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May 05, 2020

Aon plc (AON)

$177.68 (As of 05/04/20)

Price Target (6-12 Months): **$187.00**

Long Term: 6-12 Months	**Zacks Recommendation:** (Since: 01/01/19) Prior Recommendation: Outperform	Neutral
Short Term: 1-3 Months	**Zacks Rank:** (1-5)	**3-Hold**
	Zacks Style Scores:	VGM:D
	Value: D | Growth: C | Momentum: D	

Summary

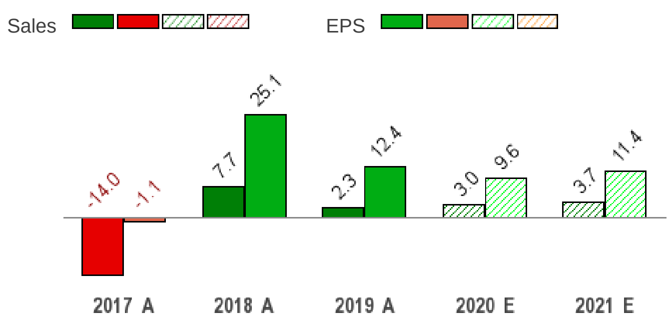
Aon's first-quarter 2020 operating earnings of $3.68 per share missed the Zacks Consensus Estimate by 0.5%. However, the metric improved 11.2% year over year on higher revenues and strong segmental contributions. Its bottom-line has been growing over the past few years on the back of buyouts and collaborations. Its position in the evolving commercial insurance market for small and medium-sized businesses also impresses. It has been divesting its non-core operations to streamline its business. It has also taken up restructuring initiative to reduce workforce and rationalize technology. The company's shares have outperformed the industry in a year's time. However, its rising debt bothers. Its geographically diversified operations expose it to forex fluctuations.

Price, Consensus & Surprise

Data Overview

52 Week High-Low	**$238.19 - $143.93**
20 Day Average Volume (sh)	**1,459,463**
Market Cap	**$41.1 B**
YTD Price Change	**-14.7%**
Beta	**0.85**
Dividend / Div Yld	**$1.76 / 1.0%**
Industry	**Insurance - Brokerage**
Zacks Industry Rank	**Top 16% (41 out of 253)**
Last EPS Surprise	**-0.5%**
Last Sales Surprise	**-2.7%**
EPS F1 Est- 4 week change	**-3.0%**
Expected Report Date	**07/24/2020**
Earnings ESP	**-4.4%**
P/E TTM	**18.6**
P/E F1	**17.7**
PEG F1	**NA**
P/S TTM	**3.7**

Sales and EPS Growth Rates (Y/Y %)



Sales Estimates (millions of $)

	Q1	Q2	Q3	Q4	Annual*
2021	3,314 E	2,580 E	2,405 E	2,959 E	11,758 E
2020	3,219 A	2,655 E	2,431 E	2,967 E	11,339 E
2019	3,143 A	2,606 A	2,379 A	2,885 A	11,013 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	$3.81 E	$2.19 E	$1.78 E	$3.23 E	$11.20 E
2020	$3.68 A	$2.00 E	$1.60 E	$2.72 E	$10.05 E
2019	$3.31 A	$1.87 A	$1.45 A	$2.53 A	$9.17 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 05/04/2020. The reports text is as of 05/05/2020.

Overview

Headquartered in London, Aon plc is a British multinational corporation that offers risk management services, insurance and reinsurance brokerage, human resource consulting and outsourcing services worldwide. The company operates in more than 120 countries. As an insurance broker, Aon utilizes its resources to develop individual as well as group insurance programs. It offers its services globally across personal lines, mid-market companies and multinational companies.

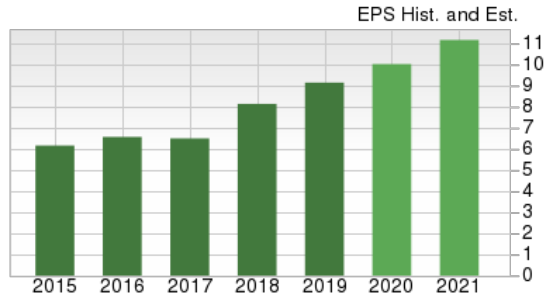
In October 2010, Aon Corporation – a wholly-owned subsidiary of Aon plc – acquired Hewitt Associates, an American company providing human capital and management consulting services. Hewitt merged with the consulting services business of Aon to form Aon Hewitt.

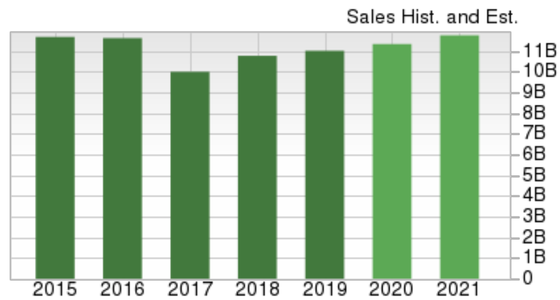
Up to 2016, Aon reported through two segments – Risk Solutions & HR Solutions. In 2017, the company divested its HR business to Blackstone.

Now the company reports through five revenue lines, namely, Commercial Risk Solutions, Reinsurance Solutions, Retirement Solutions, Health Solutions and Data & Analytic Services.

Commercial Risk Solutions (46.2% of 2019 revenues) — This segment consists of retail brokerage, cyber solutions, global risk consulting and captives.

Reinsurance Solutions (6.5%) — This business unit consists of treaty and facultative reinsurance and capital markets.





Retirement Solutions (17.1%) — This deal with core retirement, investment consulting and talent, rewards and performance.

Health Solutions (20.2%) — It deals with heath and benefits brokerage and health care exchanges.

Data & Analytic Services (10%) – This segment includes Affinity, Aon InPoint, and ReView.

Reasons To Buy:

The company’s durability lies in its core business strengthening initiatives, inorganic growth initiatives, strong bottom line and cost savings from its restructuring programs.

- **Price Performance:** In a year's time, shares of the company have outperformed its industry. Given the company’s strong fundamentals, such as steady bottom line and growth initiatives, the stock is expected to continue its rally going forward.

- **Strong Bottom Line:** The company has witnessed a steady bottom-line improvement over the last many years on the back of its strong fundamentals, such as expansions through buyouts and collaborations, divestitures and a solid financial position. In 2019 and the first quarter of 2020, the same was up 2% and 2.4%, respectively, driven by organic revenue growth. Moreover, we expect the company's bottom line to grow in the near term, driven by its core fundamentals, such as a strong capital position and strategic initiatives.

- **Acquisitions and Partnerships**: Acquisitions and partnerships form one of the main growth strategies at Aon and the company has sealed a number of acquisitions over the past three years. Its acquisitions are mainly aimed at expansion of its health and benefits business, flood insurance solutions, and risk and insurance solutions operations. Strategic collaborations also boost Aon’s capacity and makes it one of the largest insurance brokers. In 2017 and 2018, it completed a total of 17 and eight acquisitions, respectively, to enhance its capabilities. In 2019, it acquired businesses for a total valuation of $39 million. It also completed the buyout of CoverWallet, which helped it expand its position in the evolving commercial insurance market for small and medium-sized businesses. Aon also completed five acquisitions during the three months ended Mar 31, 2020. These transactions and alliances are likely to accelerate long-term growth for Aon.

- **Divestitures:** The company has been divesting non-core operations to streamline its business. During 2010–2015, it divested a total of 27 businesses in the Risk Solutions segment and seven businesses in the HR Solutions segment that generated substantial pre-tax gain. In addition, the company divested a business each from its Risk and HR Solutions segments in 2016 and its benefits administration and HR BPO platform to Blackstone in 2017. The company continued with strategic divestitures in 2019 as well. The sale of businesses will streamline the company’s operations, allowing it to focus on more profitable operations, generating higher return on equity.

- **Cost-Curbing Initiatives:** The company’s restructuring efforts to reduce workforce and rationalize technology, which recently ended, aided it to deliver $529 million of annualized savings in 2019. Aon spent $1.48 billion on restructuring and related separation costs right from the inception of its restructuring plan through Jun 30, 2019. This investment is driving expense saving as well as helping the company grow. Moreover, given the current uncertainty revolving around the COVID-19 pandemic, the company initiated reducing its non-compensation costs starting March.

Reasons To Sell:

Stiff competition, high debts and foreign currency fluctuations remain headwinds.

- **Weak Capital Position:** Aon has been issuing debts occasionally to repay outstanding debts. Long-term debt has been continuously increasing since 2014 owing to an increase in commercial paper outstanding. Interest expenses have been persistently rising since 2014 (except 2018).
  Moreover, its total debt is 248.8% (comparing unfavorably with 212.8% as of Mar 31, 2019), higher than the industry's average of 112%. As of Mar 31, 2020, it had cash and cash equivalents of $690 million, lower than its long-term debt of $6.2 billion. Although the company will have to pay not more than $750 million of term debt in the upcoming year, we are concerned about its solvency level.

- **Suspension of Share Buybacks:** Given the COVID-19-led uncertainty, the company deferred its share buyback plan and halted M&A activities. Due to this suspension, the company's bottom line will be bereft of the cushion that share repurchase programs provide.

- **Exposure to Exchange Rate Volatility:** As a global corporation, Aon is exposed to foreign currency fluctuations and has been facing an unfavorable impact of forex volatility on its earnings per share since 2012. The company suffered a 3% unfavorable impact from forex volatility in 2019. In the first quarter of 2020, forex had an unfavorable impact of 3 cents per share. Moreover, management anticipates a negative impact of 3 cents per share in the second quarter, 4 cents in the third and 6 cents in the fourth quarter. Aon's business in more than 100 countries makes its financial results sensitive to foreign exchange rate fluctuations, which might distort true period-to-period comparisons of changes in revenues or pretax income.

- **Overvalued:** Also, Aon's valuation looks expensive at the current level. Looking at the company's forward price-to-book (P/B) ratio, investors may not want to pay any further premium. It currently has a trailing 12-month forward P/B ratio of 12.6 that compares unfavorably with the industry average of 5.1.

Last Earnings Report

Aon's Earnings Miss Estimates in Q1, Increase Y/Y

Quarter Ending	03/2020
Report Date	May 01, 2020
Sales Surprise	-2.73%
EPS Surprise	-0.54%
Quarterly EPS	3.68
Annual EPS (TTM)	9.53

Aon's first-quarter 2020 operating earnings of $3.68 per share missed the Zacks Consensus Estimate by 0.5%. However, the metric improved 11.2% year over year on the back of higher revenues and strong segmental contributions.

Total revenues inched up 2.4% to $3.2 billion including 5% organic revenue growth. This can be attributed to solid new business generation in Reinsurance Solutions and strong management of the renewal book in Health Solutions and Commercial Risk Solutions.

Operating margin grew 440 basis points (bps) to 32.1% and operating margin, adjusted for certain items, expanded 200 basis points to 35.7%. Total operating expenses were down 4% to $2.2 billion, primarily owing to decrease in restructuring charges, favorable impact from foreign currency translation, and the preemptive reduction and deferral of certain discretionary expenses related to COVID-19.

The adjusted effective tax rate on a comparable basis for the first quarter was 19.3% compared with 16.9% in the prior-year period. This was due to certain changes in geographical distribution of income and a net favourable impact from discrete items.

Organic Revenue Catalysts

Commercial Risk Solutions: Organic revenues rose 4% on the back of strong growth across every major geography, highlighted by double-digit growth in Canada and Latin America, mainly on the back of solid retention and management of the renewal book portfolio. The segment witnessed a 3% increase in total revenues year over year to $1.1 billion.

Reinsurance Solutions: Organic revenues improved 9%, driven by growth in facultative placements and new business generation. Moreover, total revenues for the segment increased 8% year over year to $848 million.
Retirement Solutions: Organic revenues were flat year over year. The results reflect a solid rise in investments, consisting of double-digit growth in delegated investment management and growth in Human Capital, partly offset by a decline in core retirement due to coronavirus outbreak. However, total revenues dipped 5% year over year to $397 million.

Health Solutions: Organic revenues were up 5% year over year, led by solid international growth in health and benefits brokerage, especially boosted by a robust uptrend in Latin America, Asia and EMEA. Results reflect strength in active exchange business as well. Revenues from this segment rose 3% year over year to $502 million.

Data & Analytic Services: Organic revenues inched up 1% year over year owing to international prosperity in Affinity business, particularly in the United States. Results also reflect pressure in some discretionary parts of the business due to COVID-19. Revenues slid 1% year over year.

Financial Position

At the end of the quarter, the company's cash flow from operations soared 357% to $338 million. Moreover, free cash flow surged to $279 million from $17 million in the prior-year quarter, banking on increase in cash flow from operations.

The company exited the first quarter with total assets worth $30.2 billion, up 3% from the level on Dec 31, 2019.

As of Mar 31, 2020, long-term debt stands at $6.2 billion, declining 6% from the level at 2019 end.

Share Repurchase Update

The company bought back 2.2 million Class A Ordinary shares for nearly $460 million in the quarter under review. As of Mar 31, 2020, it had stock worth $1.6 billion left under its share repurchase program.

Recent News

Aon Acquires Cytelligence — Feb 4, 2020

Aon announced the buyout of Cytelligence, a cyber-security firm based in Canada. The buyout is expected to strengthen Aon's security position.

Aon Pays Quarterly Dividend — Jan 10, 2020

Aon declared a cash dividend of 44 cents per share, payable Feb 14, 2020 to its shareholders of record on Feb 3, 2020.

Aon Acquires CoverWallet — Jan 7, 2020

Aon has completed the pending buyout of CoverWallet, the leading digital insurance platform for small and medium-sized businesses.

Valuation

Aon's shares are up down 15% and 1.1% in the year-to-date period and over the trailing 12-month period, respectively. Stocks in the Zacks sub-industry and the Zacks Finance sector are down 14.4% and 27% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and sector are down 2.3% and 22.5%, respectively.

The S&P 500 index is down 12% in the year-to-date period and 3.7% in the past year.

The stock is currently trading at 16.85x forward 12-month earnings ratio, which compares to 17.26x for the Zacks sub-industry, 14.81x for the Zacks sector and 20.16x for the S&P 500 index.

Over the past five years, the stock has traded as high as 22.85x and as low as 12.97x, with a 5-year median of 16.92x. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our $187 price target reflects 17.74x forward 12-month earnings ratio.

The table below shows summary valuation data for AON

Valuation Multiples - AON

		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	16.85	17.26	14.81	20.16
	5-Year High	22.85	21.01	16.19	20.16
	5-Year Low	12.97	14.5	11.23	15.19
	5-Year Median	16.92	16.71	13.95	17.44
P/S F12M	Current	3.58	2.81	4.98	3.2
	5-Year High	4.68	3.31	6.7	3.43
	5-Year Low	1.88	1.83	4.98	2.54
	5-Year Median	3.18	2.51	6.04	3
P/B TTM	Current	12.62	5.18	2.07	3.77
	5-Year High	15.97	6.85	2.89	4.55
	5-Year Low	3.83	3.33	1.71	2.85
	5-Year Median	6.52	4.55	2.51	3.63

As of 05/04/2020

Industry Analysis **Zacks Industry Rank:** Top 16% (41 out of 253)

Top Peers

Company (Ticker)	Rec	Rank
eHealth, Inc. **(EHTH)**	Outperform	2
Arthur J. Gallagher & Co. **(AJG)**	Neutral	3
AMERISAFE, Inc. **(AMSF)**	Neutral	2
Brown & Brown, Inc. **(BRO)**	Neutral	3
Marsh & McLennan Companies, Inc. **(MMC)**	Neutral	3
Willis Towers Watson Public Limited Company **(WLTW)**	Neutral	3
Employers Holdings Inc **(EIG)**	Underperform	5
Robert Half International Inc. **(RHI)**	Underperform	4

Industry Comparison Industry: Insurance - Brokerage

Industry Peers

	AON	X Industry	S&P 500	AJG	MMC	WLTW
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	3	-	-	3	3	3
VGM Score	D	-	-	C	F	F
Market Cap	41.06 B	1.89 B	19.65 B	15.20 B	49.97 B	23.63 B
# of Analysts	8	6	14	7	9	9
Dividend Yield	0.99%	1.24%	2.19%	2.25%	1.84%	1.48%
Value Score	D	-	-	C	F	D
Cash/Price	0.02	0.09	0.06	0.18	0.03	0.04
EV/EBITDA	16.93	14.07	11.76	13.18	16.54	12.61
PEG Ratio	NA	2.19	2.48	1.89	4.53	1.62
Price/Book (P/B)	12.62	2.59	2.63	3.00	6.71	2.27
Price/Cash Flow (P/CF)	14.88	14.92	10.38	12.80	16.45	10.94
P/E (F1)	18.01	20.70	18.81	20.51	20.88	16.20
Price/Sales (P/S)	3.70	2.57	2.02	2.15	2.90	2.57
Earnings Yield	5.66%	4.83%	5.07%	4.88%	4.79%	6.17%
Debt/Equity	1.91	0.33	0.73	0.85	1.51	0.59
Cash Flow ($/share)	11.94	2.99	7.01	6.26	6.00	16.77
Growth Score	C	-	-	A	F	F
Hist. EPS Growth (3-5 yrs)	11.29%	12.31%	10.87%	10.92%	11.97%	12.64%
Proj. EPS Growth (F1/F0)	9.64%	3.58%	-8.14%	7.04%	1.50%	3.35%
Curr. Cash Flow Growth	-0.54%	6.15%	5.88%	9.99%	11.40%	6.15%
Hist. Cash Flow Growth (3-5 yrs)	3.75%	13.04%	8.55%	13.27%	9.25%	30.62%
Current Ratio	1.29	1.29	1.25	1.07	1.13	1.60
Debt/Capital	65.64%	24.13%	44.07%	45.98%	60.12%	36.96%
Net Margin	14.84%	9.63%	11.00%	9.63%	10.33%	11.55%
Return on Equity	63.91%	14.70%	16.43%	15.29%	30.94%	14.39%
Sales/Assets	0.38	0.37	0.55	0.36	0.55	0.26
Proj. Sales Growth (F1/F0)	2.96%	2.53%	-1.76%	0.93%	3.93%	2.11%
Momentum Score	D	-	-	D	D	F
Daily Price Chg	-0.30%	0.07%	-0.01%	3.39%	1.69%	0.11%
1 Week Price Chg	1.52%	2.17%	0.53%	2.96%	4.08%	3.45%
4 Week Price Chg	2.62%	3.66%	6.66%	-2.52%	13.06%	4.66%
12 Week Price Chg	-23.11%	-19.26%	-20.38%	-24.95%	-16.02%	-14.52%
52 Week Price Chg	-1.11%	-2.60%	-13.44%	-4.09%	5.04%	2.75%
20 Day Average Volume	1,459,463	76,736	2,567,149	1,353,757	2,194,215	1,175,485
(F1) EPS Est 1 week change	-1.34%	-1.60%	0.00%	-1.87%	-3.29%	-3.72%
(F1) EPS Est 4 week change	-3.01%	-4.99%	-6.96%	-5.00%	-6.21%	-4.99%
(F1) EPS Est 12 week change	-3.48%	-5.61%	-13.90%	-6.01%	-6.67%	-5.20%
(Q1) EPS Est Mthly Chg	-6.26%	-9.41%	-13.62%	-11.90%	-9.41%	-9.90%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	D
Growth Score	C
Momentum Score	D
VGM Score	D

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

Disclosures

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