27-Oct-2023

Aon Plc (AON)

Q3 2023 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning, and thank you for holding. Welcome to Aon plc's Third Quarter 2023 Conference Call. At this time, all parties will be in a listen-only mode until the question-and-answer portion of today's call. I would also like to remind all parties that this call is being recorded. If anyone has any objection, you may disconnect your line at this time.

It is important to note that some of the comments in today's call may constitute certain statements that are forward-looking in nature, as defined by the Private Securities Reform Act of 1995. Such statements are subject to certain risks and uncertainties that could cause actual results to differ materially from historical results or those anticipated. Information concerning risk factors that could cause such differences are described in the press release covering our third quarter 2023 results, as well as having been posted on our website.

It is now my pleasure to turn the call over to Greg Case, CEO of Aon plc.

Gregory C. Case
Chief Executive Officer & Executive Director, Aon Plc

Good morning, everyone. Welcome to our third quarter conference call. I'm joined by Christa Davies, our CFO; and Eric Andersen, our President. As in previous quarters, for your reference, we posted a detailed financial presentation on our website.

As we begin the call today, we'd like to take a moment to reflect on the ongoing conflict in Israel and Gaza. We condemn violence anywhere it occurs in the world and remain highly concerned about all in harm's way. The safety and well-being of our colleagues and their families is always our top priority. And our team is in constant contact with our leaders in Israel to ensure our colleagues, their families and our clients have our full support. As we will talk on the quarter, we want to start with a huge thank you to our Aon colleagues around the world for all they do every day to support each other and to support our clients.

Turning to financial performance. We delivered strong results in the quarter that contribute to year-to-date progress against our key financial metrics. Organic revenue growth of 6% in the quarter was highlighted by double-digit growth in Reinsurance Solutions and Health Solutions. Year-to-date, 7% organic revenue growth and ongoing operational improvement helped contribute to 80 basis points of adjusted operating margin expansion and 10% adjusted operating income growth, a strong performance.

In our solution lines, Reinsurance Solutions delivered another very strong quarter of 11% organic revenue growth with strong growth across treaty, [ph] stock (00:02:29) and our Strategy and Technology group. In addition to delivering a strong quarter, our team is already helping clients prepare for the 2024 renewals. Health Solutions also delivered another very strong quarter, with 10% organic revenue growth, as our team continued to drive strong, new and renewal business. We see ongoing focus from clients to address underlying trends impacting their workforce and health care costs, such as medical and wage inflation, population health, focus on wellbeing and overall talent engagement.

Within Wealth Solutions, organic growth of 4% reflected strength in retirement as our team continues to help clients with pension risk transfer and regulatory change. Finally, Commercial Risk organic revenue growth of 4% reflected strong renewals and net new business, with strength internationally in EMEA and the Pacific. However, overall organic revenue growth was negatively impacted by the external M&A and IPO markets as we communicated previously.

Today, we're also excited to announce actions to go further, faster on Aon United. And we will ascribe our plan and our restructuring program will accelerate key elements of our strategy. As always, our actions are driven by client need. For our clients, the difficult reality of the current world is evident everywhere as they face increasing challenges, understanding, measuring and dealing with risk.

Our forthcoming Global Risk Management Survey details this trend with input from over 3,000 public and private clients of all sizes across geographies and industries. Trade, technology, weather and workforce stability are simple forces in today's risk landscape. While each of these forces are individually impacting risk exposures, their increasing connectivity is compounding complexity and presenting new challenges for business leaders.

Responding to our clients' increasing and evolving demand help protect and build their business. We are advancing a series of actions to further accelerate our Aon United strategy. These actions, taken over the next three years, will deliver outcome that directly address client need and demand. Specifically, we will improve the quality and availability of analytic tools available to clients, substantially improve their service experience and expand the quality and scope of solutions we bring to them. This work will put our clients in a much stronger position to make better decisions to support their companies.

We will accomplish this by delivering on three commitments over the next three years. Internally, we call this [ph] 3 by 3 Plan (00:04:56). The three commitments include, first, leveraging our risk capital and human capital structure and capabilities to unlock new integrated solutions across our core business, but also address new requirements in client demand. Second, embedding the Aon Client Leadership model across our enterprise clients in large and middle market segments to further strengthen and expand our client relationships. And third, accelerating the Aon Business Services plan to set a new standard for service delivery and next-generation analytic tools.

The benefits of this plan accrue to our colleagues, our clients and our shareholders. Colleagues win with greater capability to serve clients. Today, our team is exceptional in their client leadership focus and impact. And this work provides them with next-generation tools and capability to serve clients and to meet increasing client demand.

Clients win with better solutions and better service. This work resets client service to a higher standard and provides analytic tools and solutions required to meet demand. And investors win through our greater client relevance, continuing margin improvement and sustained double-digit free cash flow growth. And while we could have achieved these benefits over time, we have instead decided to act now an accelerated proven strategy.

Let me describe how our team came to this conclusion. The last 10-plus years have demonstrated that a more connected firm is a more capable firm and a connected Aon isn't done in concept. It's accomplished through meaningful structural change, which must be embraced and led by colleagues. It is cultural and only viable as a defining part of our DNA.

And even though we remain on a journey with plenty of distance to travel and opportunity ahead to improve, we have made progress. And the results have been meaningful for clients in terms of innovation and support; for colleagues in the form of excitement and engagement currently at an all-time high; and for shareholders measured by sustainable value -creation, including a 30.8% full-year 2022 operating margin, compound free cash flow growth of 13% a year from 2010 to 2022 and return on invested capital at year-end 2022 of 30.6%. However, two observations give us conviction that going further, faster is a requirement. The first is increasing client demand and the second is our execution competence based on our proven track record, the [ph] 3 by 3 (00:07:21) action plan we have defined and the diligent work already underway.

Accelerating our plans requires greater upfront investment. And as announced in our press release, we'll execute this through a $900 million restructuring program focused on two areas. First is on accelerating our Aon Business Services plan by focusing on standardizing operations, integrating operating platforms and driving product innovation. And the second is on workforce planning, to align skills and capability required to deliver on the digital-first opportunity embedded in Aon Business Services, as well as workforce changes to strengthen our client-serving capability in risk capital and human capital.

This investment will also drive $350 million of cumulative annual run rate savings by year-end 2026, which Christa will describe in more detail. Overall, our team is very excited about the opportunity to accelerate our plans to strengthen client leadership, and fortunate that we have the opportunity and option to take this step as a direct result of the work of our colleagues.

We continue to expect to drive mid-single-digit or greater organic revenue growth over the course of 2023 and the long term. We further expect these savings will contribute to ongoing annual margin expansion. While the program will impact free cash flow in the near term, over the long term, we expect to continue to deliver double-digit free cash flow growth, driven by operating income and working capital improvements.

In summary, our strong year-to-date operational performance, including 7% organic revenue growth, 80 basis points of adjusted operating margin expansion and 10% adjusted operating income growth demonstrate strong momentum against our Aon United strategy and creates the opportunity for us to double down on our strategic commitments around risk capital , human capital , our Client Leadership Model and Aon Business Services. These steps will enable us to continue to address evolving client demand, improve colleague outcomes and continue our track record of long-term shareholder value-creation.

Now, I'd like to turn the call over to Christa for her thoughts on our financial results and long-term outlook. Christa?

Christa Davies

Chief Financial Officer & Executive Vice President-Global Finance, Aon Plc

Thanks so much, Greg; and good morning, everyone. As Greg highlighted, we delivered strong operating results in the third quarter and year-to-date. Through the first nine months of the year, we translated 7% organic revenue growth into 80 basis points of adjusted margin expansion and 10% adjusted operating income growth. These results position us very well to continue driving results in 2023 and over the long term. We look forward to building on this momentum as we head into the last quarter of the year.

As I reflect on our performance year-to-date, as Greg noted, organic revenue growth was 6% in Q3 and 7% year-to-date. We continue to expect mid-single-digit or greater organic revenue growth for the full-year 2023 and over the long term. I would also note that reported revenue growth of 10% in Q3 includes a favorable impact from changes in FX of 2%, primarily driven by a weaker US dollar versus most currencies compared to the prior-year period. Reported revenue growth of 7% year-to-date includes an unfavorable impact from changes in FX of 1%, primarily driven by a stronger US dollar versus most currencies compared to the prior-year period.

I'd also highlight, fiduciary investment income, which is not included in organic revenue growth, was $80 million in Q3 and $196 million year-to-date, or 3% of total revenue in Q3 and 2% of total revenue year-to-date.

Moving to operating performance. We delivered strong operational improvement through the first nine months of the year with adjusted operating margins of 30.8%, an increase of 80 basis points, driven by revenue growth, efficiencies from Aon Business Services overcoming expense growth, including investment in colleagues and technology to drive long-term growth.

We translated double-digit adjusted operating income growth into adjusted EPS growth of 15% in Q3 and 8% year-to-date. As noted in our earnings materials, FX had an unfavorable impact of approximately $0.01 per share in Q3 and an unfavorable impact of $0.20 per share year-to-date. If currency remain stable at today's rates, we would expect a favorable impact of $0.03 per share in the fourth quarter, totaling an unfavorable impact of $0.17 per share for the full-year 2023.

I'd also note the change in other non-operating expense had a $0.15 per share or 7% unfavorable impact in Q3 and a $0.59 per share or 6% unfavorable impact year-to-date. This reflects an unfavorable impact from an increase in noncash net periodic pension expense, as well as balance sheet FX remeasurement in the current period and a gain on sale of businesses in the prior-year period.

Turning to free cash flow. Cash flow from operations decreased $3 million year-over-year, reflecting double-digit operating income growth, offset in part by higher cash tax payments, as we've mentioned previously and the negative impact of working capital in the third quarter caused by temporary invoicing delays associated with the implementation of a new system. Free cash flow decreased 4% to approximately $2 billion, primarily driven by a $77 million increase in CapEx.

CapEx was elevated in the first nine months of the year compared to the prior-year period as we executed a number of technology projects to drive long-term growth. I'd note CapEx could be lumpy quarter-to-quarter. And we expect CapEx to moderate in the fourth quarter for total CapEx investment of $220 million to $250 million in 2023. As we've said before, we manage CapEx like all of our investments on a disciplined ROIC basis, and we expect it to grow as a business going forward.

Now, let me share more details about our Accelerating Aon United program. As Greg highlighted, we are doubling down on three strategic commitments, including accelerating Aon Business Services, which in turn enables us to unlock advances in risk capital and human capital and our Aon Client Leadership strategy. Together, these commitments will drive more value for clients, colleagues and shareholders.

The investment to accelerate our three-year Aon Business Services operating model focuses on the same three areas we've mentioned previously. We see proven benefits and will now accelerate. Number one, standardized operations; number two, integrating operating platforms; and number three, increasing product innovation and development. We've already made considerable progress in standardizing our operations, but we see significant opportunity, both within and across our solution lines. The work we're doing to standardize operations will drive integrated service delivery platforms, which provides additional opportunities to standardize how we do business. And standard operations, combined with integrated platforms, enables more effective new product development and innovation at scale.

By accelerating standardization across the portfolio and establishing fewer, more integrated platforms, we'll be able to deliver more analytical tools to colleagues and clients across the entire portfolio. With this underlying infrastructure in place, we'll be able to leverage advances in AI and machine learning to further accelerate the product development cycle and unlock new efficiencies across the portfolio.

Let me provide a bit more financial detail about the strategic investments. We expect total annual in-year savings of $350 million to be achieved in 2026, contributing to ongoing sustainable long-term margin expansion. I'd note, we expect savings to ramp over time, with annual in-year savings expected to be $100 million in 2024, $250 million in 2025 and $350 million in 2026.We do not expect material savings or impacts to cash flow in 2023.

Cash restructuring charges of $900 million reflect the savings ratio of 2.6 times and are largely for technology costs and workforce optimization. I'd note you can think of the $900 million cash restructuring charge as less than 10% of underlying free cash flow over the next three years and the $350 million of savings as a full percent cost takeout relative to our cost base of approximately $9 billion.

We also expect an additional $100 million of noncash charges, largely related to asset and lease impairments. We do not expect significant incremental CapEx associated with the program and we expect CapEx will grow in line with the business in the future from our guidance of $220 million to $250 million in 2023. In the third quarter of 2023, we incurred $6 million of restructuring charges, and we'll communicate charges and savings going forward each quarter.

Contemplating the program. As we look forward, we continue to expect mid-single-digit or greater organic revenue growth for the full-year 2023 and over the long term. We expect program savings will contribute to ongoing, sustainable, long-term margin expansion and expect to deliver margin expansion in 2023, 2024 and over the long term. As we've noted previously, over the last 12 years, we've delivered 1,120 basis points of margin expansion or about 90 basis points a year on average.

Our outlook for free cash flow remains strong. We expect to deliver high-single-digit free cash flow in 2023. I'd note this guidance contemplates the impact from restructuring on free cash flow in Q4, but we do not expect restructuring to have a material impact on cash flow this year. While free cash flow will be reduced in the near-term by restructuring, we expect to return to our trajectory of double-digit free cash flow growth over the long term, driven by operating income growth and ongoing working capital improvements.

As we've said previously, as we look at the opportunity in Aon Business Services and across our client-facing capability, we know that delivering this strategy will result in long-term progress against our key financial metrics, organic revenue growth, margin expansion and free cash flow growth.

Now, turning to capital allocation. Given our strong outlook for free cash flow, we expect share repurchase to continue to remain our highest return on capital opportunity for capital allocation. We believe we're significantly undervalued in the market today, highlighted by nearly $2 billion of share repurchase year-to-date. We also expect to continue to invest organically and inorganically in content and capabilities that we can scale to address unmet client needs. Our M&A pipeline continues to be focused on our global priority areas that will bring scalable solutions to clients' growing and evolving challenges. We'll continue to actively manage the portfolio and assess all capital allocation decisions on an ROIC basis.

Turning now to our balance sheet and debt capacity. We remain confident in the strength of our balance sheet and manage liquidity risk through a well-laddered debt maturity profile and expect to add incremental debt as EBITDA grows over the long term, while maintaining a strong investment-grade credit profile.

In summary, our strong financial results in the quarter and year-to-date reflect strong operational performance driven by our Aon United Strategy and our Aon Business Services platform. We see an opportunity to accelerate the next stage of our Aon United Strategy and expect this investment will contribute to sustainable long-term, top and bottom line growth and ongoing shareholder value-creation.

With that, I'll turn the call back over to the operator, and we'd be delighted to take your questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Our first question is from Rob Cox with Goldman Sachs. Please proceed.

Robert Cox
Analyst, Goldman Sachs & Co. LLC

Q

Hi. Thanks for taking my question. Just curious on the free cash flow. I just want to make sure I understand what exactly is driving the lower free cash flow guide, because it sounds like the restructuring isn't material this year, and you mentioned the invoicing was a temporary issue. So, just trying to understand what exactly is driving that guide lower?

Christa Davies
Chief Financial Officer & Executive Vice President-Global Finance, Aon Plc

A

Yeah, it's really about the temporary invoicing delay, Rob. We had that in Q3. And while we're addressing the system issue, we could continue to see temporary impacts to working capital in the fourth quarter.

Robert Cox
Analyst, Goldman Sachs & Co. LLC

Q

Okay. Got it. Thank you. And just on the restructuring program, just compared to your history with these programs and some peers, the 2.6x saving ratio maybe seems a little conservative for a program that includes an element of workforce rationalization. So, just curious if management views it that way, and if we could potentially see more savings come to life beyond the $350 million?

Gregory C. Case
Chief Executive Officer & Executive Director, Aon Plc

A

Rob, we're glad you asked the question. We appreciate it. Listen, I think, it's worth stepping back here a little bit and really making sure you understand exactly what we're trying to get accomplished here, because this is different than anything you've certainly ever seen from us before, and we're very excited about it. We've said before, look, our clients and our colleagues, they're demanding better solutions. You're seeing it every day. The survey I described identified some of the challenges they see really around risk capital beyond our solution lines and human capital . And to be clear, we're delivering on those solutions through Aon United.

But they're demanding we go further, faster, and they're asking us about this. Our colleagues see it and they're incredibly excited about our ability to deliver on it. And for us, the opportunity is clear. We've got Aon Business Services. We've got the platform in place. We have a long way to go on it, but supported by 15,000 colleagues, we know we can accomplish this objective around clients, and we can do it faster and accelerate the strategy and build a stronger client-facing firm. So, that's basically the focus, what we're trying to do.

And to be clear, this is easy to say but hard to do. I mean, data analytics, the operating platforms have all got to be connected and integrated; teams have got to be aligned to accomplish the goal, and that's exactly the path we're on. And now we're going to accelerate it. And as Christa observed, for a firm that really obsesses around return on invested capital, we believe this investment's going to be one of the most compelling ever.

But I'm thinking, Eric, to bring it to life, it's just so important everyone understands exactly what we're doing. How does this show up from a client standpoint, in your view?

Eric J. Andersen
President, Aon Plc

A

Sure, Greg, and maybe I'll do an example, might be the easiest way to bring it to life. Because it's evolving so quickly that as clients are looking at these exposures and these developments, they're pressing us for more insight, more analytics. And maybe just that's come to mind around climate, which is such a topic today.

We had a client in Asia Pacific that was looking at severe weather and how it was going to affect their loan portfolio, how it was going to affect their future financial obligations in terms of disclosure. And we engaged with them because they had asked us about their future. They asked us about the physical climate risk that was coming. But as we began to talk to them, they were really starting to press for a baseline of their loan exposures today, which required climate analytics that are cutting-edge and are really just coming to the fore. And so, what they're doing with it today is they're looking at integrating their climate analytics into their risk modeling themselves as they go forward as a business.

And I guess the point of it is, that capability, as it's being developed and being brought to the market, really allows all types of clients to look at climate physical risk, put it into their own business model as they go forward, but they're starting from one place and often ending in another. But to be able to deliver those analytics in the form that they can use to be able to build their own business – and Business Services provides that engine to be able to aggregate the data, to be able to put it in usable format going forward. So, we're really excited about what this gives us and the ability to replicate that across the globe as financial institutions of all type are being pressed to understand their climate risk.

Christa Davies
Chief Financial Officer & Executive Vice President-Global Finance, Aon Plc

A

And then just in terms of the financial piece, Rob, it is $900 million of cash restructuring charge to deliver $350 million of savings in-year in 2026. We don't expect to go above that guidance. We do expect, in terms of financial guidance to continue to expect mid-single-digit organic revenue growth or greater for the full-year 2023 and over the long term. We expect to deliver adjusted operating margin for the full-year 2023, full year 2024 and over the long term. And we expect these program savings will contribute to ongoing sustainable long-term margin expansion. And then while free cash flow will be impacted in the short term, we expect to return to our trajectory of double-digit free cash flow growth over the long term, driven by operating income growth and ongoing working capital improvements.

And then, lastly, as Greg said, we look at all of these investments across Aon on a disciplined ROIC basis. And I want to reiterate, we focus intensely on cash. And we think about all investments on this disciplined basis. This investment is no different. It will enable us to accelerate the work we're doing across the firm, and ultimately, contribute to great long-term shareholder value creation across our key metrics in line with our track record.

Robert Cox
Analyst, Goldman Sachs & Co. LLC

Q

Great. Thanks. I appreciate all that color.

Operator: Our next question is from Paul Newsome with Piper Sandler. Please proceed.

Paul Newsome
Analyst, Piper Sandler & Co.

Q

Good morning. Thanks for the call. Congratulations on the quarter. I want to ask about whether or not the restructuring charge here – the cost savings from the restructuring charge we're looking at is really additive to the ongoing margin improvement. In other words, do you need to have this effort to continue that margin expansion? I think given how good the margins are, people sometimes wonder if there's a limit here, and if more extraordinary things need to happen to continue have that margin expansion?

Christa Davies
Chief Financial Officer & Executive Vice President-Global Finance, Aon Plc

A

Thanks so much for the question, Paul. And look, the way we think about financial guidance going forward is mid-single-digit or greater organic revenue growth in 2023 in the long term, margin expansion in 2023 to full-year 2024 and over the long term, and then double-digit free cash flow growth long term. We do expect this program to help us accelerate the strategy and we expect the savings to contribute to margin expansion next year.

But what we'd also say is, we think about margin expansion holistically, Paul. And so each year, we've continued to say this, we have a gross margin expansion that's higher than what we met – generate for shareholders and we continue to invest. And you've seen that in calendar year 2023 as well, where we've continued to invest in technology. You can see technology expenses up; CapEx, where we're investing in long-term technology platforms to drive long-term productivity. And so, we're investing in the long-term strategy as we generate great results for shareholders each and every year.

Gregory C. Case
Chief Executive Officer & Executive Director, Aon Plc

A

And maybe just add one other point on this, Paul. When you think about margin, we often get asked about this as – it's almost like it's treated like a zero-sum game, the split between clients, and colleagues and shareholders. We don't see it that way. We see it around value.

The example Eric described is really around incremental value to a client. Asking a question they hadn't asked before, we provide an insight around analytics that's simply not possible without Aon Business Services on a scaled basis. We provide incremental value. We get obviously compensated for that. That contribution is really what drives margin over time.

So, greater value means more margin, and so that's what you're hearing today. So, how we're going to invest, create greater capability to deliver more value for clients. And that really is the engine around margin improvement, which is why we're so confident; now, even more so with this investment to continue margin improvement over time.

Paul Newsome
Analyst, Piper Sandler & Co.

Q

So, it's been pointed out to me this morning that the restructuring charge that you folks are planning on taking relative to the ongoing savings, it's on the larger end of where historically you folks have done. You've done a lot of these sort of efforts successfully. Is there anything structurally different with what you're doing here as compared to some of the other efforts – other charges and saving effort that you've done past? [indiscernible] (00:28:12)

Christa Davies

Chief Financial Officer & Executive Vice President-Global Finance, Aon Plc

A

It is, Paul. Yeah, it is very different. So, what we would say, and I think Greg said this earlier is, it's responding to client need and meeting unmet client needs. And we are seeing more of that than ever before. You saw that in our risk survey, where clients have significant unmet client needs. But Aon Business Services was the catalyst here. And we're really building on a proven track record of success. And we see Aon Business Services as the catalyst which drives risk capital , human capital in our Aon Client Leadership strategies.

And we've brought together a set of new leaders and developed a three-year strategy to further strengthen and connect our firm. And this strategy accelerates our ability to deliver on standardized platforms, standardized operations and innovative products at scale. And so, that is very different than what we've done before, Paul. And that really is much more sustainable long-term strategy development that's going to benefit clients, that's going to benefit colleagues and going to benefit shareholders.

Gregory C. Case

Chief Executive Officer & Executive Director, Aon Plc

A

And if you think about it, Paul, we've got tremendous reinforcement around risk capital and human capital and how we're approaching clients in that regard. Everyone can talk about a piece of good work for an individual client. We're talking about taking Eric's example, and really how do you scale that and do that all over the world? And then, when you're done with that, keep getting it better and better.

You can't do that without Aon Business Services. I mean, this is 15,000 colleagues around the world with a team led by Christa, [indiscernible] (00:29:33) Mindy Simon and others who brought talent from really outside of our industry, our purpose think about how to resolve that. And the strength of that is extraordinary in our ability to actually scale new integrated analytics.

This is the structural investment that we now see, we can do much faster in our clients' requirements, to do it much faster than we would have done over time. That's what's fundamentally different. This is very different than anything you've ever seen before, and the reason we're so excited about it is because, again, clients are demanding, our colleagues are excited to deliver it. And this is a structural move that really bets on our history. We've already made progress. This is the strategy. We're doubling down and investing on it. In a structural way, it will help us scale and really innovate more effectively.

Paul Newsome

Analyst, Piper Sandler & Co.

Q

Great. Thank you. Always appreciate the help and your patience.

Operator: Our next question is from Charlie Lederer with Citi. Please proceed.

Charlie Lederer

Analyst, Citigroup Global Markets, Inc.

Q

Hey. Good morning. I'll ask another on the Acceleration program. It sounds like our revenue synergy play in a lot of ways, too. Am I digesting that correctly? And can you talk about how it will differentiate you from your competitors?

Christa Davies
Chief Financial Officer & Executive Vice President-Global Finance, Aon Plc
A

Yeah. So, let me describe. What I would tell you is, this is absolutely using Aon Business Services as the catalyst. And the Aon Business Services strategy is really around standardizing operations, creating scale and standardized platforms, and then building on top of those platforms to create products at scale that really drive innovation for clients.

And then, if you think about it, if you bring all of those people, as Greg said, 15,000 people in Aon Business Services, 1,000 data scientists driving analytics – data and analytics, then you could actually apply AI, whether that's at the machine learning end or the Generative AI end, across these platforms and services to drive greater analytical insight and greater value for clients.

But Eric, I mean, you see this every day with clients. What's your side here?

Eric J. Andersen
President, Aon Plc
A

Yeah, absolutely. Absolutely, Christa. Listen, the whole strategy is predicated upon bringing our risk capital and human capital colleagues together to able to do more for clients. And we can talk about a lot of examples, and I'll use one, the parametric business, which is actually bringing reinsurance knowledge to commercial clients; as well on the health care side, where we're using bonds to be able to do resiliency and other things.

That just doesn't happen by accident. It needs capability. It needs analytics. It needs connectivity. And it needs an enterprise client strategy where we could deliver those capabilities right at the largest, most complex clients. So, yeah, really excited about the opportunity, Paul (sic) [Charlie] (00:32:16), to do it.

Charlie Lederer
Analyst, Citigroup Global Markets, Inc.
Q

Got it. Thanks. And I guess, do you guys feel like you have the data science talent in your workforce today to have this, or are those hires kind of part of this plan?

Eric J. Andersen
President, Aon Plc
A

We have 1,000 data scientists across our risk capital business. And so, we feel like we're cutting edge in that area.

Gregory C. Case
Chief Executive Officer & Executive Director, Aon Plc
A

The other piece you kind of come back to, and this is what – these individual pieces are around the firm. They're phenomenal. They're tremendous in their own right. What Christa's describing is the wiring, the mechanism to connect them more effectively. So, it's not just 1,000. It's 1,000 interconnected against a strategy around analytics and prioritization around analytics, against specific client issues. So, it's a thoughtful strategy that we can actually execute at Aon Business Services.

And the acceleration, as we would have done that over time, now, we're going to double down and do that. This is what's going to change the relevant profile for our clients. So, these are the questions we're asking. And so, it's not just the 1,000 and whatever it ends up becoming over time, it's how that 1,000's going to work together. And the level of comparable data they're going to have around the world.

In the example, Eric has given, it's not just in single analytics and commercial risk or reinsurance, it eventual will cut across talent, it will cut across health. And so to have that integrated platform that you can actually do the analytics upon, with the talent on top of it, is huge.

And some of the folks that Christa has brought in, Mindy Simon have brought in, have come from outside the industry, literally from some companies who are world-class at analytics. And they see an opportunity to really help the world understand risk and volatility in different ways. They find it incredibly compelling. And so, our view is, this is a great opportunity for colleagues, in a way, that really unlocks a lot of opportunity for them because they're going to be talking to clients about these types of issues.

Charlie Lederer
Analyst, Citigroup Global Markets, Inc. Q

Thank you.

Operator: Our next question is from Elyse Greenspan with Wells Fargo. Please proceed.

Elyse Greenspan
Analyst, Wells Fargo Securities LLC Q

Hi. Thanks. Good morning. My first question is on commercial risk. Growth slowed there in the quarter. I was hoping to get more color on what's driving that, is that still a slowdown in M&A and IPO activity or is there something else going on within that business in the quarter?

Eric J. Andersen
President, Aon Plc A

So, hi, Elyse. Why don't I take this. This is Eric. We continue to see strong activity across EMEA, Pacific in core P&C; very solid new business retention, all the sort of underpinnings that you would look for. We did continue to see a slowdown in M&A, and what I call M&A services, which are the things that come off of mergers and acquisitions, whether it'd be a one-off, whether it's reps and warranties, things like that, continued to slow down pretty significantly in the quarter.

Gregory C. Case
Chief Executive Officer & Executive Director, Aon Plc A

And we've said it last time, I think on the call, Elyse, we love this area and this team. They are phenomenal. We just got such great capability here. And Eric and team will continue to kind of double down and invest behind content capability. We're quite confident the transactions will come back at some point in time. When they do, we're unbelievably well-positioned. And we'll absorb that win in the process, but very bullish on the future in this category.

Elyse Greenspan
Analyst, Wells Fargo Securities LLC Q

So, until the activity comes back, would you expect like the organic growth within commercial risk to stay in like the 4$ to 5% range, or was there anything unique to the third quarter?

Gregory C. Case
Chief Executive Officer & Executive Director, Aon Plc A

No, there was nothing unique in the third quarter. When we look at some of the strong areas around the world, some of the specialty businesses like construction, that continued to have very solid performance, we're pretty happy with the way the business has been performing and whether that area comes back, we've held the team and are really excited about the future opportunities there.

Elyse Greenspan
Analyst, Wells Fargo Securities LLC

Q

And then, I want to come back to the savings program. So, $350 million by 2026. Are you expecting the entirety of that to fall to the bottom line? And then, I know you guys mentioned, in your comments as well as in the slide, that there is platform [ph] quantification (00:36:24), technology, there's some workforce changes. Can you bucket – can you break down the $350 million by the areas that are specifically driving the savings?

Christa Davies
Chief Financial Officer & Executive Vice President-Global Finance, Aon Plc

A

So, thanks so much for the question, Elyse. The first answer is yes, we do expect the $350 million to drop to the bottom line. We obviously are continuing to invest in the business as I described earlier. A good example of that is the investments we've made in technology in the first nine months of the year. You see that in our technology expense and our CapEx expense, both being up, funding investments in long-term operations, technology platforms and product development to meet client needs.

And so, we will see those savings drop to the bottom line, but they are in the context of our overall financial guidance, which is mid-single-digit or greater organic revenue growth for 2023 in the long term, margin expansion in 2023/2024 in the long term and long-term double-digit free cash flow growth. And then in terms of the breakout, we do expect the breakout of the $900 million to be primarily technology expense and workforce optimization. We have not provided specific details on that and we will report on it each quarter.

Elyse Greenspan
Analyst, Wells Fargo Securities LLC

Q

Thank you.

Operator: Our next question is from Jimmy Bhullar with JPMorgan. Please proceed.

Jimmy S. Bhullar
Analyst, JPMorgan Securities LLC

Q

Hi. Good morning. So, first, just on organic growth. Are you able to quantify how much of a headwind, the slower M&A and transaction related to bid activity has been to your growth, maybe either in an absolute sense versus normal or maybe versus a year ago? Just so we get a sense of how your results would be versus peers that have less of that.

Eric J. Andersen
President, Aon Plc

A

Sure. This is Eric. We don't disclose that number. But I would just say, if you track M&A from outside sources, certainly down 30% year-on-year, and that continues to show headwinds. And I would just say, listen, as that recovers, we will recover with it. We've maintained the team. We've maintained the relationships. We continue to stay very close to those clients. And when they react, we will be right there with them. But it's a good business for us. We really think it provides great value to them and the ultimate clients. And we continue to hold and invest in that team.

Jimmy S. Bhullar
Analyst, JPMorgan Securities LLC

Q

And then, on free cash flow, should we assume that it'll get to double digit growth in 2026 once the program's done, or is it after that, earlier than that?

Christa Davies
Chief Financial Officer & Executive Vice President-Global Finance, Aon Plc

A

So we haven't given specific guidance on the timing. What we have said is that we absolutely expect long-term free cash flow growth. We run the firm on free cash flow. We are extremely bullish on long-term free cash flow growth, driven by operating income growth and working capital improvements. And so, this will absolutely contribute to that. And so we're very, very excited about the outlook for free flow growth long term.

Jimmy S. Bhullar
Analyst, JPMorgan Securities LLC

Q

Okay. And then, just lastly, we've gotten a lot of questions on the sort of impact on your business from the Vesttoo fallout. And do you expect any financial impact, or reputational or otherwise; or have you seen anything that you're able to discuss beyond what's in your regulatory filings?

Eric J. Andersen
President, Aon Plc

A

Listen, I would say from a Vesttoo – oh, go ahead Christa. I'm sorry.

Christa Davies
Chief Financial Officer & Executive Vice President-Global Finance, Aon Plc

A

No, you go, Eric.

Eric J. Andersen
President, Aon Plc

A

Look, I would just say, Vesttoo is one of the many parties that have been involved in the business, whether it's reinsurance, whether it's other areas. And we continue to monitor the situation very carefully, working with our clients, helping them to provide options to replace that loss capital. And we continue to see that work being done. And our expectation is, it will continue to evolve as their bankruptcy process works its way through.

Jimmy S. Bhullar
Analyst, JPMorgan Securities LLC

Q

All right. Thank you.

Operator: Our next question is from David Motemaden with Evercore ISI. Please proceed.

David Motemaden
Analyst, Evercore ISI

Q

Hi. thanks. Good morning. I just had a question on the Accelerated Aon United Program, more soon the revenue side, and how we can think about that. It sounds like a big opportunity. I guess, I'm a little surprised that you aren't making any changes to your organic growth outlook, the mid-single digit or greater.

So, maybe could you just talk about how much you would expect this program to contribute to accelerated organic growth? You know, it would be helpful just maybe put some numbers around it. I'm sure you guys look at it internally. So, yeah, I'm just trying to get a sense for how we can think about the revenue opportunity here.

Gregory C. Case
Chief Executive Officer & Executive Director, Aon Plc

A

David, I would come back and just think about, this is about client relevance, as Eric described, I think very well. What this is going to do is help us innovate and be more relevant to clients on the issues that matter most to them. That will have impact over time. What we want to be clear, though, is in terms of sort of the progress, we're staying mid-single digit or greater organic revenue growth, continuing margin expansion and double-digit free cash flow growth.

For us, that will be the validation and this accelerates that strategy and certainly increases probability and our success against that in every way, shape or form. And if there's opportunity beyond that, fantastic, but we'd start with that. We love that story, and we're incredibly excited about what this does with that story, which is just really, really delivers on it.

David Motemaden
Analyst, Evercore ISI

Q

Got it. Thanks. And then, maybe this is an acceleration of Aon United. But I believe there was a number of maybe five or six years ago that you guys had initially instituted the strategy, the Aon United strategy. So, I'm wondering if you just – not thinking about the new program but looking at Aon United in the past, once you instituted that program. I there anyway to size historically how much that program contributed to the organic growth that we saw, I guess, maybe leading up to the COVID pandemic?

Gregory C. Case
Chief Executive Officer & Executive Director, Aon Plc

A

This is very important because we obviously track and look at this all the time. This is why, as we described in the opening, we came to a level of conviction that said, we're not going to evolve this. We're doing it now. We're moving now. We're going to make investments now to accelerate faster than we would have before.

Because the track that we've laid is this continues to get more relevant for clients. If you think about it, 10 years ago, we talked about increasing risk. It turns out, 10 years later, my God, we might have been right on that. So, there's risk everywhere around the world, interconnected. Climate's real. All of a sudden, everything's real. Cyber, everything. And so, our clients are asking for more.

And the fundamental aspect to that, everybody can talk about delivering. But unless you're a connected firm, truly supporting each other around the globe, you cannot deliver on it. And you certainly can't innovate at a level that equates to what client demand is. And so, that's what Aon United has given us.

What you've seen us do over the last bit of time is really structurally double down on that. risk capital and human capital only five, six, seven months ago, structurally ,really connected how we bring analytics across the entire risk spectrum, not just in commercial risk reinsurance, but also the risk spectrum on talent, on health, et cetera. All of these things come together and that's the next step sort of in the process. So, for us, it isn't about – it equated to a dollar value here or there, or revenue or margin here or there. It's fundamental DNA. This connectivity around Aon United allowed us to do risk capital and human capital. It allowed us to do Aon Business Services. That's an impossibility without Aon United.

And what we've got now with Eric and the team giving risk capital and human capital the chance to accelerate it into the market with innovation, under Christa's leadership, with Aon Business Services, a chance to really enable it, structurally in ways we've never done before. So, this for us is a natural step that we would have evolved in the process. And all you're hearing about today is that excitement level is higher than ever before, not because of us, but because the clients and our colleagues saying, we need this, we want to deliver it. And what you see us doing today is saying, okay, we're going to accelerate and drive it. And that's really what the investment's about.

David Motemaden
Analyst, Evercore ISI

Q

Understood. I appreciate the color.

Operator: Our next question is from Yaron Kinar with Jefferies. Please proceed.

Q

Hi, guys. Good morning. This is [ph] Charlie (00:45:09) on for Yaron. You guys, in the past, have pointed to a multiyear track record of roughly 90 bps of annual margin expansion. And I guess, should we expect the new cost savings program to be incremental on top of that, or should we continue to expect roughly 90 bps year-over-year?

Christa Davies
Chief Financial Officer & Executive Vice President-Global Finance, Aon Plc

A

: Thanks so much for the question, [ph] Charlie (00:45:30). So, you're right, for the last 12 years, we've delivered 1,120 basis points of margin expansion, so approximately 90 basis points a year. And what we've said with this program is the $350 million of savings in-year in 2026 will fall to the bottom line. They are incorporated into and are part of our long-term sustainable margin expansion, where we will deliver margin expansion in 2023, full-year 2024 and over the long term.

And as I mentioned earlier, what we're really doing, [ph] Charlie (00:45:58) is, we are investing in the business, in client-facing innovation, and content and capability, and data analytics to help solve client need and provide more innovative solutions to clients, to help provide better colleague technology and to drive long-term productivity. And that's really the heart of the Aon Business Services strategy, which is really the catalyst for us investing here today.

Q

Okay, thanks. And then, I guess, just you guys have talked about expecting cost savings to ramp towards the $350 million by 2026. How should we think about the cadence of the $900 million over that same period?

Christa Davies
Chief Financial Officer & Executive Vice President-Global Finance, Aon Plc

A

We have not given specific guidance on the $900 million, [ph] Charlie (00:46:41). So what we will do is report charges and savings each quarter.

Q

Okay. Thanks.

Operator: Our last question is from Meyer Shields with KBW. Please proceed.

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

Q

Great. Thanks. First, conceptual question, I guess, maybe for Eric. You talked about being committed to the M&A space, which suggests that there are disproportionate amounts of expenses relative to current revenues. Can you give us a way of thinking about maybe the margin impact that this revenue pressure is providing?

Eric J. Andersen
President, Aon Plc

A

Well, listen, I wouldn't think about it that way. I would think about what can we do with the talent while there's a downturn. And so, the skills that, that that team has in terms of client coverage and product expertise, we can redeploy that across the firm and put them to work today, while we're waiting out the market. Certainly still working those clients and trying to innovate with new product and opportunities, but at the same time, they bring skill sets around client coverage, industry knowledge, product knowledge that we can use across the firm. So, they're not just sitting there, if that was what you're thinking. But we're deploying them into the client base.

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

Q

Yeah. Okay. It wasn't specifically thinking. That is helpful. Second question that I've got, and it's sort of an interesting one. We've talked about double-digit free cash flow growth once the charges of these are done. Is 2022 still a good base for the compound annual growth rate or that's double digit from the now lower cash flow we expect toward 2026?

Christa Davies
Chief Financial Officer & Executive Vice President-Global Finance, Aon Plc

A

Thanks so much for the question, Meyer. Look, it is off the 2023 baseline. That's the right answer. And I would note that we're really excited about free cash flow growth in 2023. It's high-single digits. And so, we'll report 2023 free cash flow, and you should grow double-digit long term from there.

But what I would say, Meyer is, is as you think about the free cash flow growth long term, it's exceptional. We've delivered 13% CAGR in free cash flow over the last 12 years, and we'll continue to drive mid-single-digit or greater organic revenue growth, long term; margin expansion in 2023, 2024 and long-term and double-digit free cash flow growth long term. And we're really excited about our free cash flow growth long term.

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

Q

Okay. That's very helpful. Thank you.

Operator: Thank you. I would now like to turn the call back over to Greg Case, for closing remarks.

Gregory C. Case

Chief Executive Officer & Executive Director, Aon Plc

Just wanted to say thank you for everyone joining us. Look forward to our conversation next quarter. Thanks very much.

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