

Goosehead Insurance, Inc. (GSHD)

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Domestic Financials

Goosehead Insurance (NASDAQ: GSHD) is an independent insurance agency offering personal lines of insurance through more than 145 carriers. The company's share of total written premiums includes Homeowners (56.7%), Automotive (39.6%), Commercial (2.5%), and Other (1.1%). Revenue is generated through Goosehead's Corporate Channel (55.6%), consisting of company-owned and financed operations with employees who are hired and trained by the firm. Other revenues are generated by its Franchise Channel (44.4%), including operations that are owned and managed by franchisees. The company was founded in 2003 by CEO Mark Jones and his wife, Robyn Jones, and went public in 2018. Goosehead is headquartered in Westlake, TX.

Price (3/19/22) (\$):	80.30	Beta:	1.10	FY: Dec	2021A	2022E	2023E	2024E
Price Target (\$):	118.61	WACC (%):	10.99%	Revenue:	151,312	204,564	268,385	345,746
52WK H-L (\$):	\$62.40 - 181.30	M-Term Rev. Gr Rate Est (%):	29.24%	Growth (%):	29.3%	35.2%	31.2%	28.8%
Market Cap (Mil):	\$3,058	M-Term EPS Gr Rate Est (%):	45.33%	Op. Income:	20,838	38,172	52,052	72,260
Insider Holding (%):	53.80	Debt/Equity:	3.9%	Growth (%):	(25.1%)	83.2%	36.4%	38.8%
Avg. Daily Vol (3M):	188,111	Net Debt/EBITDA (TTM):	4.31	Operating Margin (%):	13.8%	18.7%	19.4%	20.9%
Short Interest (%):	6.50%	ROA '21:	4.8%	EPS (ex. Equity Comp)	\$0.48	\$0.93	\$1.22	\$1.52
Yield (%):	0.00	ROE '21:	-59.2%	P/E (Cal):	166.0	86.6	66.0	52.7
ESG Rating:	BB	ROIC '21:	27.1%	EV/EBITDA (Cal):	142.5	77.8	57.0	41.1

M-Term: '22 - '26

(\$USD '000)

Recommendation

Goosehead Insurance has generated highly predictable, recurring revenue since its founding in 2003, evidenced by its 10-year Total Written Premium (TWP) CAGR of 40% with a retention rate of 93%. In 2003, Robyn Jones was struggling to find an insurance provider that she felt was knowledgeable and cared about her real estate business. Mark and Robyn understood the importance of service quality and built an insurance agency with an impressive Net Promoter Score (customer loyalty and satisfaction measurement) more than 2.5x the insurance industry average. There are principally three types of businesses that sell personal lines insurance products. Direct Distribution (20% market share) is where insurance carriers market their products directly to customers (i.e., Geico, Progressive). Captive Agencies (44% market share) sell products for only one carrier, earning revenue through sales commissions based on premiums placed on behalf of clients. Goosehead Insurance operates as an Independent Agency (36% market share), leveraging multiple carrier relationships to offer its clients an array of insurance products at the most competitive prices. GSHD offers a unique value proposition to prospective agents and those seeking to move their book of business out of the captive structure. Through its Franchise Channel, Goosehead separates the sales function from the service function, enabling agents to focus on building their book while the company focuses its service personnel on delivering superior client service. Franchisees are given access to GSHD's 145+ carrier relationships; process, training, and implementation systems; and a back-office support team to place insurance in exchange for an initial franchise fee (20% of new policies) and royalty fees (50% renewal policies). This relationship has allowed franchisees, tenured three years or more, to build their book of business over 70% faster than the industry's average personal lines agent. Because of industry tailwinds, new client referral initiatives, and latent margin expansion, it is recommended that GSHD be added to the AIM Small Cap Fund with a price target of \$118.61, representing an upside of 47.7%.

Investment Thesis

- Ear to the Industry.** Many InsurTech companies attempt to “disrupt” the insurance industry by bringing to market online purchase channels that underwrite and offer claims in a matter of minutes. Although convenient, these start-ups fail to realize that most individuals prefer to take the extra time to speak with a trusted agent, outsourcing the responsibility of finding the most appropriate claim, which is evidenced by a historically consistent ~80% of total premiums sold by agents. GSHD also recognized that the average age of insurance agent principals is 55, where nine in ten agencies have a perpetuation plan, and four in ten anticipate some ownership change in the next five years. To combat this trend, the company's average corporate agent age is 26. Goosehead is aptly positioned to gain from displaced clients and avoid the shrinking workforce challenges faced

by many competitors as their corporate agents can build longer-term relationships. The benefit of age, coupled with the company's separation of sales and service functions, has allowed corporate agents, tenured three years or more, to generate 2.9x as much new business production per agent as the industry best practice. For these reasons, new business commissions (corporate revenue) are forecasted to increase at 15% in FY '22 and grow at a decreasing rate of 100 bps thereafter.

- **Client Referral Initiatives.** Few companies can grow at a 45% annual rate on virtually no advertising. With customer acquisition costs in the Property and Casualty (P&C) industry sitting well over \$1,000 per customer, management has made it clear GSHD is not competing in this space. What they are focusing on is leveraging their referral network to bring the best product and customer experience to market. With a customer satisfaction score (NPS) of 91, yet only one-third of new business currently generated from referrals, management recognizes GSHD's pain points in its referral efficacy and cross-selling strategies. By budgeting \$2 million for marketing in 2022, GSHD looks to improve in these areas via "possible partnership opportunities" and other digital marketing strategies. Ann Challis is a newly hired CMO with prior experience leading marketing teams at BlackRock, Wells Fargo, and other FinTechs. To account for this growth, new business royalty fees (franchise revenue) are forecasted based on recruiting agent productivity. Despite high conviction that new leadership and marketing dollars will make the recruiting agent's job superfluous, quarterly net adds per agent were conservatively estimated at 1.5x (historically ~1.8x) and decreased as a function of time at -0.07x per year.
- **Latent Margin Expansion.** Goosehead's moat expands as its business grows. Carriers are drawn to GSHD's ability to maintain strong premium growth with a dedicated service team committed to retaining premiums above 90%. As Goosehead continues to prove its ability to expand new business at high retention rates, carrier relationships will expand, allowing the company to offer an even broader array of products at even more competitive prices. Presently, GSHD invests through its P&L to drive growth through SG&A and R&D expenses. Since employee compensation grows as a function of employee growth, this expense cannot sustain historical growth levels as total employee growth plateaus. A similar relationship exists with G&A expenses. To err on the side of conservatism, employee compensation and G&A expenses are both modeled on a per-employee basis, increasing as a function of time per employee but decreasing as a percentage of total growth YoY after FY '24. Revenue growth, driven by an increase in carrier quantity, less diminishing operating expenses, allows EBITDA margins to grow at a ~11% CAGR for the next ten years.

Valuation

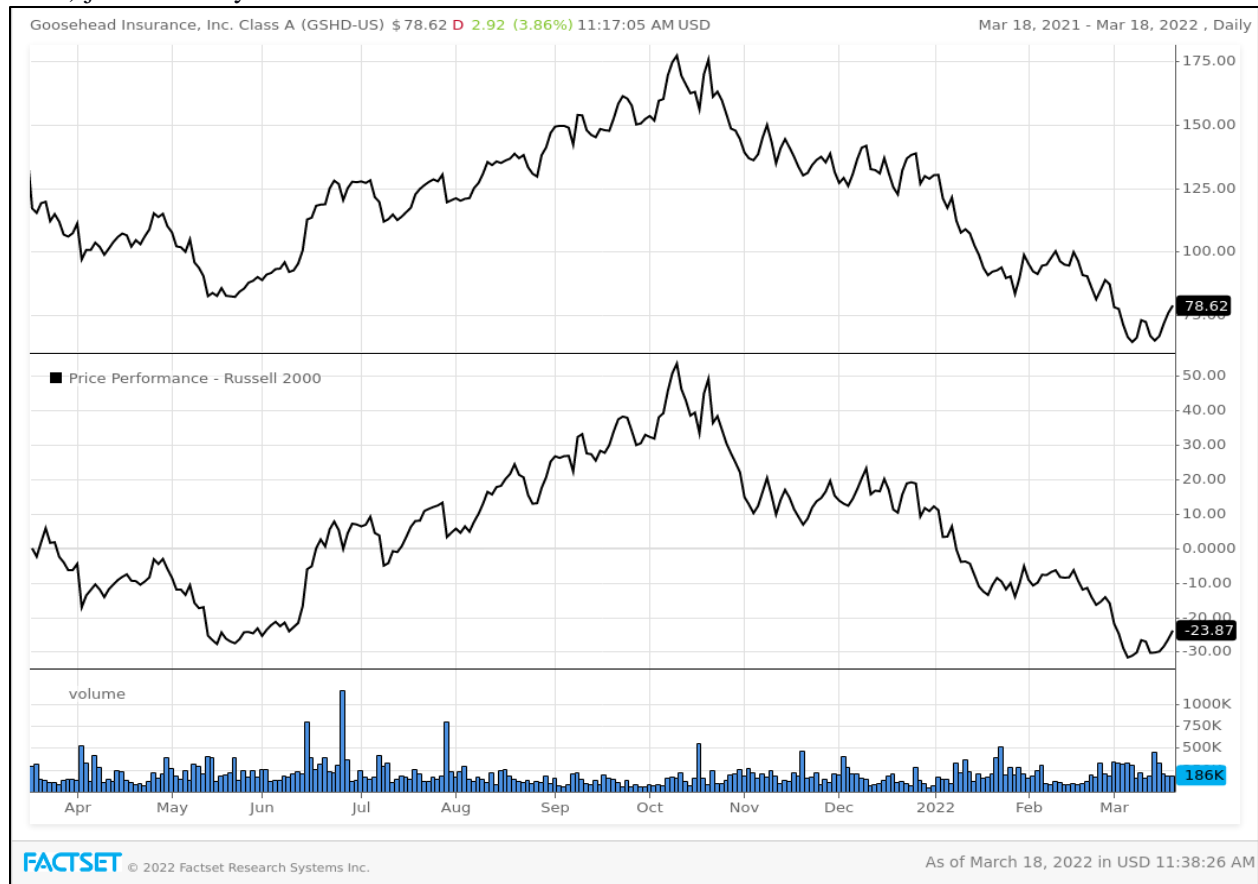
To reach an intrinsic value for GSHD, a 10-year DCF model was created. Using a terminal growth rate of 1.82% and a WACC of 10.99%, an intrinsic value of \$139.40 was reached. A sensitivity analysis of the terminal growth rate (+/- 25 bps) and WACC (+/- 50 bps) ranged from \$130.34 to \$149.84. Additionally, an NTM P/E multiple was calculated using a weighted average peer multiple of 54.5x, resulting in a relative valuation of \$50.50. An EV/Revenue/Employee multiple was calculated using a weighted average peer multiple of 24.7x, resulting in a relative valuation of \$78.26. Finally, an EV/EBITDA was calculated using a weighted average peer multiple of 144.6x and a relative valuation of \$81.52. By weighing these models 70/10/10/10, a price target of \$118.61 was reached, representing a 47.7% upside. GSHD does not pay a dividend.

Risks

- **Insider Selling.** In 2018, GSHD went public with a 65% non-controlling interest in the operating entity, GSHD, LLC. Founders Mark and Robyn Jones have since diminished this NCI to ~50%.
- **Emerging Purchase Channels.** An independent study found that 35% of agencies believe direct distribution of P&C will have a significant impact on their agency in the next two years. A shift away from agent sales might force GSHD to engage in the absurdly high CAC of P&C customers.
- **Referral Productivity Regression.** Much of GSHD's value is, directly or indirectly, attributed to recruiting agent production. Any threat to productivity could materially impact this firm's FCF.

Management

Customer-centric Co-founder, Chairman, and CEO Mark Jones founded GSHD alongside Vice Chairman Robyn Jones in 2003. Three years later, the first of three Colby brothers joined the firm after spending several years at KPMG in Auditory Services. Michael Colby (President and COO) joined in 2006, Mark Colby (CFO) rejoined in 2012 after three years at Ernst & Young, and Matthew Colby (VP of Agency Sales) joined shortly thereafter.



Source: FactSet

Peer Valuation						
Company	Ticker	Market Cap (Mil)	Operating Margin	P/E NTM	EV/Rev/Employee	EV/EBITDA
Goosehead Insurance, Inc.	GSHD	\$3,058	10.6%	86.6x	25.3x	142.5x
BRP Group	BRP	\$2,949	8.1%	22.2x	25.5x	213.7x
Brown & Brown, Inc.	BRO	\$17,931	28.1%	27.9x	82.6x	18.8x
Green Dot Corporation	GDOT	\$1,506	3.4%	11.3x	0.6x	5.0x
Planet Fitness, Inc.	PLNT	\$7,881	24.0%	51.4x	23.6x	44.5x
RE/MAX Holdings	RMAX	\$557	11.0%	11.4x	0.9x	6.9x
Chegg	CHGG	\$4,291	10.1%	25.9x	9.5x	32.4x
GoHealth Inc.	GOCO	\$427	(9.7%)	187.8x	6.8x	488.4x
Peer Average			9.3%	54.5x	24.7x	144.6x

Peer Weights (%): 19, 19, 19, 8, 8, 8, 19

Source: FactSet

Peer Fundamentals						
Company	Ticker	Revenue (Mil)	ROIC (%)	ROE (%)	EBITDA Margin (%)	Net Profit Margin (%)
Goosehead Insurance, Inc.	GSHD	\$151	27.1%	-59.2%	13.8%	5.5%
BRP Group	BRP	\$567	8.2%	16.5%	3.2%	16.0%
Brown & Brown, Inc.	BRO	\$3,051	10.3%	15.3%	33.1%	20.3%
Green Dot Corporation	GDOT	\$1,388	11.7%	11.8%	10.3%	8.8%
Planet Fitness, Inc.	PLNT	\$587	7.0%	-10.6%	35.8%	12.7%
RE/MAX Holdings	RMAX	\$330	5.4%	-	25.4%	13.8%
Chegg	CHGG	\$776	7.1%	25.1%	18.5%	22.4%
GoHealth Inc.	GOCO	\$1,062	60.4%	-	1.1%	51.0%
Peer Average		\$1,109	15.7%	11.6%	18.2%	20.7%

Peers Unweighted

Source: FactSet (TTM)