Aon Plc (AON)

Updated November 19th, 2021, by Josh Arnold

Key Metrics

Current Price:	$295	**5 Year CAGR Estimate:**	5.7%	**Market Cap:**	$66 B
Fair Value Price:	$233	**5 Year Growth Estimate:**	10.0%	**Ex-Dividend Date:**	01/30/22[1]
% Fair Value:	127%	**5 Year Valuation Multiple Estimate:**	-4.6%	**Dividend Payment Date:**	02/15/22
Dividend Yield:	0.7%	**5 Year Price Target**	$375	**Years Of Dividend Growth:**	10
Dividend Risk Score:	C	**Retirement Suitability Score:**	F	**Last Dividend Increase:**	10.9%

Overview & Current Events

Aon is a professional services firm headquartered in London, United Kingdom. The company provides a variety of services including consulting, risk management, and health plan management. Aon has approximately 500 offices worldwide that serve 120 countries through a workforce that numbers about 50,000. U.S. investors can initiate an ownership stake in Aon through American Depository Receipts that trade with a market capitalization of $66 billion on the New York Stock Exchange, under the ticker AON. Aon should generate around $12 billion in revenue this year.

Aon reported third quarter earnings on October 29th, 2021, with results coming in ahead of expectations on both the top and bottom lines on an adjusted basis. Total revenue was up 13% year-over-year to $2.7 billion, which was driven by a 12% organic revenue increase, a 2% favorable impact from forex translation, and a -1% headwind from acquisitions and divestitures.

Total operating expenses were up 80% year-over-year to $3.5 billion, but that was due almost entirely to a $1.3 billion charge related to the terminated Willis Towers Watson transaction. Organic expenses were up 12% along with organic revenue, as well as some additional costs from forex and discretionary expenses.

Operating margin was down 30bps on an adjusted basis to 22.1% of revenue, including 240bps of negative impact from discretionary expenses. Earnings-per-share excluding the WTW transaction fee was up 14% to $1.74 in the third quarter. We've left our estimate of earnings-per-share for this year unchanged at $11.65.

The company repurchased 4.4 million shares during the quarter and had $3.7 billion left on its current authorization at the end of the quarter.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
EPS	$2.86	$2.99	$3.53	$4.66	$4.88	$5.16	$6.52	$8.16	$9.17	$9.81	***$11.65***	***$18.76***
DPS	$0.60	$0.62	$0.68	$0.92	$1.15	$1.29	$1.41	$1.56	$1.72	$1.78	***$2.04***	***$3.44***
Shares[2]	325	311	301	280	270	262	254	245	237	230	***225***	***205***

Between 2011 and 2020, Aon compounded its adjusted earnings-per-share at a rate of nearly 15% per year. Looking ahead, we believe that the company's growth is likely to continue to be quite strong, albeit a bit slower than its historical pace. More specifically, we are forecasting 10% annualized earnings growth over a full economic cycle.

Management continues to be bullish, and rightfully so, as Aon's businesses are posting very strong rates of growth across the board, for the most part. We see expense savings as a driver of earnings growth along with the buyback, and organic revenue growth should continue to move the top line higher as well. Given the broad assortment of professional services the company offers as well as its global footprint, we are bullish on Aon's future. We note forex translation has been a sizable headwind in the past, but Aon has thus far been able to overcome that, and then some.

[1] Estimated date

[2] Share count in millions

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The dividend should continue to rise at roughly the rate of earnings, and we forecast the payout to be at $3.44 in 2026, up from the current $2.04. Aon is not a high-yield stock by any means, but its dividend growth potential is strong.

Valuation Analysis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Avg. P/E	16.9	16.8	19.2	18.6	19.8	20.4	20.1	17.9	17.7	20.3	***25.3***	***20.0***
Avg. Yld.	1.2%	1.2%	1.0%	1.1%	1.2%	1.2%	1.1%	1.1%	0.9%	0.9%	***0.7%***	***0.9%***

Aon has traded at an average price-to-earnings ratio of ~19 over the last decade, and we are using 20 for a fair value estimate. The company is trading for a price-to-earnings ratio of 25.3 using our 2021 earnings-per-share estimate. That implies a headwind to total returns from the valuation, as Aon is trading above our estimate of fair value. We see the yield staying about where it is for the foreseeable future.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	21%	21%	19%	20%	24%	25%	22%	19%	19%	18%	***18%***	***18%***

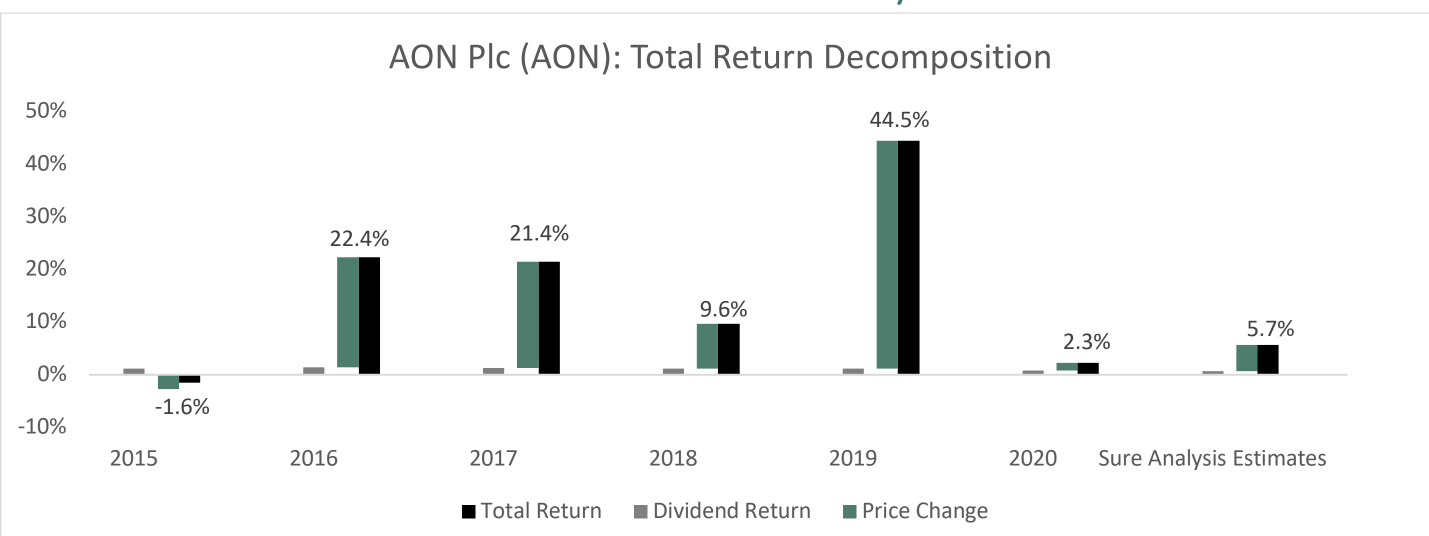
Aon's payout ratio is still very low, consistent with the company's historical practices, and we do not believe that will change. We see the dividend remaining around one-fifth of total earnings, so the payout is extremely safe. However, this means Aon is highly unlikely to have a meaningful yield anytime soon. Management has stated that it plans to protect the dividend during periods of uncertainty.

Aon was resilient during the Great Recession, and we expect that will be the case again, the product of its very diversified revenue streams. This is also a competitive advantage for the firm, along with its world-class client list and reputation.

Final Thoughts & Recommendation

We are forecasting 5.7% total annual returns, consisting of the 0.7% yield, 10% EPS growth, and a headwind from the valuation. We're reiterating the stock at a hold rating. Aon offers dividend growth potential, but also a long runway for earnings-per-share growth. The now-terminated merger with Willis Towers Watson – and the $1.3 billion cash payment Aon made in Q3 – are unfortunate, but do not impact the long-term outlook for Aon.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	11287	11514	11815	12045	9480	9409	9998	10770	11013	11,066
SG&A Exp.	3,124	3,209	3,199	3,065	1,951	1,765	2,039	2,354	2,226	5,161
D&A Exp.	582	655	635	594	338	319	891	769	564	46.6%
Operating Profit	1,596	1,596	1,671	1,966	1,587	1,811	1,065	1,544	2,169	1,967
Operating Margin	14.1%	13.9%	14.1%	16.3%	16.7%	19.2%	10.7%	14.3%	19.7%	413
Net Profit	979	993	1,113	1,397	1,385	1,396	1,226	1,134	1,532	2,781
Net Margin	8.7%	8.6%	9.4%	11.6%	14.6%	14.8%	12.3%	10.5%	13.9%	25.1%
Free Cash Flow	777	1,150	1,524	1,556	1,809	2,170	551	1,446	1,610	1,969
Income Tax	378	360	390	334	175	148	250	146	297	17.8%

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets	29,552	30,486	30,251	29,772	26,883	26,615	26,088	26,422	29,405	32,106
Cash & Equivalents	272	291	477	374	384	426	756	656	790	884
Acc. Receivable	3,183	3,101	2,896	2,815	2,564	2,106	2,478	2,760	3,112	3,070
Goodwill & Int.	12,046	11,918	11,575	11,380	10,628	9,300	10,091	9,320	8,948	9,306
Total Liabilities	21,432	22,681	22,056	23,141	20,824	21,083	21,440	22,203	25,956	28,523
Accounts Payable	1,832	1,853	1,931	1,805	1,772	1,604	1,961	1,943	1,939	---
Long-Term Debt	4,492	4,165	4,389	5,582	5,700	6,205	5,966	6,244	7,339	7,729
Total Equity	8,078	7,762	8,145	6,571	6,002	5,475	4,583	4,151	3,375	3,495
D/E Ratio	0.56	0.54	0.54	0.85	0.95	1.13	1.30	1.50	2.17	2.21

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	3.3%	3.3%	3.7%	4.7%	4.9%	5.2%	4.7%	4.3%	5.5%	6.4%
Return on Equity	12.0%	12.5%	14.0%	19.0%	22.0%	24.3%	24.4%	26.0%	40.7%	57.3%
ROIC	7.7%	8.1%	9.1%	11.3%	11.6%	11.9%	11.0%	10.8%	14.4%	17.8%
Shares Out.	325	311	301	280	270	262	254	245	237	230
Revenue/Share	33.11	34.62	37.46	40.20	33.40	34.81	38.35	43.60	45.77	47.47
FCF/Share	2.28	3.46	4.83	5.19	6.37	8.03	2.11	5.85	6.69	11.33

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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