on the New York Stock Exchange, closed at $43.15 on July 9. The 52-week high and low were $45.95 and $29.20, respectively.