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Ryan Specialty Group Holdings, Inc.

(RYAN)

Q4 2021 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Greetings. Welcome to the Ryan Specialty Group Fourth Quarter 2021 Earnings Call. At this time, all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation. [Operator Instructions] Please note this conference is being recorded.

I will now turn the conference over to your host, Noah Angeletti, Treasurer and Head of Investor Relations for Ryan Specialty Group. Thank you. You may begin.

Noah Angeletti
Senior Vice President, Head-Investor Relations & Treasurer, Ryan Specialty Group Holdings, Inc.

Thank you, operator. Good afternoon, and welcome to Ryan Specialty Group Holdings fourth quarter 2021 earnings call. This afternoon, the company released its financial results for the quarter and year ended December 31, 2021. The earnings release is available on the Investors section of the company's website at ryansg.com.

I would like to remind everyone that certain statements made during this call are not based on historical information and may constitute forward-looking statements. Any statements that refer to projections, forecast, guidance, outlook or other characterizations of future plans, integration, expectations, events or circumstances, including any underlying assumptions, are forward-looking statements.

These statements are based on management's current expectations and beliefs and are subject to a number of trends and uncertainties that could cause actual results to differ materially from those described in the forward-looking statements. I refer you to the company's filings made with the SEC for a more detailed discussion of the risk factors that could cause actual results, timing, levels of activity, performance or achievements to differ materially those expressed or implied in any forward-looking statements made today.

Investors should not place undue reliance on any forward-looking statement. The company undertakes no duty to update any forward-looking statements that may be made during the course of this call, except as required by law.

Additionally, certain non-GAAP financial measures will be discussed on this call, including organic revenue growth rate, adjusted net income, adjusted EBITDA and adjusted diluted EPS. Our presentation of this information is not intended to 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 available in the Investors section of the company's website at ryansg.com.

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

Patrick G. Ryan

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

Good afternoon, everyone. Thank you for joining us on our fourth quarter 2021 earnings conference call. On today's call, I will provide a brief overview of the quarter and the full year, and our strategy moving forward. Our President, Tim Turner, will then give an update on each of our three specialties and recent events. Last, our CFO, Jeremiah Bickham, will walk you through our financials. And then we'll open it up for Q&A.

Our fourth quarter performance capped off an outstanding 2021 for Ryan Specialty. We continued to execute well across our business during the quarter, generating another strong quarter of double-digit organic revenue growth, leading to full year 2021 organic revenue growth of 22.4% and total revenue growth of 41%. We continue to demonstrate every single day a clear and differentiated value that the Ryan Specialty platform provides through its new and existing clients.

Along with our extraordinary top line growth, we are proud of our numerous additional accomplishments in 2021. We grew our adjusted EBITDAC by 57% from the prior year, driven by our strong organic growth and the inclusion of All Risks for a full year. Just as importantly, the scalability of our platform was clearly validated in 2021, as we improved our adjusted EBITDAC margin by 330 basis points from 2020 and 710 basis points in 2019.

As Jeremiah will discuss shortly, we have navigated the pandemic well and have taken the right steps to further build and scale our platform to be able to generate operating leverage over the long term. All Risks and Ryan Specialty are truly working as one company. The transition and cultural fit continue to exceed our expectations. We successfully completed our initial public offering in July. And it's been wonderful to welcome those of you on the phone today to the Ryan Specialty story.

Lastly, our team is stronger than ever. As we finished 2021, we maintained our 97% producer retention rate, which speaks to the winning culture we have developed at Ryan Specialty. We have created a true destination of choice for the top talent in the industry, and we're just getting started. Here in the fourth quarter, we were pleased to complete two highly strategic acquisitions, Crouse and Associates, and Keystone Risk Partners. Combined, these two acquisitions generated approximately $34 million in additional revenue for the trailing 12 months prior to the acquisition.

Crouse represents a leader in transportation and specialty wholesale brokerage. It's located on the West Coast [ph] progress wise in all 50 states, expands (05:48) the breadth of our transportation offering and enhances our ability to compete for the most complex accounts, with solutions ranging from traditional open market wholesale brokerage to niche binding authorities. Keystone represents our entrance into a natural adjacency, covering the alternative risk space, which you'll hear Tim touch on in his remarks. Keystone is an acquisition I'm particularly excited about, as it will expand our ability to serve brokers, agents and carriers by leading with innovation and offering alternatives to more traditional insurance placements.

We closed out 2021 on a high note. As we progress through 2022, here's what you should expect to see from Ryan Specialty. First, we expect to keep growing. The complexity of risks continues to increase and as a result, the E&S market continues to expand faster than the admitted market, which we believe puts the opportunity to sustainably grow our business firmly within reach.

In addition, pricing in E&S market remains firm. But even with moderation in rates, our model is built to succeed in any pricing environment. Along those lines in 2022, we also expect to strengthen our business to position us to generate sustainable growth for years to come. And that means prudently investing more in each of our three specialties.

In particular, that means both investing in our existing talent base and constantly bringing in new talent. We expect to onboard our largest broker class ever in 2022 and currently see incredible opportunities in the marketplace to hire additional experienced talent and fortify our position as an industry leader.

Further, this rapidly evolving capital landscape provides many unique opportunities for innovative platforms like Ryan Specialty, who enjoy broad capital support and robust distribution network. We plan to leverage one of our core strategies, de novo programs in MGAs, MGUs, as we're well positioned to combine the underwriting expertise and distribution capabilities with carrier appetite for profitable growth and new lines of business, including the transition of admitted lines portfolios to the E&S market.

[ph] None of (08:38) these opportunities are spurred by the dislocation of underwriting talent. And we are in a unique position to capitalize on this dislocation, as we've created a destination of choice for skilled underwriters and brokers. This core competency complements our M&A strategy. And in environments where available M&A targets don't meet our selective criteria of being both strategic and accretive, we believe we still have very exciting high growth opportunities to augment the organic growth of our existing business.

As you know, a hard market leads to increased competition, particularly in managed underwriting. Our competition comes from MGUs, as well as carriers looking to opportunistically enter or expand certain lines since we act as a delegate for insurers. Creating de novos, which comprise nearly half of our MGU offerings, as well as adding experienced talent, remain integral to our success, especially now as new entrants in managed underwriting intensify the battle for specialty underwriters and market share.

To that point, we are working on launching three de novo MGUs, supported by highly rated carriers. We're in the process of finalizing the definitive agreements necessary to start underwriting business. I hope to be able to share more detail with you on our next call. These investments are among the highest return investments that we can make.

Finally, our deep M&A expertise should enable us to act quickly and prudently when we see an opportunity to add to our robust platform, which will help enhance our future organic growth capabilities. And we're looking for A+ players who can leverage our platform to enhance their own growth profile.

We maintain active dialogue with a number of potential partners, including several proprietary conversations. As we mentioned before, we don't set dollar spend targets for M&A. We will continue to be as disciplined now as a public company, as we were when private, to help ensure that each acquisition is both accretive to our strategy and to our shareholder returns. Equally important, we will never compromise on our culture.

In summary, 2021 was a banner year for Ryan Specialty, which is a testament to our business model and the entire team rowing in the same direction, executing day in and day out for our clients and trading partners. We have a winning culture that empowers the best team in the specialty insurance industry, and that is reflected in our performance for the year and remain excited for the future growth of our firm and our ability to continue to deliver long-term value for our shareholders.

With that, I would now like to turn the call over to our President, Tim Turner. Tim?

Timothy W. Turner

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

Thank you very much, Pat. And as Pat highlighted, it was another excellent quarter and a fantastic year at Ryan Specialty and we are hard at work on making 2022 another successful year. It's an incredibly challenging environment for many insurers and carriers. We believe we're uniquely positioned to help our clients navigate a very dynamic risk landscape.

Our Wholesale Brokerage specialty continued to experience solid growth across all property and casualty lines of business, especially in our professional liability lines, driven by our continued strong performance in this prolonged hard market and the increasing flow of business into the E&S channel. We are also excited about the addition of our new teammates from Crouse and Associates who will integrate into our transportation practice group and national Binding Authority platform.

Our transportation team had been working diligently to create new products for our trading partners. And the addition of Crouse's team on the West Coast will be a significant complement to these efforts and further fill in our national transportation footprint. This allows us to be even more competitive for the largest national transportation accounts and to provide staying power for this critical line of business.

At our Binding Authority specialty, we continue to see strong growth within our small commercial lines of business. As Pat mentioned, we have a fantastic opportunity to participate in the consolidation of the highly fragmented delegated authority market [ph] where we did (13:48) with the Crouse acquisition on our path toward building the first truly 50-state binding authority operation. We believe we are attracting the best talent and positioning ourselves well, so that we're able to strike when the right opportunities arise.

Meanwhile, our Underwriting Management specialty completed a solid quarter and an exceptional year, growing total revenue 46% from 2020. It's important to remember for this specialty that carriers entrust their underwriting authority to us. Growth must be balanced with delivering underwriting profit back to our trading partners, and we are constantly reacting to market pricing and competitive dynamics. Underwriting performance and carrier relationships are measured in years, not in quarters.

As Lloyd's has pulled back in the market, we've had the good fortune of replacing it with large US, Bermuda and European insurers and reinsurers to fill the gap. We've been expanding our capacity with even better financed individual carrier units, putting our platform in an even stronger position than prior years. Underwriting Management has been proactively investing in specific initiatives to drive sustainable long-term growth and arranging incremental underwriting capital to further strengthen our operations.

In addition, onboarding experienced talent and market leaders is always critical to remaining an industry leader, and even more so when a prolonged hard market attracts new entrants. To that end, we have hired several industry leaders to launching excess casualty MGU and, as Pat referenced, are in the final stages of securing capital.

The rate environment remains full of opportunities within this product line. Finally, we're seeing solid progress with our UK-based D&O specialist StartPoint, as they ramp up their US branch. With recent key hires, the US team is coming together well and we are securing capacity for its entry into the US distribution system.

Along with the progress we are making at our three specialties, our M&A pipeline remains robust, including potential opportunities for our new employee benefit specialty. As we've noted before, today's acquisition is tomorrow's organic growth and we look forward to partnering with successful specialty firms that are aligned with our goals, culture, values and expectations for organic growth.

A great example of this is our recent acquisition of Keystone, which allows us to facilitate access to alternative capital. This transaction is exciting for several reasons. It enhances our mission to provide innovative solutions for brokers, agents and carriers, and it represents a significant growth opportunity as alternative risk capital is a natural home for some E&S risks.

Together with the talented team from Keystone, we will be able to develop entirely new insurance products when and where we see a need in the market. I'm pleased to report that we've already created one such product with more in the pipeline. That's exactly what we're trying to do with our M&A strategy, add talent and capabilities to our business that can use differentiated platform and trading partner relationships to immediately drive growth, while better serving our clients.

We also continue to aggressively recruit new talent. As Pat mentioned, we are expecting our largest broker class ever in 2022. And in addition, we anticipate a record matriculation at Ryan Specialty University later this year as well. Because we have a university and formalize training program for new graduates as well as a sizable internship program, we're able to recruit top-level graduates from risk management programs from across the country. Our ability to continue to add the best specialized talent to our already world-class producer team will enable us to keep growing our business well into the future.

In terms of the E&S market, while we are seeing early signs of additional competition entering on the fringes as they become more comfortable with the environment and their balance sheets, flow remains steady thus far in 2022. As we've noted, we expect that the increasing flow of business into the non-admitted market will continue to be one of the most significant drivers of Ryan Specialty's growth. Coupling this market segment growth with our industry leading talent and culture position, Ryan Specialty is very well positioned for the coming year. We are excited for 2022 and we will continue to press our competitive advantages to grow our business.

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

Jeremiah R. Bickham

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

Thank you, Tim. Let's get straight to the financial results. In Q4, we grew total revenue 16% period-over-period to $379 million. Our top line increase was driven by continued strong organic revenue growth of 15.4% for the quarter, attributable to a combination of new client wins and expanding relationships with existing clients.

We are very pleased to have performed so well in Q4 2021, especially considering we were comping against 21.8% organic revenue growth in the fourth quarter of 2020. As we noted on our prior call, the Q4 2020 comp was challenging in part because of a large balance of pandemic deferred business like M&A and construction risk, which wasn't expected to repeat in Q4 of 2021.

Total operating expenses for the fourth quarter were $323 million, a 16% increase year-over-year. Net income for the fourth quarter of 2021 was $30 million, or $0.09 per diluted share. Adjusted net income for the quarter, which excludes IPO-related and other unusual expenses, increased 24% period-over-period to $77 million.

Adjusted EBITDAC for the fourth quarter grew 18% period-over-period to $120 million, while adjusted EBITDAC margin rose 70 basis points to 31.8% for the quarter. Primary drivers of these increases were our revenue growth leading to scale in adjusted comp and benefits, as well as the continued realization of cost savings from our restructuring plan, which we initiated in 2020. This was partially offset by the realization of public company costs incurred in Q4, which will also generate a drag to adjusted EBITDAC margin when comparing quarterly margins year-over-year in Q1 and Q2 of 2022, as we did not yet have these costs included in the comparable periods in 2021.

As we think about adjusted EBITDAC margin for the full year of 2022, with Omicron receding, we welcome a return to a more normalized pre-pandemic level of T&E expense as we experience a broader return to in-person meetings and events. We will also have a full year of public company costs in 2022. And most importantly, we will continue to invest in the long-term growth of our business. In particular, the current environment offers us a unique and very exciting opportunity to hire A+ level underwriters and brokers, as Pat and Tim have both highlighted, and we expect to capitalize on this opportunity to pursue and onboard top talent to our platform.

With that said, I do want to highlight a crucial takeaway and provide some important context for 2022 in terms of adjusted EBITDAC margin. In 2019, which was the last full year prior to the pandemic, we generated adjusted EBITDAC margin of 25.0% as a private company.

Now, in 2020 and 2021, we certainly benefited from reduced levels of T&E spend. But even as that normalizes in 2022 and we record a full year of public company costs, we still expect to generate adjusted EBITDAC margins well above what we recorded in 2019. This is a clear testament to the scalability of the platform that we've built here at Ryan Specialty, and we are very proud of everything we've accomplished over the last several years. And as I've noted, over the long term, we expect that our growth will yield additional and sustainable operating leverage in the form of adjusted EBITDAC margin.

Finally, we reported adjusted diluted EPS of $0.29 for the quarter and believe that adjusted diluted EPS provides a more comparable period-over-period measure of our operating performance. Please refer to the earnings release and 10-K for further discussion of the components of adjusted diluted EPS.

Also, we are initiating our full 2022 outlook for organic revenue growth and adjusted EBITDAC margin as follows. We are guiding organic revenue growth rate for the full year 2022 to be between 13% and 15%. As a reminder, with our exceptional growth in 2021 and now that All Risks is part of the full year organic growth rate calculation, our organic growth comps are more challenging giving the significantly higher revenue base.

Further, we are in the prolonged stages of a very hard market and increased flow into the E&S market. And as such, we want to be prudent with our outlook, given what Tim noted earlier regarding the additional competitors beginning to enter the market. Thus, our forecast assumes that current conditions, which Tim and Pat have both noted, are still very conducive to growth at this moment, do gradually soften and decelerate somewhat during 2022.

Adjusted EBITDAC margin for the full year, we are guiding to be between 28.0% and 30.0%. We are investing heavily in talent and growth in 2022 to best serve our clients over the long term, which could impact margins in the near term. That said, if you compare this range to our 2021 result on a like-for-like basis in terms of T&E spend and public company costs, our forecast actually represents a healthy amount of operating leverage, especially when you consider the current human capital environment and the large potential long-term investment opportunities that we have in front of us.

As a reminder as well, Q1 and Q3 are our lightest quarters from an adjusted EBITDAC margin perspective and typically fall below our margin for the full year. Q2 and Q4 are typically our highest adjusted EBITDAC margin quarters, and Q1 tends to generally be our lowest margin quarter overall. As an example, in 2020, we printed 22.1% in Q1 and 28.8% for the full year. As Pat noted, it was a truly banner year for Ryan Specialty and we are very excited about another year of exceptional growth ahead of us.

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

QUESTION AND ANSWER SECTION

Operator: Thank you. At this time, we will be conducting a question-and-answer session. [Operator Instructions] Our first question comes 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 is on the organic revenue outlook. So, as we think about the 13% to 15% for this coming year, can you help us think about the seasonality there? Just given the Q2 and the Q3 of 2021 were your strongest quarters, should we think about the Q1 and the Q4 benefiting from easier comps? Just can you help us think about how you expect the organic to progress as we move through the year?

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

A

Yes. Elyse, well, so we'll stop short of giving actual revenue guidance on a quarterly basis. But you are correct, Q2 and Q4 are typically the largest quarters from a seasonality perspective. Q1 and Q3 are typically the lightest. And remember that margin typically follows those trends as well.

Elyse Greenspan
Analyst, Wells Fargo Securities LLC

Q

And then can you disclose how All Risks performed from an organic perspective in the fourth quarter of 2021?

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

A

That would be below the level of materiality that we disclose. But we can say, as we said on our Q3 call, we're really excited about the integration progress about how RT and the former All Risks folks are working really as one company. And we're really excited about having them in the organic revenue calculation because they are contributing mightily.

Elyse Greenspan
Analyst, Wells Fargo Securities LLC

Q

Okay. And then one last one on the M&A side, you guys seem pretty bullish, describing the pipeline as robust. Any color you can give us on the size of deals in the pipeline as you think out over 2022 and even beyond?

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

A

Yes. The size varies, obviously. There are some moderate sized, a few smaller, but very strategic. At the moment, we're not really in discussions and don't expect to be with mega deals like All Risks. But we're staying pretty much within the average of the past without All Risks, and I think that will continue.

Elyse Greenspan
Analyst, Wells Fargo Securities LLC

Q

Okay, thanks for the color.

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

Tracy Benguigui
Analyst, Barclays Capital, Inc.

Q

Thank you. Can we discuss your $400 million debt raise in January? I realize the use of proceeds is for general corporate purposes. But would it be fair to assume a good portion of those use of proceeds can be used for M&A?

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

A

Tracy, that's a correct assumption. I mean, as you have probably seen from looking at the earnings release, we have ample liquidity and we actually didn't specifically need the cash from the bond raise in January, but we saw an opportunity and we were proactive. And we're really glad that we were proactive given where the market is now. The plan is still for excess capital to be deployed to fund internal growth, but mostly M&A. And we are still planning to generally operate in the 3 to 4 times net leverage category.

Tracy Benguigui
Analyst, Barclays Capital, Inc.

Q

Okay, great. You provide some really good color regarding your EBITDAC margin guide. I'm just wondering, you also discussed your larger broker class of 2022 also trying to think about your latest acquisitions. So, to what extent do you think the comp structure may be playing into your EBITDAC margin guide?

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

A

The comp structure of the legacy business of acquisitions or of the new hires?

Tracy Benguigui
Analyst, Barclays Capital, Inc.

Q

Everything. Any color you could provide, how it should all come together?

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

A

Well, so that's an important – I mean, let's just talk about the labor market and wage inflation because I think that's part of your question. So, our margin range does contemplate the current labor market. But keep in mind, Tracy, most of our comp is related to producers who are actually paid a commission, which is based on the percentage of revenue they generate. So, wage inflation doesn't really affect them the same way that it does salaried employees.

And fortunately, even in this environment, we offer not just competitive pay, but also a unique culture and unique long-term professional development opportunities. So, we feel really good about our ability to remain a destination of choice in this environment.

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

A

Well, you asked about all of the above. And I'd like to add to Jeremiah's very appropriate comments that we mentioned that we are looking for A+ players as underwriters and as brokers. A+ players as underwriters and brokers can make a lot of money. But business follows to them quickly and we've built our business on attracting and developing A+ players and there's a unique period of time right now that we feel that it's a very opportune time to be looking for that kind of talent and we are doing that.

Tracy Benguigui
Analyst, Barclays Capital, Inc.

Q

Thank you.

Operator: Our next question comes from the line of Mike Zaremski with Wolfe Research. Please proceed with your question. Mr. Zaremski, please proceed with your question.

Mike Zaremski
Analyst, Wolfe Research LLC

Q

Sorry, I was on mute. Thanks. So, maybe first question, in the prepared remarks and in the guide, you mentioned a moderation in rates which – I think there's different camps of thought on the rate outlook. Some kind of feel like there's stability. Some feels like there could be an uplift due to the current macro backdrop, and some feel like there's likely deceleration. Clearly, it sounds like you're in the deceleration camp. But maybe any color on what you're seeing so far year-to-date or just kind of what's driving that outlook.

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

A

Well, we certainly see some modest rate deceleration in certain product lines and some real early signs and stages of standard markets writing some high excess layers of D&O and excess casualty placements taking them back. But we continue to operate in a very hard market space. The conditions in the market firm almost every month.

We just received January surplus lines stamping results from WSIA, and that flow is up over 20% once again. So, the flow into the channel is a better gauge for us in terms of the market share in the commercial P&C market that's available to us. And again, that continues to grow. We continue to capture more of it and there's no sign of the hard market letting up.

Jeremiah R. Bickham A

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

So, Mike, it's a consistent theme for us. We like to forecast prudently and we're trying to draw on the five cycles that Pat's lived through, the three or three plus that Tim has lived through. It's subtle, but I tried to touch on it in my prepared remarks. We are seeing the very early signs. They're really not detectable in the numbers right now and we're not saying we know how far or how fast they will progress, but those very early signs just reinforce our view that it's prudent to predict moderation during the year.

Patrick G. Ryan A

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

There's another factor that needs to be considered and that's the war. And we can get into that broader discussion a little bit later, if you'd like. But with the war, that introduces a lot more risk into the world and you've watched what's going on in Russia with the nationalization and so on. So, all kinds of new risks coming in that the insurance industry has to cope with.

Mike Zaremski Q

Analyst, Wolfe Research LLC

Yeah. And that's it. And maybe we can dig into that, unpack this unfortunate situation. I mean, are there cycles we can look at where we can say this is the impact, the insurance cycle or demand post previous [ph] altered (35:40) wars, or is there any color how you guys are thinking about how this could change the marketplace?

Patrick G. Ryan A

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

Well, I was talking with a friend of mine, the CEO of an insurance carrier, who's been in this position three-plus years, and he said, I think I'm a jinx. Climate started to hit really hard three-plus years ago, social inflation hit, then we got a pandemic, and now we got a war. There's no history – there's no precedent on that. It's never occurred in the history of this country in terms of insurance coverages.

Jeremiah R. Bickham A

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

Correct. And, Mike, just to be clear, too, we're not saying we have – we actually have no direct revenue exposure to Russia or Ukraine. It's more of a statement that we live in a global economy, and the whole world is impacted by geopolitical events like this.

Mike Zaremski (

Analyst, Wolfe Research LLC

Understood. Maybe one follow-up separately, so just on the leverage levels, we can see where your pro forma leverage level is now. We know roughly what the cash generation of the company is. Should we be thinking that you'll have runway to deploy the debt raise, plus free cash flow kind of over the next year or so? And also just is there a – when we think about the acquisitions you're making, is there – should we be thinking they're usually kind of margin-neutral, or is there no common – is there no just way to think about that as they're all going to be different?

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

A

They are all going to be different. But I would say that, for modeling purposes, Mike, just assume margin-neutral. As we start to actually close on benefits businesses, wholesale benefits businesses at some point, those often do have a little bit of a different margin profile to our legacy wholesale businesses. And we can give more color on that as time progresses.

But the answer to the first part of your question is, yes, we think that given the robust market and our robust pipeline, that's why I said earlier that the excess liquidity we have on our balance sheet is earmarked for M&A. I don't want to put a timetable on that because I think that creates the wrong incentives. But we are hopeful that there are ample opportunities out there that meet our highly selective criteria of being strategic and accretive that – and we're hoping we can talk to you about those very soon.

Mike Zaremski
Analyst, Wolfe Research LLC

Q

Thank you very much for the color.

Operator: Our next question comes from the line of Alex Scott with Goldman Sachs. Please proceed with your question.

Alex Scott
Analyst, Goldman Sachs

Q

Hey. Good afternoon. First one I had for you is just on the growth outlook for 2022. I was wondering if you could maybe even just qualitatively discuss sort of how Wholesale Brokerage, Binding Authority, and Underwriting Management play into the growth outlook that you've provided.

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

A

So, we won't give – we give guidance at the segment level, we're one segment, so consolidated. You may have noticed in some of Pat's prepared remarks, the current environment is favorable overall for E&S specialists like us, but the competitive dynamics are a little bit different, for example, for a wholesale broker like RT versus an underwriting manager.

There's also differences that I'm sure you're aware of in terms of a delegated authority underwriter has to be mindful of the capital providers' balance sheet. So, growth has to be balanced with an underwriting profit. And so, that does has an impact on the growth prospects. But we've said before that all of our – all three specialties are robust contributors to the aggregate organic growth percentage, and they're all currently, in some way or another, benefiting from the favorable market conditions that Tim said at this moment are still alive and well.

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

As you know, in the wholesale distribution market, there are far fewer competitors than there is in the underwriting business. Most of these lines have 20, 30, 40, sometimes less, sometimes 10 markets that are anxious to write the business. And we're a microcosm of that in that we represent those carriers.

So, if we're representing a carrier as an MGU, we're going up against other carriers who are dealing without an MGU and some carriers who are dealing with an MGU. So, there's just – I know you know this, but I'm maybe [ph] appreciative of the quarter (41:01). But it's important to understand that the competitive profile of the delegated authority against a wholesale broker and the different responsibility, the dual responsibility of [ph] carer (41:21) to capital provider and to client, client being retail broker or the wholesale broker has a duty of [ph] carer (41:28) to the retail broker.

Alex Scott
Analyst, Goldman Sachs
Q

Got it. Very helpful. A follow-up question sort of separate is just following up on the comments about the environment and just disruption from the conflict going on in Ukraine and in Russia. Are you starting to see that actually in pricing of specific lines? I mean, is it more isolated to maybe cyber policies or anywhere else you're seeing that start to actually make its way in in a tangible way to pricing?

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

Well, that's really a good question, and the answer is there's all kinds of factors that are driving prices up in cyber. And probably, all the global issues on hacking and the accusations that go back and forth has been affecting cyber. So, there's probably some cyber influence already from the geopolitical issues. Nationalization of airplane leases, that's not one that I don't think is in the marketplace at all, but will be quickly.

The inflation that is becoming more and more apparent in more people's minds, being driven by the war with supply chain issues and lots of other disruptions, I think those are just beginning to come into the market. So, I think that the war only being a few weeks old is obviously front of mind to everybody and then trying to sort out what it means.

So, I don't think you see much of it, maybe the cyber part, as you pointed out or probably nothing, but you can look at political risk, you can look at trade credit, you can look at D&O because corporations will get blamed – corporate leaders will get blamed for problems that come up. And so, ocean marine and cargo, but we don't have any managing underwriting business, very modest in ocean marine and cargo, [ph] a tremendous (43:54) piece. Now, in terms of Wholesale Brokerage, yes, we have that. But that's not the same kind of risk. When we're representing the carrier, we have to make sure that their appetite stays satisfied and gratified that we've given them profitable business.

Alex Scott
Analyst, Goldman Sachs
Q

Thanks for the responses.

Operator: Thank you. [Operator Instructions] Our next question comes from the line of Weston Bloomer with UBS. Please proceed with your question.

Weston Bloomer
Analyst, UBS

Q

Hi. Thanks for taking my question. And my first one is on the de novo formations that you talked about in the prepared remarks. I know you're not going to get any specifics on how material the impact may be, but is there any way you could quantify the typical – how that typically trends in a typical year or in 2021 or any additional color on the rationale in 2022 versus prior years ?

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

A

So, just to make – I'm going to repeat the question just to make sure I understand it. You're looking for any sort of color we can provide on, like, maybe the ramp-up to scale or to even just revenue for some of these de novo MGUs.

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

A

[ph] Currently (45:16).

Weston Bloomer
Analyst, UBS

Q

Exactly, yes. And maybe what impact was there in 2021 or prior years from other like de novo formations? How should we think about that in a typical year?

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

A

Well, the ramp up is unpredictable because we're assembling the capital. In some cases, we've hired the talent. In all cases or each of the cases, we have talent about to be hired. So, that's a timing issue. But then as the assembly of the capital, you need the front or the primary carrier, and then you need quota share participants on a subscription basis or quota share reinsurance. We're very experienced and professionally strong in supplying all of that. But it's a process and it's not instantaneous by any means. And so, we just can't forecast what the near-term ramp-up rate is.

But I would say this, they're in lines of business that the market needs or we wouldn't be doing it, and we're attracting talent that would be differentiating, I mean, half of the market. So, we're optimistic about the results. And near term slowly for the first few months and that accelerating, we can't forecast the acceleration. But in the past, as past being prologue, we've had excellent returns on our de novos and we've built some very sizable businesses on de novo with just getting the right talent and then getting the right amount of capital support.

The good news now is that we have all of what it takes to set up a de novo MGU in that we have access to the primary paper or the fronting paper. We have access to support of reinsurance and/or subscription to support very strong carriers. We have good infrastructure support. We have access to the retail brokers, and we just have to get the right talent and we're pretty good at that.

Weston Bloomer
Analyst, UBS

Q

Got it. Thank you. And then on free cash flow, is there any way you could provide additional color on how we should think about free cash flow conversion in 2022, either as a percentage of revenue or earnings? Or could you talk to what initiatives that you're taking to improve your free cash flow overall?

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

A

So, I just want to remind you of the way that we think is most instructive to calculate that. And the formula is starting with adjusted EBITDAC, then taking out interest expense, take out adjusted income tax expense and then CapEx. Under that formulation, if you track 2019, 2020, 2021, trending in the right direction, we expect 2022 to be a continuation of that trend as well.

Weston Bloomer
Analyst, UBS

Q

Got it. Thank you for the color.

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

Thanks very much. Both Pat and I want to say, Tim, mentioned that this is a very good opportunity for recruiting. I was hoping we could dig into that a little bit. And the reason I'm asking is because we haven't seen, to the best of my knowledge, these really disruptive potential acquisitions that I thought would have been a great source of recruitment opportunity.

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

A

So, Meyer, you're looking for color from us on sort of maybe some of the underlying factors or conditions that lead to this opportunity for all these new hires we're talking about?

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

Q

Exactly.

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

A

Sure. I'll start it and Tim could pick up. With all the disruption in the marketplace with – well, all the disruption, there's been an entrepreneurial spirit sort of stimulated, and underwriters and brokers want to be a part of an organization that has a platform for broad growth opportunities. That's where our independence has been very important to us. And so, we have that.

They're also looking for a culture where they can have freedom of a real bureaucratic nature and that they see that with us, and frankly they're looking for reward for performance. These people, they're all paid on a performance. Even the underwriters are paid on performance just based on the growth of the business and the profitability for the underwriters. So, they're performance-driven. They're high achievers. And then, lastly, many of them are in companies where they don't have equity available. And you've seen the phenomenon of the roll-ups with PEs. That has stimulated people to think, well, maybe it's time for me to get some equity.

So, our going public frankly has helped attract people to our story they read about us not much more [ph] than this (51:12) when we were private. So, they know a lot more about us and they've seen that we performed well so that our stock has reflected that. And so, I think there's this greater interest in exploring things with us.

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

Q

Okay. Thank you. That was very helpful. And if I can follow up with a quick question, not with regard to guidance, but when we talk about the initial signs of increasing competition, is there one of the specialties – in other words, Wholesale versus Binding Authority or Underwriting Management, where that should manifest itself sooner?

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

A

Meyer, are you trying to figure out in terms of related to the prepared remarks, where we were most – where the competition comments are most relevant among the three specialties of Wholesale Binding versus underwriting managers?

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

Q

Yeah, that's right.

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

A

Okay. Well, it's definitely on the managing underwriting, because of the abundance of carriers, Meyer. As I know you know, many of these lines have 20 to 30 to 40 carriers. When you're a wholesale broker, you either get the order or you don't. And we get the order a great deal of the time. And managing underwriting at retail broker or a wholesale broker might well be getting three, four or five quotes.

And so, there's much more competition out there for that business. And then – and you've seen this, Meyer, that with rates escalating in certain lines and terms tightening, that's attracting more aggressive pursuit by carriers, but we're just a mirror image of what happens with the carrier because we represent these carriers.

Now, the good news is that we're all – we're very [ph] discreet (53:25) specialties and our differentiated talent has allowed us to be quite successful. But it's competitive. So, competition demands that you keep hiring higher quality and more quantity because the volume is so high. You have to have the large teams, underwriting teams to analysts. But you have to have the really expert underwriters and that was the process I described in the earlier question.

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

Q

Okay, excellent. Thank you so much.

Operator: Ladies and gentlemen, we have reached the end of the question-and-answer session. I will now turn the call back over to management for closing remarks.

Patrick G. Ryan

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

Okay, well, thank you, operator and thank you, ladies and gentlemen. Thanks for your continued interest and support of Ryan Specialty. We value that very highly. We look forward to speaking with you again when we discuss our first quarter 2022 results. Thank you and have a good evening.

Operator: This concludes today's conference and you may disconnect your lines at this time. Thank you for your participation and have a wonderful day.