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Ryan Specialty Holdings, Inc. (RYAN)

Q3 2022 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Greetings. Welcome to the Ryan Specialty Holdings Third Quarter 2022 Earnings Call. At this time, all participants are in listen-only mode. A question-and-answer session will follow the formal presentation. [Operator Instructions] Please note, this conference is being recorded.

At this time, I'll now turn the conference over to Noah Angeletti, Head of Investor Relations and Treasurer of Ryan Specialty Holdings. Noah, you may now begin.

Noah Angeletti

Treasurer & Head-Investor Relations, Ryan Specialty Holdings, Inc.

Good afternoon and thank you for joining us today for Ryan Specialty Holdings third quarter 2022 earnings conference call. In addition to this call, we filed a press release with the SEC earlier this afternoon, which has been posted to our website at ryanspecialty.com.

On today's call, management's prepared remarks and answers to your questions may contain forward-looking statements. Investors should not place undue reliance on any forward-looking statements. These statements are based on management's current expectations and beliefs, and are subject to risks and uncertainties that could cause actual results to differ materially from those discussed today. We encourage listeners to review the more detailed discussion of these risk factors contained in the company's filings with the SEC. We assume no duty to update such forward-looking statements in the future, except as required by law.

Additionally, certain non-GAAP financial measures will be discussed on this call and should not be considered in isolation or as a substitute for the financial information presented in accordance with GAAP. Reconciliations of these non-GAAP financial measures to the most closely comparable measures prepared in accordance with GAAP are included in our earnings release, which is filed with the SEC and available on the company's website.

With that, I'd now like to turn the call over to the Founder, Chairman and Chief Executive Officer of Ryan Specialty, Pat Ryan.

Patrick G. Ryan

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

Good afternoon and thank you for joining us to discuss our third quarter results. Joining us on today's call is our President, Tim Turner; and our CFO, Jeremiah Bickham. Also joining is Miles Wuller, CEO of our Underwriting Managers Specialty who will be around for the Q&A.

It was a solid quarter for Ryan Specialty and our differentiated platform. Total revenue grew 16.8%, led by 13.7% organic growth. In addition, we achieved double-digit growth in adjusted EBITDAC and solid growth in adjusted net income. Specific to the third quarter, the hard market for rates largely continued and we saw additional firming in many of our lines of business.

As we noted last quarter, one notable exception was public company D&O, which saw a rapid rate decline in the quarter, beyond what we and the market anticipated, and which Tim will touch upon shortly. Importantly, our ability to generate another quarter of double-digit organic growth despite this headwind and the exceptional third

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quarter 2021 comp speaks volumes about the strength of our team, our diverse product and services offering, and the winning culture we have built at Ryan Specialty.

As we've noted previously, risks across industries are only becoming more complex. Our products are largely compulsory, and our clients value the expertise we bring. Our producers continue to provide our clients and our trading partners with innovative solutions. But we want to acknowledge the increasingly challenging insurance and macroeconomic environment in specifically three areas where we are seeing headwinds that will likely [ph] cure (03:51) into at least the first half of 2023.

First, while the E&S marketplace remains a standout within the insurance industry, we began to see a deceleration in the growth rate of inbound flow towards the end of the quarter, which is backed by states' stamping reports. Second, a faster-than-anticipated economic deceleration, coupled with significantly higher interest rates, are delaying certain project-based construction policies, along with M&A transaction liability policies that rely on highly functioning debt markets. Third, changing market conditions in the public D&O market have had an impact on our professional lines book.

After years of rate hardening, new capacity entered the market, leading to additional supply and a decrease in rate at a time when IPO activity is down significantly. This has also led to increased opportunities for retail brokers to place some of this business directly. Our collective experience has allowed us to successfully manage through different economic cycles in the past and we are confident that our leadership team is well-positioned to execute our game plan through this cycle as well.

We're also pleased to note that productivity among our brokers continues to improve, a testament to their tireless efforts to be laser-focused on client centricity and to match market needs with industry-leading expertise. We are also prudently continuing to onboard top-decile talent to add to our industry-leading team and deep bench to take advantage of the resilient E&S flow and continue gaining market share. Additionally, our M&A pipeline remains robust as we look for additional opportunities, both tuck-ins and larger acquisitions, to enhance and differentiate our platform and capabilities.

We remain disciplined in our pursuit of acquisitions, particularly in the current environment, as we will only move forward when all our criteria are met. Every acquisition must be a strong cultural fit, strategic and accretive. Our discipline is bolstered by our core results, which have proven throughout this year that we do not require acquisitions to achieve robust growth in any given period.

As we begin to turn the page on 2022, we believe we remain well-positioned to succeed over the long-term, given our resilient and flexible operating model that enables us to quickly adapt and pivot to an increasingly challenging macroeconomic environment. We, nonetheless, remain confident that the value we bring to our trading partners, particularly in times of uncertainty, remains extremely valuable as we anticipate their needs and work tirelessly to provide the right solutions to protect their insurance risks.

As it has in the past, we expect the E&S market will continue to grow as the world becomes riskier and more complex. This, along with other secular growth drivers, should allow us to generate annual double-digit organic growth for years to come.

In summary, I remain proud of our entire team at Ryan Specialty, as their incredible effort led to another solid quarter and a 2022 that will surpass our expectations from when we started the year.

Now I'll turn it over to Tim. Tim?

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Timothy W. Turner

President & Director; Chairman & Chief Executive Officer-RT Specialty, Ryan Specialty Holdings, Inc.

Thank you very, Pat. As Pat highlighted, it was another solid quarter across our specialties, and the E&S market continues to serve a critical role in an increasingly challenging insurance landscape. This was backed up by AM Best's recent report, which highlighted the sustained expansion and rise in demand for E&S solutions, driven by constantly evolving risks and rapidly innovating technology. We are in a prime position to continue to capitalize on these positive trends.

Diving into our specialties, our Wholesale Brokerage specialty achieved another quarter of strong growth across property and casualty lines of business. Once again, cat property was the strongest driver of new business into the non-admitted market. Since our last call, Hurricane Ian, a devastating storm, caused tens of billions of dollars of damage. I would like to take a minute to send our best wishes to all of those that were impacted by this horrible disaster.

We believe these types of loss events, along with themes we've previously discussed, are leading to shrinking capacity as well as even higher rates. Ultimately, we believe these factors will lead to more flow into the E&S market as reinsurers further de-risk their portfolios during upcoming renewal cycles. We also expect increased flow from other non-cat markets. There will be a significant need for E&S solutions in 2023, and our depth and breadth of experience and products will remain in high demand. We will continue to develop innovative solutions in our brokerage and delegated underwriting authority businesses in these high-hazard niches in order to take advantage of these incoming opportunities.

Cyber was a strong performer in the quarter. Flow continued to be robust into the E&S channel. As noted previously, we complement our brokers with capacity from our delegated underwriting authorities, as evidenced by our announcement of a new $15 million exclusive excess cyber facility, supported by highly rated carriers. It's another example of our brokers innovating on behalf of their clients, as well as the staying power our delegated authority demonstrates and how it continues to be a top choice for carrier capital.

Our transportation practice, particularly in trucking, continues to see sizable flows. We continue to win business in this line and remain well positioned to capitalize on additional growth opportunities. Our construction practice performed well in the quarter. We are encouraged by the submissions that we're seeing in the current pipeline of projects. However, we should note that we've begun to observe delayed project starts due to the rapid increase in interest rates and a slowdown in the economy.

As Pat noted, our public company D&O practice experienced some headwinds in the quarter as well. As we noted on our prior call, we began to see rate decreases in public company D&O during the second quarter. In the third quarter, the pace of rate decreases in that line accelerated. This and the market forces that Pat referenced are what we began to observe earlier this year and have referenced in prior calls. These had a significant mitigating impact on the strong growth in our other lines. We expect these trends in public company D&O to continue into at least mid-2023. However, we are confident that we have the team and platform in place to continue to grow in this line over the long term.

In our Binding Authorities specialty, we saw solid growth in traditional binding, which includes small commercial business that has historically been economically sensitive. This growth was reduced by our personal lines binding authority, which has experienced capacity constraints, an area of focus for our upcoming carrier renewals. Additionally, the panel consolidation opportunity that we've mentioned for a number of quarters is just beginning to bear fruit. We see this as a long and steady growth opportunity and we are well positioned to execute.

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Our Underwriting Management specialty posted another strong quarter despite dislocated debt capital markets and less M&A activity, resulting in less transactional liability business being bound, while continuing to deliver solid underwriting results for our carrier trading partners. We are also seeing continued progress with our de novos through our Harleysville of New York arrangement with Nationwide.

In terms of the E&S market, pricing remains firm in many classes of business, with the notable exception of public company D&O rates that Pat mentioned earlier; and cyber, where we are seeing a flattening in rate. As we said several times before, we expect the flow of business into the non-admitted market to continue to be a significant driver of Ryan Specialty's growth opportunity, more so than rate.

With that, I will now turn the call over to our Chief Financial Officer, Jeremiah Bickham, who will give you more detail on the financial results of our third quarter. Thank you.

Jeremiah R. Bickham

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

Thank you, Tim. In Q3, we grew total revenue 16.8% period-over-period to $412 million, which was fueled by another solid quarter of organic revenue growth at 13.7%, reflecting the ongoing tailwinds in most of the E&S market and continuing to win a substantial amount of new business, despite the nearly 29% year-over-year comp.

Net income for Q3 2022 was $29 million or $0.09 per diluted share. Adjusted net income for the quarter, which excludes IPO-related and other unusual items, increased 6% period-over-period to $67 million or $0.25 per diluted share. Adjusted EBITDAC for the third quarter grew 11% period-over-period to $117 million, while adjusted EBITDAC margin declined 140 basis points to 28.4%.

Our adjusted EBITDAC margin was impacted by continued investments in the business and T&E continuing to return to normalized levels, and also improved by higher fiduciary income. It should be noted that relative to Q3 of 2019, which had a full run rate of T&E, our margin was up 450 basis points in the quarter, again, showing the proven scalability of our model over the years.

Moving forward, we will prudently continue our hiring practice of finding the industry's top talent in both underwriting and broking, where there are clear opportunities to grow lines of business. We also fully intend to continue investing in our platform, which allows us to generate sustainable margins, while producing industry-leading organic revenue growth.

As we do so, we will continue to closely monitor the macroeconomic environment and industry for additional signs of slowing to ensure that our investments in talent and infrastructure are accretive. Furthermore, our balance sheet remains fortified with $833 million of cash and cash equivalents, as of September 30, in addition to our $600 million of undrawn revolving credit facilities.

To that end, it has always been important to us to maintain a strong financial position. I want to highlight our timely capital raise at the beginning of this year, before the cycle of steep rate hikes began, which diversified our funding sources. We expect to record GAAP interest expense, which is net of interest income on our operating funds and includes amortization on our interest rate cap, of approximately $31 million for Q4 2022. And for the first time, we are beginning to receive payments under our interest rate cap.

Again, it is important to be mindful that the impact of increased interest expense is mitigated by the natural hedge on our fiduciary balances, which benefit from the rising rate environment. These fiduciary balances continue to generate fiduciary investment income at approximately one-month term SOFR less approximately 50 basis points.

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This spread to SOFR factors an earnings yield that may lag the forward curve, as well as some fiduciary balances which are not permitted to earn yield or that earn soft yield that is instead an offset to our bank fees and SG&A expense. Additionally, it is important for us to note that given the timing of our M&A pipeline, it is unlikely that we will close a sizable deal in Q4. But as Pat mentioned, our M&A pipeline remains robust and we remain disciplined in our approach.

Taking a step back, through our first nine months, we generated exceptional organic growth and healthy adjusted EBITDAC margin. As Pat and Tim mentioned, the long-term Ryan story remains very much intact. However, given current headwinds in public company D&O and macroeconomic headwinds impacting construction starts and M&A transaction liability activity, we are lowering our full-year 2022 guidance for organic revenue growth to 14.5% to 16.0% from the previous guide range of 16.5% to 18.0%. This implies a mid-single-digit midpoint for organic revenue growth in Q4.

This guide range is ahead of where our expectations were for full-year 2022 at the beginning of the year, when it was difficult to predict the timing and degree of these market changes and macroeconomic impacts. In addition, we are now guiding our adjusted EBITDAC margin for the full-year 2022 to be between 29.5% and 30.0% from the previous guide range of 29.0% to 30.0%.

In summary, we remain very pleased with our performance year-to-date and are focused on the path ahead, as we navigate through the coming economic cycle.

With that, we thank you for your time and would like to open up the call for Q&A. Operator?

QUESTION AND ANSWER SECTION

Operator: Thank you. Before we begin, I'm aware that there may be an audio issue as participants dialed into the conference line. If you are able to switch to the webcast, we understand that this is unaffected by the audio issues. Thank you. And at this time, we'll be conducting a question-and-answer session. [Operator Instructions] Thank you. And our first question is coming from the line of Elyse Greenspan with Wells Fargo. Please proceed with your question.

Elyse Greenspan
Analyst, Wells Fargo Securities LLC

Q

Hi. Thanks. Good evening. My first question, you guys said that you're expecting a slowdown in organic growth to the mid-single digits in the fourth quarter. Is there an overconcentration in public D&O, M&A and some of these other lines that you're calling out as having headwinds in the fourth quarter? Because from Pat's comment, it sounds like you guys are still looking for consistent double-digit organic growth, so would you expect things to pick up to that level next year? I'm just wondering how business mix is impacting the fourth quarter versus what we could see in 2023.

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

A

Hi, Elyse. Thank you for your question. So we are, in fact, still double-digit growers on an annual basis. We are talking about Q4. And like we've said in the quarters of 20%-plus growth, you can't look at any quarter up or down and extrapolate a trend.

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To your question about concentration, I can say that no single product line, including public D&O, is even 10% of our overall book. We have a very overall well-diversified portfolio of products and specialties. It's just last year, public D&O specifically had an outsized growth contribution and this quarter it actually shrank dramatically. So it went from being a contributor to a drag on our organic. But we are confident that D&O and our entire professional lines practice is one that we're very strong in and that we can continue to grow long-term.

Elyse Greenspan
Analyst, Wells Fargo Securities LLC

Q

And then, in terms of the property exposure, can you give us a sense how big that is of your book? And I would think that when we think about 2023 and the market hardening post-Hurricane Ian, that that could be a tailwind to your growth next year.

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

A

So, in terms of the property exposure, well, I want to say be careful and not use exposure and insinuate underwriting risk exposure. The percentage of our book that is related to property is many, many multiples of our D&O book. We don't disclose the exact percentage, but it's material. And in terms of the impacts on our business overall and what we're seeing in that market, I think Tim is best positioned to speak to that.

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

A

Yes, I'd be happy to. The forecast for catastrophic property, a very large part of our property practice group, is much hardening. We expect the market going into 2023 to get extremely difficult and hard and the flow of business into our channel to increase substantially. We're set up to absorb it and capture it. And we're ready to take on the challenge. But it will be a very big driver of new business for us as we go into 2023.

Elyse Greenspan
Analyst, Wells Fargo Securities LLC

Q

And then just maybe one last one. You guys had mentioned that you saw a little bit of a slowdown in flow of business to the E&S market. Was that specific to certain business lines and would you expect that [ph] working in (22:29) and I guess the ramifications on the property market could reserve that?

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

A

We've seen a very slight indication of a slowdown in flow into the channel through the last month in the stamping offices, very slight. And the flow remains double-digit, very strong, flowing into our world. So, no let-up that we can see in general casualty. And again, property, we're already seeing signs of the effects of the storm and affirming and an increase in flow here in this quarter.

Elyse Greenspan
Analyst, Wells Fargo Securities LLC

Q

Thanks for the color.

Operator: Our next question comes from the line of Weston Bloomer with UBS. Please proceed with your questions.

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Weston Bloomer
Analyst, UBS Securities LLC

Q

Thank you for taking my questions. The first one is a follow-up on the organic growth commentary that should be slower in the first half of the year. Are you expecting kind of organic to come in kind of below that double-digit range in the first half or could we maybe see an offset from stronger property growth? Just trying to figure out how we should think about the magnitude of...

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

A

Weston, hey, it's Jeremiah. The same glitches that the operator mentioned at the beginning of Q&A, we're actually getting on this side too. So you broke up. Would you mind repeating the question?

Weston Bloomer
Analyst, UBS Securities LLC

Q

Yes. Switching from the headset too. Is this better?

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

A

Yeah. So far, so good.

Weston Bloomer
Analyst, UBS Securities LLC

Q

Great. I was hoping you could comment on kind of the magnitude of the slowdown that you're expecting in the first half of the year. I know you've historically guided to annual double-digit organic growth. But could we potentially see single-digit organic growth in the first half if these trends continue? Or maybe would we see a partial offset from an accelerating property market?

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

A

Fair question. It is a little bit premature to talk about 2023 guidance. Like, we'll obviously know a lot more when we come back to you in February, Weston. But a couple of points to keep in mind between now and then. And most importantly, our strategy, our thesis, our competitive position, our value-add to our clients, no change there. All of those are very much intact. And rate decline, by the way, which we're going to talk a lot about – we talked a lot about in our remarks. Specifically in D&O, it's not our kryptonite. Like, it's part of life for our company. We've managed through it for years and produced double-digit organic growth on an annual basis year-in and year-out through that. So we actually think that this whipsaw in D&O is fairly unique.

And we've got this known public headwind, D&O, but we believe that we will cycle through it by the beginning – I'm sorry, the middle of next year. And we also have macroeconomic factors that play an unknown role in terms of impact and duration. And I think all companies are facing that right now. But as you mentioned, not all the variables in play, especially when we're talking about next year, are negative. The property market, as Tim said, is expected to get very hard and will be a benefit to us. And as I said, our property book is many multiples of our D&O book.

And so we're not trying to convey a concern. As I said, we are still double-digit organic growers on an annual basis. We're just trying to be transparent that there's a lot of uncertainty out there. It's difficult to predict all the

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rates of change that are affecting our industry. And so, like always, we have to be prudent with regards to setting expectations. But we're still very bullish about our long-term growth prospects and the durability of the E&S market overall.

Weston Bloomer
Analyst, UBS Securities LLC

Q

Great. And a follow-up to that, I know 1Q and 2Q organic outperformed and you had called out in the past kind of some timing – or lumpy timing with transactions. How much of that was related to the D&O book and the transaction liability? Like, is there a way to quantify how much of that outperformed in the first half of the year?

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

A

Weston, I hope that you can hear us better than we can hear you because we missed the first half of your question.

Weston Bloomer
Analyst, UBS Securities LLC

Q

The question was really how much of maybe the M&A transaction liability or D&O led to the outperformance in the first half of this year? Is there a way to quantify that?

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

A

I would say – I'm going to start and then Miles Wuller, who's on the call who manages our two transaction liability MGUs, will speak to some of the trends there. But the bigger theme here is that the surge in D&O happened last year. And so we're facing an exceptionally difficult comp. And as much – actually more than it was a contributor to our growth last year, it was a drag this year. And it actually started modestly at the very, very end of Q2 and we adjusted our expectations for H2 as a result of that, but it accelerated even more than we anticipated.

On the M&A side, we didn't have a outsized H1 that's now reversing. We had a fairly normal H1 just because despite the fact that there's been no substantial IPO activity this year and – M&A activity, I'm sorry, M&A activity, the impact of on closing those deals – the timing of closing those deals didn't really start affecting us until Q3. And we have to assume, because rates don't appear to be coming down or moderating any time soon, that that persists at least for the short term.

But, Miles, I don't know if there's any other color you want to add to that trend.

Miles Wuller
President & Chief Executive Officer-Underwriting Managers, Ryan Specialty Holdings, Inc.

A

No, absolutely. I mean, we benefit from both the US and international practice within our portfolio. So, global M&A is drifting down this year compared to last year, as much as 20% to 30% depending on geography. Year-to-date, as a leader, we've continued to grow and achieve rate. But I think we've rightly flagged here that submissions have started to decline more in the last 90 days, somewhat linked to the recessionary environment, either keeping sellers from bringing new deals to the market or not finding market clearing price on deals.

And as both Pat and Tim have highlighted, a reasonably functioning debt capital markets is needed to keep our optimal growth rates up. I'm happy to say we've recorded record levels of deals in inventory that are signed and the coverage is accepted. However, the deals are waiting to close as they await financing.

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Weston Bloomer
Analyst, UBS Securities LLC

Q

Great. And last one for me. I know you don't give organic growth by underwriting practice. I was hoping you could kind of help size the growth you saw across underwriting, binding and MGU in the quarter, and kind of what your expectations are by each one in the 4Q.

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

A

Jeremiah, you want to take that one? And, Miles, you can pick up on the underwriting.

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

A

So, in the Q, Weston, you can actually see revenue growth by specialty. We break it out by binding, brokerage and underwriting managers. As we've said before, all of these specialties have double-digit growth capabilities, and more often than not, they do. The headwinds we're talking about them are affecting each of them differently. So the SME market slowdown, that's mostly a binding specialty effector.

What's going on in public D&O, that's hitting brokerage more than the other two specialties. And then transaction liability, the majority of the impact there that Miles just talked about, that's in underwriting managers. So what we're assuming for Q4 is actually that all the headwinds that we experienced in Q3 not only continue but get a little bit worse.

Weston Bloomer
Analyst, UBS Securities LLC

Q

Great. Thanks for taking my questions.

Operator: Thank you. Our next question comes from the line of Rob Cox with Goldman Sachs. Please proceed with your questions.

Robert Cox
Analyst, Goldman Sachs & Co. LLC

Q

Hey. I just had a question on supplemental and contingent commissions. I noticed in the 10-Q, they declined 36% year-over-year, after growing pretty solidly in 2Q. And I was just wondering what that was driven by and if it was related at all to catastrophe activity in the quarter.

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

A

You broke up at the end. Did you ask if it was related to Ian?

Robert Cox
Analyst, Goldman Sachs & Co. LLC

Q

Yes.

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

A

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Hello?

Robert Cox
Analyst, Goldman Sachs & Co. LLC

Q

Yes, yes. If it was related to catastrophe activity, yes.

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

A

The answer is no. It's really a timing issue more than anything. The effects of Ian won't show up until down the line, like mostly next year and beyond, although we do expect that impact to be immaterial. The quarter-over-quarter is, as I said, a timing issue. And sometimes we restructure to often improve our profit commission or contingent commission arrangements, and we actually restructured a material one this year that altered the timing of what we would normally receive. So, no material negative impact on the contingent commission front specifically related to Ian.

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

A

Miles, do you want to add anything or Tim?

Robert Cox
Analyst, Goldman Sachs & Co. LLC

Q

Okay.

Miles Wuller
President & Chief Executive Officer-Underwriting Managers, Ryan Specialty Holdings, Inc.

A

All that I would say is we're having a strong year for profit commissions year-to-date, as Jeremiah mentioned, that's reflective of recent years. Our view on that forward-looking view of Ian actually is we are extremely pleased with our loss results so far. We're actually – based on claims activity to date and model results, we're expecting to dramatically outperform the industry in Ian. So we're counting on that as a future benefit leading into next year.

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

A

And I would add, our Binding Authorities within RT continue to perform exceptionally well. Our contingency forecast remains very strong and we're on track. So, everything's working out very well in that unit.

Robert Cox
Analyst, Goldman Sachs & Co. LLC

Q

Got it. Thank you. And then, was growth impacted at all in the quarter by lower property placements in this quarter versus kind of first half of the year?

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

A

I'm sorry to ask you again. It broke up for the first part of your question.

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Robert Cox
Analyst, Goldman Sachs & Co. LLC

Q

Yeah. Was growth impacted by lower property placements in 3Q versus the first half of the year?

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

A

No, I don't believe so.

Robert Cox
Analyst, Goldman Sachs & Co. LLC

Q

Got it. Thanks.

Operator: Our next question comes from the line of Meyer Shields with KBW. Please proceed with your question.

Meyer Shields
Analyst, Keefe, Bruyette & Woods, Inc.

Q

Great. Thanks. Good evening. I hope I'm coming through clearly.

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

A

So far, so good. Fingers crossed.

Meyer Shields
Analyst, Keefe, Bruyette & Woods, Inc.

Q

Okay. All right. Just hoping. Just to follow up on Rob's questions. Did the year-over-year decline in contingents – did that impact organic growth in the quarter at all?

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

A

I only heard the back end of your question, but I think I picked up the essence. Contingent commissions are stripped out of the organic growth calculation. No. So, no impact to organic.

Meyer Shields
Analyst, Keefe, Bruyette & Woods, Inc.

Q

Okay. Perfect. I was hoping, I guess this is for Tim, for a little bit more color on the – or maybe Miles, the impact of personal lines capacity, because you had called that out as one of the issues that's maybe also a bit of a headwind right now.

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

A

Yes. Our personal lines division, a much smaller division within binding, was short of some wind and flood capacity that affected their ability to write new business and the competitive landscape prior to Ian. But we've remedied that and we expect that to be – our capacity to be where it needs to be as we head into the fourth quarter and geared up for 2023. So we've fixed that and we expect it to be back to normal capacity.

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Meyer Shields
Analyst, Keefe, Bruyette & Woods, Inc.
Q

Okay. Perfect. That is helpful. And then last question. Just in terms of overall expectations, do you see any connection between a weakening economic environment and the incremental competitiveness or deal flow case? Are those connected at all or is that just a function of what's happening within P&C?

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

I'm sorry, Meyer, would you repeat it? I heard is there a connection between the economic slowdown and the competitiveness and the pace of deal flow. Is that related to risks that need to be placed or like M&A?

Meyer Shields
Analyst, Keefe, Bruyette & Woods, Inc.
Q

So, in terms of risks, it need to be placed. Are we seeing less business go to the specialty channel as a consequence of a potential economic slowdown? Or do you see that as separate and just coinciding right now?

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

We really see that as separate and have not identified any impact on flow. As we said, the top stamping office results that have come in in the last couple of months showed a very, very slight deceleration, hardly detectable, still double-digit very strong flow coming into the non-admitted space.

Meyer Shields
Analyst, Keefe, Bruyette & Woods, Inc.
Q

All right. Perfect. Thank you very much.

Operator: Our next question comes from the line of Tracy Benguigui with Barclays. Please proceed with your question.

Tracy Benguigui
Analyst, Barclays Capital, Inc.
Q

You took up the lower end of your EBITDAC margin guide by 50 basis points with lower top line growth. What is driving that? Are you focusing more on expense savings now that you're seeing these top line growth pressures?

Jeremiah R. Bickham
Chief Financial Officer & Executive Vice President, Ryan Specialty Holdings, Inc.
A

We're always focused on managing to the bottom line, Tracy. And 50 basis points may seem tight, but it represents a decent amount of variability given that we only have two months left in the year. We are definitely making investment in hiring decisions in the context of top line expectations. We haven't spent as much on new talent acquisition as we thought we potentially could in the beginning of the year. And quite frankly, investment income has been a little bit higher than we expected. But we have a pretty good sense of where we're going to end the year, given that it's already November 10.

Tracy Benguigui
Analyst, Barclays Capital, Inc.
Q

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Got it. And then on the D&O, I'm just wondering, were there any programs that maybe you're no longer a part of. So it's not just the pressures we're seeing on pricing, but maybe something more specific to your business.

Miles Wuller
President & Chief Executive Officer-Underwriting Managers, Ryan Specialty Holdings, Inc.

A

I'll respond from the Underwriting Managers. We've kept all of our facilities intact. We've delivered great results to our carriers. We actually grew our capacity last year. And so, no, there's nothing unique to us. We have the capacity, the capability. It's just an overall pullback in the marketplace and we're not going to chase.

Tracy Benguigui
Analyst, Barclays Capital, Inc.

Q

Thank you.

Operator: Our next question is from the line of Jimmy Bhullar with JPMorgan. Please proceed with your question.

Jimmy S. Bhullar
Analyst, JPMorgan Securities LLC

Q

Hi. So, first on just your organic growth, I think you're implying that growth slowed as the quarter – as you went through the third quarter. Can you maybe quantify or just give us a better idea on what the actual growth was early in the quarter versus late in the quarter and so we get a better sense of how 4Q is looking?

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

A

Well, we're definitely not going to break out growth by month. But given that it is November 10 already, we're taking everything we've seen through today into account with our Q4 outlook, for sure. And as I said, Jimmy, we are assuming that all the things that slowed us down in Q3 persist and actually accelerate. It's really difficult to predict where a rate of change actually inflects. But we're sticking to our MO of being as prudent and transparent as we can.

Jimmy S. Bhullar
Analyst, JPMorgan Securities LLC

Q

Okay. And then if you think about the overall E&S market and your business, obviously it's grown a lot faster than the standard market and partly because exposures have been coming into the E&S market. Do you think at all if pricing in the primary market sort of slows down a little bit or flattens out, would that affect the flow of business into E&S in the short-term? Like, would some of the business that's come into E&S, could that end up going back to standard lines, even if the – in the short-term, even if the long-term growth outlook for the market stood?

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

A

I'm not sure I fully understood the question, but I think what you're asking is, would that have any impact on the flow into the non-admitted business, the [indiscernible] (40:51)?

Jimmy S. Bhullar
Analyst, JPMorgan Securities LLC

Q

Exactly. Yeah, yeah.

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

A

Yeah. I don't believe so. I believe that the losses coming from social inflation and global warming continue to impact the balance sheets of the standard markets. And they're continually de-risking their portfolios, directly affecting that heavy flow into our channel.

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

A

Jimmy, with your question, I think it's appropriate. This is Pat. Myles talk about cyber because cyber needs to be explained in terms of some really good news for the industry and for commerce in general. So, Myles, you want to explain the cyber?

Miles Wuller
President & Chief Executive Officer-Underwriting Managers, Ryan Specialty Holdings, Inc.

A

Yeah, absolutely. So, dovetailing your question, Jimmy, I mean, using cyber as an example, last year, the US cyber market actually doubled and E&S met that need by growing at 220% relative to only 20% growth in the admitted market. So, 2022 might not be as dramatic, but E&S will continue to lead the way. Why is this even more relevant, this class? Well, despite a doubling of growth in the market, we still believe that only 90% – excuse me, as much as 90% of the cyber market remains uninsured today. So, there's a huge runway for us to pursue regardless of short-term pricing trends.

But as it relates to pricing, exactly, so we are monitoring it closely. There is some flattening underway. Again, another class that we've benefited from the hard market dynamics. Our underwriting has enabled us to grow our facilities both in limit and total premium available to write on a delegated basis. But within the market, companies have invested in risk management and loss control, resulting in improving loss trends.

Risk premium related to the Ukraine war is slowly leaking out of the market as there hasn't been an associated shock loss to date. And so, ultimately we are seeing a stabilizing environment where rate adequacy has improved. And there is an increase in carrier competition, but that doesn't change our overall view that we're in the early stages of penetrating this addressable market.

Jimmy S. Bhullar
Analyst, JPMorgan Securities LLC

Q

Sure. And lastly, just in terms of growth versus margins, I think versus many of the retail brokers and some of the more mature companies, you have had a preference for investing in the business while you were growing very fast. So I think margins haven't expanded as much as they normally would have expanded, given your significant growth. But should we assume a change in focus in terms of growth spending if revenue growth slows down? Or are you going to be consistent with how you've been in the past in terms of sort of investing in the business?

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

A

Hi, Jimmy. The short answer is we're going to stick to our game plan, which is balancing, making necessary investments to continue outsized organic growth, while managing margin and growing it over time. It doesn't mean every quarter. It won't even mean every year necessarily. But what we're on record for shooting for here is that most years on a reported basis, we are going to show scaling in margin.

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And as I said in answering Tracy's question, just with our lower growth in Q3 and our expected lower growth in Q4, we're already beginning to adapt. And fortunately, we've got practice adapting and being flexible and we're fortunate because, for starters, a huge amount of our cost basis is variable to begin with. So we're going to stick to our plan.

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

A

One last comment by Myles.

Miles Wuller
President & Chief Executive Officer-Underwriting Managers, Ryan Specialty Holdings, Inc.

A

Yeah. And, Jimmy, just to be fulsome on cyber, as an example, the hardest to place commercial business, a lot of that is the growth continues in E&S. However, in some of the small and medium business, there is increasing competition that the admitted lines can't solve for in some cases. So, there might start to be fraying in that end of the market.

Jimmy S. Bhullar
Analyst, JPMorgan Securities LLC

Q

Yeah. And then cyber is understandable because it's – there's way more demand than there is supply of capital to cover the risk. But how big...

Miles Wuller
President & Chief Executive Officer-Underwriting Managers, Ryan Specialty Holdings, Inc.

A

That's all right.

Jimmy S. Bhullar
Analyst, JPMorgan Securities LLC

Q

But it's a pretty small market, right? Cyber is like 2% of the market for the primary companies. Is it a lot larger than that for you guys?

Miles Wuller
President & Chief Executive Officer-Underwriting Managers, Ryan Specialty Holdings, Inc.

A

Well. Back to Jeremiah's response, we have the benefit of 23 MGUs in the family in the National Programs unit with 17 niches. So we're not dependent on any particular product within the family. But we feel we have a material practice with a lot of upside in addressing the market.

Jimmy S. Bhullar
Analyst, JPMorgan Securities LLC

Q

Thank you.

Miles Wuller
President & Chief Executive Officer-Underwriting Managers, Ryan Specialty Holdings, Inc.

A

Thank you.

Operator: The next question is from the line of Mike Zaremski with BMO. Please proceed with your questions.

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Mike Zaremski
Analyst, BMO Capital Markets Corp.

Q

Hey. Good evening. Questions on cash flows from operations. I know there's noise in this that we need to back out. But curious if there's anything you want to call out on the call or should we be thinking that cash flow from operations grows on a full-year basis or especially into 2023.

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

A

So, thank you for bringing that up, Mike. This quarter is the perfect example why we guide people towards our adjusted view of cash flow. Operating cash flow this quarter was impacted significantly by a 100 – a nine-figure payment to finish out the all-risk LTIP plans, which by the way, are earn-outs. Essentially they're purchase price reductions.

But because they're paid to employees, non-equity holders, GAAP forces you to run that through the P&L as comp. And we absolutely love that because it's sticky and it makes a lot of new family members happy. So this concept is not going away. We're going to put these in as many deals as we can. But it's a great example of why a traditional view of operating cash flow is going to have noise in us for quite some time.

Mike Zaremski
Analyst, BMO Capital Markets Corp.

Q

Okay. That's very helpful. And just curious, I know it's early days in terms of higher interest rates, but is – do you see that impacting the M&A marketplace in terms of deals and competition for deals you guys are looking at or not really yet?

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

A

We have a very robust pipeline, both in brokerage, managing underwriting and benefits. As we've said, we've been very disciplined in not reacting to just doing a deal. So we've done a lot of – we've had a lot of discussions. We have some people we're in significant discussion with on quite strategic opportunities. So we're bullish on our M&A activity. But we won't close anything this calendar year, but we're in good position to bring in strategic opportunities next year. And the market has still been robust in terms of multiples. And so we've avoided what we consider to be excess multiples in terms of valuation.

And as I said, we look at the culture and the strategy in the equation, but also we look at the impact we can have on our total enterprise by bringing these companies in. And so, we'll look at valuation and say, what kind of cost synergies are there that are material. We never price in the value of revenue synergies, but our revenue synergies have historically been very significant. So, if you take the All Risks acquisition, they have outperformed our expectations in terms of their brokers' productivity increases. So, synergy on revenue is something that we look for as we value our potential opportunity, but we don't pay for that.

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

A

And Mike, to the part of your question related to firepower and how that positions us versus other would be veterans, we actually feel like we're in a great spot because we raised our bond in January. And I'm sure you saw we've got over $800 million of cash on the balance sheet. We have an $600 million undrawn revolver. We're levered at less than 2.5 times net.

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So it's not as important for like tuck-in deals, but if we're competing on a large property and our competition has to go raise new capital, like, that is going to be an advantage for us. We're really fortunate that we could take down big targets right now without raising new capital. As Pat said, it hasn't – we haven't seen a huge impact in multiples yet, but for big deals, we think it could give us an edge.

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

A

I'd like to just say [ph] one last (51:17) one of my comments. It's possible that we could close the deal before year-end. Here we are almost November, so forecasting that. But we have some attractive opportunities.

Mike Zaremski
Analyst, BMO Capital Markets Corp.

Q

Thank you.

Operator: Thank you. At this time, there are no additional questions. I'll now turn the call over to Pat Ryan for closing remarks.

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

Thank you all for your continued interest and support of Ryan Specialty. We look forward to speaking with many of you in the next few days, but we particularly look forward to discussing our fourth quarter 2022 results. Thanks for your support and your interest.

Operator: This will conclude today's conference. You may disconnect your lines at this time. Thank you for your participation.

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