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Ryan Specialty Holdings, Inc. (RYAN)

William Blair Growth Stock Conference

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Adam Klauber
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MANAGEMENT DISCUSSION SECTION

Adam Klauber

Analyst, William Blair & Co. LLC

In case you don't know me, I'm Adam Klauber. I run our insurance and insurance technology group. Really lucky to have Ryan here. And obviously, I won't talk too much, save it for the management team. We've got really good leaders of the business.

But one thing I'll say about Ryan is that in following the business for good many years that it's tough to have a very unique franchise because insurance is such commodity. And Ryan, which I think you'll hear very shortly, is very special. Not only is it good company, but again it's a very unique franchise. And that franchise has a tremendous amount of levers. I think it's actually very early. The company's been around 12, 13 years. I think really thrilled with their development.

So with that, I'll turn it over to Founder and CEO, Pat Ryan. Thanks. Go ahead, Pat.

Patrick G. Ryan

Founder, Chairman & Chief Executive Officer, Ryan Specialty Holdings, Inc.

Thank you, Adam, and thank you for your attendance. As we decided to embark on Ryan Specialty back in 2010, we saw some very attractive opportunities that really we were part of [ph] the result (01:12) that the world just getting far riskier. And that those risks were really going to be addressed in the US E&S market. And that the need for freedom of rate and form to meet these challenging risk changes like climate change, like social inflation, like technology risk coming through cyber and so on, it's clear that there was going to be a great opportunity in that US E&S market.

I had the good fortune of bringing Tim Turner, to my right, to partner with me to build what we saw as a solution for building a combination of a new wholesale distribution broker, being a broker for retail brokers for high hazard risk. It feels like energy, construction, healthcare, [indiscernible] (02:15) parts of real estate, almost all construction lines.

Additionally, as the risks were getting so much more difficult, there are some trends that we saw coming. And that was the consolidation of the use of wholesaler by retailers because it was a very inefficient distribution system they were doing, doing business with, in many cases, a couple hundred wholesalers. So not really taking the business to market in an informed way where they could optimize the scale that they had and the scope that they had.

Additionally, there was a consolidation going on of retail brokers by sponsors, mostly PE firms. So they were buying up because of the free cash flow characteristics of insurance broking. They were consolidating the retail brokers. So that became sort of a sales force for us. If we got the relationship with them, they would be out buying up businesses that would make them larger and our relationship larger. So we saw that as growing dramatically as well.

And then the fourth factor was delegated authority, where carriers are willing to delegate the underwriting, the administration, and the distribution of specialty lines products. And what we needed was the intellectual capital to differentiate to do that on their behalf.

What they got out of that was variable costs. They got specialty skills that they didn't have. They didn't have to take the risk on retaining the talent. And we have a culture that could retain the talent by virtue of the culture which set up of empowerment, innovation, client centricity.

And what we've brought, and Tim and I share this philosophy, was independence because we felt that it was really important not to compete with our clients. So we made a decision, Tim and I together, and I actually made this commitment to AON when I retire that I was going to go into business, but not compete with them. But have them become a big client, and that's what's happened.

So we felt that the independents who were not competing with your client was critical. So the moats that we built was this differentiating specialty lines talent and product lines and industries. So property, casualty, professional lines, and then the industries that I talked about.

And those have expanded. Those opportunities have continued to expand. So not only have we had the ability to build these moats, but the TAM opportunity was really quite significant. And so we've been doing that through unusual organic growth, double digit all the way through our – from 2010 on through 2022 and in the first quarter of 2023, but also blended with strategic acquisitions to bring in more talent or differentiating intellectual capital, expanding our distribution capability in our specialty lines.

So one of the things that we've done is expanding that. We've expanded our specialty lines through these acquisitions and we have the first vertical of wholesale broker distribution. The second vertical was managing under a delegated authority as I referenced.

We were the only wholesaler to identify the need to bring in alternative capital for our clients to be able to bring to their insurers for risks that couldn't get insurance at all or couldn't get enough insurance. Or as said, those prices are just way too high, I'm willing to take on some risks to put up capital. So it's a captive strategy to bring capital brought by the insurance. And so that's the third vertical that we've set up.

And then a fourth vertical, which we just really launched today, where we're bringing specialty services in the form really of what we would call an MGA, but in the life and health business or benefits. It's called a general [indiscernible] (06:53) distribution of taking people from fully insured plans to self-insured plans. Taking them to self-insured plans, bringing them services like pharma, like loss mitigation to help them control those benefits' costs.

The medical stop loss product is a solution for that and it's one that we believe has a long runway of organic growth and inorganic growth. So this has all resulted in quite good results. We like it. Double-digit organic growth and then added to that was the M&A strategy. So we retained 97% of our brokers and we have a culture of innovation and ownership by the employees.

So our people think as owners, not as investors, not as employed. That we're aligned with our shareholders, we're aligned with our people. So we're very confident in our ability to be able to sustain this kind of growth.

And I would turn it over to my colleague here, Jeremiah Bickham, who's our Chief Financial Officer.

Jeremiah R. Bickham

Chief Financial Officer & Executive Vice President, Ryan Specialty Holdings, Inc.

Thank you, Pat. Hi, everyone. I'm excited to talk to you today. And one of the topics I get to touch on is growth. One of our favorite topics here, I imagine for a few of you as well, given this is a growth conference.

Since we've been public – well, actually going back to our entire history, we've put up exceptional organic growth. And in the last couple years, no doubt, there's been what some I think clever journalists dubbed as the broker supercycle. So there's been an unusual amount of flow into our channel and rapid price increases in multiple lines.

So that's no doubt a part of the story of our growth recently and everyone else's. But the more important part of our growth story is actually secular growth drivers, and Pat talked about it a moment ag. But if you have one takeaway related to that, it's the world is getting riskier and more complex. And we think that today and for the foreseeable future, more solutions will need to find their way into the E&S market, and that's where we specialize.

And if you take away nothing else regarding our growth today, it's that we are double-digit organic growers, agnostic of the pricing cycle. I'll say it again, we are double-digit organic growers regardless of the trajectory of pricing. And we can say that with conviction because there's actually structural elements to our organic growth engine that are not cyclical. We think they're secular, and I'll give you some examples.

So our clients remember our retail brokers and they have a built-in GDP-plus growth baseline that is the baseline of our growth as well. They also spend billions on M&A every year. That M&A benefits us. They're buying customers for us.

The other thing that retailers do that benefits us that it's been a tremendous benefit for the last decade-plus, and we think that there's at least another decade-plus of benefit is, as Pat said, they want to work with fewer, more sophisticated, scaled counterparties and we're one of very few that meet all that criteria. And in looking forward into the future, as retailers look to optimize that strategy, we stand to benefit disproportionately.

Again, 70% of the business that we manage is placed in the E&S market, and historically that's grown at roughly twice the rate of the Admitted market. We don't know what the exact growth rate will be going forward, but we believe that it is going to keep growing and that it's going to consistently outpace growth in the Admitted market.

And then last but not least, we have a unique competitive position that allows us to take market share. We're one of the few scaled counterparties with the breadth and depth of expertise to meet the needs of the largest, most sophisticated, most demanding retail brokers. We have a culture of innovation that's going to help us stay ahead of the curve in terms of where the market is going.

So let me touch briefly on our financial profile. So, everyone asked about capital allocation. First and foremost, we have to and we do reinvest in our business. We're a talent business. We have to keep refreshing the talent pool. That is easily accomplished with our operating cash flow. So where do we spend our next dollar for the foreseeable future? We believe that's going to be M&A.

There is a large amount of M&A opportunity set that will be accretive to our organic growth engine, which is really what our M&A strategy is. Rather than buying growth like a traditional rollup, we're just looking for new specialist tools to bolster our organic growth engine.

One reason you should love the broker business and the wholesale business model is our free cash flow profile. So think of recurring revenue. So we are almost entirely commercial and most of the products that we deal with are compulsory. We have very low CapEx needs. So for us – it's different for everyone, but for us, it's less than 2% of revenue.

And our costs are almost entirely – not almost entirely, the majority of our costs are variable. So our compensation, the majority of that is on the wholesale broker side, which they are based on a commission model. So all three of these things are good, say, in a recession scenario. The variable cost piece, especially valuable.

From a leverage perspective, so we are very, very comfortable operating in the 3 to 4 times total net leverage. The business, because of the free cash flow properties, can actually sustain leverage much higher than that. Our sort of expectation is 3 to 4 times. We're about 2.5 times right now. We don't expect to stay there for long because when M&A comes, it tends to be lumpy. We actually announced two deals this morning, which we'd be happy to talk about in Q&A, but think 3 to 4 times in the medium term.

In terms of margin versus investment versus growth, it's our belief, it's our philosophy and this has been reinforced by feedback from our investors that if we can combine a healthy margin, 30-plus percent, with sustained unusual organic growth, that's a winning combination. That's our goal right now.

In an effort to bolster what we would consider a, on average, very consistent annual, at least modest margin scaling, we initiated a restructuring plan earlier this year, which again happy to take questions on in Q&A. But rather than a garden variety cost-cutting exercise, what this is, is investments in our platform that will actually help us sustain efficiency and operating leverage over time, in addition to giving us a step change in margin by 2025.

So, when it comes to margin or when it comes to growth, remember we're not dependent on price when it comes to margin. We are focused on it, but we believe that we can and should balance a healthy margin with steady incremental change and making investments that keeps the organic growth going for as long as possible.

With that, I will turn it over to my colleague, Tim, to talk about growth and industry trends.

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Timothy W. Turner

President & Director-Ryan Specialty and Chairman & Chief Executive Officer-Ryan Turner Specialty, Ryan Specialty Holdings, Inc.

Thanks, Jeremiah. It's great to see everyone today. We appreciate your support.

The growth in the market today continues to be exponential and non-Admitted property and casualty market specifically grew over 20% in the first quarter. So standard companies Admitted P&C insurance companies continue to not renew business and it gets dumped into our channel.

So right from the beginning, as Pat and Jeremiah mentioned, we developed a platform that was highly specialized, highly technical in all the practice group verticals that were important to the retail brokers and agents across the country, and then we set out to find differentiating talent. That may be the biggest difference between us and our competitors. We put more time, effort and analysis into recruiting, training, developing, acquiring the very best talent in the specialty E&S arena in the US today.

So, as we look ahead, I have a great illustration of what really happens in our marketplace. So quickly, last week, I'm sure you saw State Farm pulled out of personal lines in the state of California. Not a big deal if you're a commercial P&C carrier, but it is a big deal. It's another indicator of a very large company basically concluding that they can't get the right rate for personal, auto and home in the state of California. That has ripple effects through the catastrophic property and casualty market in the US. That's been going on in Florida. It's been going on in the coastal Tier 1 areas for a couple years now. But that is a classic example of dumping and shutting business that can't do statutory rates, get the right price on the risk, so they dump it.

That's the business we're in. We have to adjust. We saw that coming a couple years ago. We develop high net worth, personal lines, facilities, recruited underwriters, recruited brokers, and that's now a new practice, new vertical for us.

Personal lines wasn't even in the E&S market 10 years ago. So, lots of acceleration coming into our industry, lots of opportunities for innovation, and again focusing on differentiating talent is the whole approach to the business.

Pat mentioned creativity, innovation, creating product or solutions, being able to move quickly and swiftly to create proprietary product, exclusive facilities that make us inexchangeable (sic) [unexchangeable] (16:50) with our competitors.

And so, today, there's two or three mega wholesalers in the US. One of them is owned by a big retail broker. That's a problem for them. That's channel conflict, distribution friction for them. If you look at their rate of growth, it's a fraction of ours. Two are pulling away, Amwins and ourselves. Clearly dedicated to independence, clearly dedicated to differentiating talent, building practice through verticals, a hub-and-spoke strategy.

But where we may be having the edge here, as we go forward, it's in the underwriting side of the business. It's binding authorities and small commercial. It's program business and affinity business opportunities, and MGUs and MGAs, which my partner, Miles Wuller, will get into in more detail.

But really Pat's vision was weaving that all together to create a higher value in the marketing exchange with our retail brokers and agents, and that's exactly what we've done. We've made ourselves indispensable to them as an extension of their marketing efforts on these very technical, high-risk property and casualty risks.

So, as we've talked about, you've heard of it a million times, the world unfortunately is getting riskier. Global warming, making commercial property risks almost in uninsurable uncertain regions. Casualty, social inflation, economic inflation, the litigation climate in the US is very, very difficult. We live it. We see it every day. That's driving more casualty business into our segment.

Latency on claims, COVID, all of that has made that whole process a lot more difficult. Standard companies, again, shedding the unprofitable business, and our role is to fill that void. The freedom of rate and form is the magic sauce, being able to handcraft these solutions very quickly and not be surrounded by the regulatory and compliance issues of rate and form.

So the outlook is very bright. We're bullish. We believe that market will continue to grow, and our commitment is to continue to recruit, train and develop broking talent, underwriting talent and manufacture our own. We're doing that today and leading the industry, being enable to create talent and make it accretive very quickly. And accelerating that process is something that we're very, very committed to. And you can see that in our numbers.

But we're excited about it. We appreciate your partnership. And now, I'll turn it over to the Underwriting CEO of Ryan Specialty. Thank you.

Miles Wuller

President & Chief Executive Officer, Ryan Specialty Underwriting Managers

Okay. Thank you for that, Tim. Great to be here today, I'm going to briefly discuss the marketplace today and what we've done to uniquely position Ryan Specialty delegated underwriting or Underwriting Managers segment.

So there is a structural shortfall in available underwriting capital today that's worth mentioning. We've had well over a decade of runaway inflation, compounded with social inflation, carriers said they actually subsidized a lot of that cost themselves to their balance sheet.

Look, if you look back on the last six years, five of them have been outsized cat years, both in wind and fire losses. So this is a property-centric comment, but there could be a $20 billion to $40 billion capital shortfall in the gap to meet the current southeast wind need in the US.

In past years, ILS might have swung in to fill some of that gap. It hasn't. Two reasons. Recent returns haven't been strong enough. Second, based on where interest rates have now become, they have other alternative uses for that capital. And then, additionally, in circumstances like this, we've often seen a Bermuda class arise to meet this need. There has not been a class of 2023 in Bermuda yet, in part because the community is still evaluating if pricing adequacy has been achieved in certain classes.

So, in cycles like this, often in these hard market conditions, carriers actually historically have delegated less to intermediaries such as ourselves. So, why have we thought that trend? So, I'm proud to say with our structure and what we've built that I'm going to dive into, we've been consistently adding capability and capacity throughout this cycle of the most recent years.

This comes in a couple of forms, all compounding growth opportunities for us. Incremental MGUs, which essentially mark an entrance into a new product specialty or new expertise, while bringing tangential product lines to existing MGUs. And then, lastly, we're increasing our carrier capital under management.

And so, what do I mean by that? So we're evaluated on a lot of the same themes as the investment community. We have a track record. We're delivering underwriting profit to our carriers. We have a 10-plus-year record. We're increasing returns to our carriers, and we're also deepening our expertise in -by verticals. And this has a bit of a virtuous cycle. So, carriers, once they see our expertise in one class of business, they understand our robust level of care in alignment to them will bring their support to incremental lines of business that we're doing, that are fueling incremental organic opportunities for us.

Structurally, what's making us unique – my colleagues have touched on our expertise. So each one of our 22 MGUs within our family are led by career experts. These are folks with decades of specialty experience. They've either come from the carrier marketplace or they've built and led other MGUs in those industry verticals. We have deep alignment that often carriers are unable to achieve on their – in a traditional balance sheet. So these staff are aligned to their results and there's an even greater alignment to the underwriting profit that they deliver to their carriers.

We happily share that with our teams. It perfects our alignment to our carriers that support us, and it also creates a bit of an earning trailer with these teams and for them to stay with us longer. Another investment we've made that started 13 years ago was our investment to deeply resource those teams. So data, technology, analytics, actuarial, cap modeling, regulatory compliance.

These are elements that set us apart from others in our space. And the most important element here is the carriers know that we are thinking about risk in the same manner. We're measuring it. We're going about to bed with the same concerns they are, and that we have the tools to essentially look around the corner and avoid some of these risks.

And I'll end with one of the greatest tools for us, and this has been our flexibility and speed to market. So we have the benefit of being such a great platform that when we see tailwinds, we have the ability to rapidly pivot our business to capture those tailwinds. And if we do see headwinds, again, we rapidly react to moderate them.

So, we appreciate the chance to be here and we look forward to answer some questions. And with that, I'll turn it back to Adam. Thank you so much.

QUESTION AND ANSWER SECTION

Adam Klauber
Analyst, William Blair & Co. LLC

Q

Thanks. I'll ask one or two and then we'll have time. By the way, the breakout will be here afterwards. So [indiscernible] (25:17) for questions.

I think one of the interesting things about your business is it's a very innovative product company that the products are changing all the time. So, as new markets like California, homeowners and personal lines is rapidly becoming more and more E&S and wholesale-centric, right? So maybe if you give examples, maybe let's pick cyber because cyber wasn't a big E&S market maybe five, six years ago. How do you develop a product? How do you put together a team? How quickly does it take to really get that up and running?

Timothy W. Turner
President & Director-Ryan Specialty and Chairman & Chief Executive Officer-Ryan Turner Specialty, Ryan Specialty Holdings, Inc.

A

I'd be happy to start on the brokering side and then maybe Miles can address it on the underwriting side.

Like so many of our products and specialties, we do both. We broker it and we underwrite it. Again, that's part of our differentiating approach and what creates a stronger value trading relationship with our retail brokers. But cyber is a great example of a new product. I call it a young broker's expertise. These kids really gravitated toward cyber early on before the big ransomware claims came in, before it became unprofitable for standard companies, and it emerged as a highly technical E&S product line. So the market really became hard.

Reinsurers withdrew. Standard markets withdrew. And over the last two, three years, it became a very much an E&S product line, very technical product line, short limits. Degrade online. And like a lot of this business, the percentage of cyber that poured into the E&S market grew exponentially.

And so, today, what we have is a market that is really burgeoning. Only 20% of the commercial buyers actually buy primary cyber limits. So 80% of the market is potentially a new buyer. And so, while cyber and ransomware claims flattened out over the last year or two, so the flow kind of started to stabilize into our channel, the ransomwares claims, picked up again.

And you can get those details monthly now. Those claims are pouring in. Standard markets are starting to get skittish again. So there's a lot of up and down volatility in cyber. And the brokers and the underwriters that spent their last three, four, five years dedicating themselves to the technical and crafting of these solutions are now in high demand.

So we're perfectly positioned in cyber. It's a great illustration of moving quickly, making sure you have depth and breadth in the broking ranks, and you're creating underwriting products and solutions to weave into our overall solution.

Adam Klauber
Analyst, William Blair & Co. LLC

Q

So, Tim, for you, just for example, I mean, how many people did you have in cyber in say four or five years? So roughly how many people in that group today?

Timothy W. Turner
President & Director-Ryan Specialty and Chairman & Chief Executive Officer-Ryan Turner Specialty, Ryan Specialty Holdings, Inc.

A

A couple dozen and now hundreds.

Adam Klauber
Analyst, William Blair & Co. LLC

Q

Yeah. You built a big business within two, three years, right?

Timothy W. Turner
President & Director-Ryan Specialty and Chairman & Chief Executive Officer-Ryan Turner Specialty, Ryan Specialty Holdings, Inc.

A

Yes.

Adam Klauber
Analyst, William Blair & Co. LLC

Q

Yeah. Miles, yeah, interested in it.

Miles Wuller
President & Chief Executive Officer, Ryan Specialty Underwriting Managers

A

Yes.

Adam Klauber
Analyst, William Blair & Co. LLC

Q

[indiscernible] (28:31)

Miles Wuller
President & Chief Executive Officer, Ryan Specialty Underwriting Managers

A

So all I would add is we have the benefit. It's a young vertical as Tim mentioned. So we have the benefit of – we identified talent early on in this space. And so the gentleman that has led this for us has been in the industry for 12 to 15 years, which is actually a healthy tenure in this space. He's surrounded himself with a great team, and it doesn't just stop there with underwriters. We have to bring claims experts, risk analysts, not just to track the aggregate exposure, but to have a detailed understanding of the threat landscape out in the marketplace and are insureds taking the right steps to protect themselves.

And so, we've built the team. We've equipped them with the resources. And as Tim said, we're constantly evolving our forms and coverage to meet the needs of the client. And we're also evolving the segments of the marketplace we decide to participate in to give the best results to the carrier.

Adam Klauber
Analyst, William Blair & Co. LLC

Great. With that, our time has to conclude. So I'd like to thank Pat and the team.

Patrick G. Ryan
Founder, Chairman & Chief Executive Officer, Ryan Specialty Holdings, Inc.

Thank you.

Adam Klauber
Analyst, William Blair & Co. LLC

And I want to emphasize again that they built a great franchise, but it's still very, very early given the ramp-up in the business. And the breakout section is here. So if you want to ask questions, please stick around.