Blackstone Strikes Again: Blackstone to Acquire Aon Unit for $4.8bn

The Blackstone Group L.P. (NYSE: BX) - market cap as of 24/02/2017: $35.23bn
Aon plc (NYSE: AON) - market cap as of 24/02/2017: $30.67bn

Introduction

On February 10, 2017, Blackstone agreed to acquire Aon's employee benefits outsourcing unit for $4.8bn. Blackstone will pay $4.3bn in cash to Aon's shareholders, and an additional $500m based on future performance.

The deal is expected to improve Aon's return on invested capital as well as its 2018 earnings per share. Besides, the acquisition will allow the target to exit a mature business and focus more on growth, while Blackstone will receive ownership of a business that deals with the work benefits of 15% of the whole US population.

The deal is expected to close in the second quarter of 2017.

About Blackstone

Blackstone Group LP is an American leading company providing asset management and advisory services. It primarily manages private equity funds as well as proprietary hedge funds and mutual funds. The company was founded in 1985 in New York City. Its main business segments are: corporate private equity, real estate, marketable alternative asset management and financial advisory.

As a major financial sponsor and one of the world's leading investment firms, Blackstone deploys flexible capital to make sound investments for its shareholders while helping solve companies' problems. With more than $360bn assets under management Blackstone aims at making a positive impact while assuring extraordinary returns on its investments. In line with this policy, the deal is to be considered within the context of private equity firms assisting companies in cutting costs and outsource large part of their administrative operations in return for strong cash flows.

In 2016, Blackstone reported Sales for $5.13bn (a 10.3% increase with respect to 2015), an EBIT of $2.20bn, and a Net Income of $1.04bn (up 46.3% compared to the previous year). The company's EPS is at $1.56 and the dividend yield amounts to 7.14%.

About Aon

Aon Plc is a leading provider of insurance brokerage, reinsurance brokerage, risk management services, and human resource consulting and outsourcing. The company is the result of the 1982 merger between Ryan Insurance Group and Combined International Corporation, later introduced as Aon to Wall Street in 1987. With more than 72,000 colleagues globally, the company delivers effective risk management and human resource productivity solutions. Its innovative strategies are offered every day to clients throughout its more than 500 offices in over 120 countries all over the world.

Given its high profile and reliable reputation, Aon has managed through the years to fuel its growth by expanding in size through several acquisitions: in November 2008 Aon acquired reinsurance intermediary and capital advisor Benfield Group Limited for $1.75bn, and in 2010 Illinois-based Lincolnshire for $4.9bn, with the aim of amplifying its broking capabilities, and position itself as one of the largest players in the industry. The results of this aggressive growth strategy allowed Aon to be awarded no. 1 global insurance brokerage in 2009 and best insurance intermediary in 2010.

Aon's revenues in 2016 amounted to $11.63bn (almost stable with respect to 2015). The reported EBIT was $1.95bn, and Net Income $1.40bn (both figures fairly stables compared to the previous years of operations). The company's EPS is at $5.17 and its market cap is $30.67bn with around 263 million shares outstanding.

Deal structure

The private equity funds affiliated with Blackstone will pay a gross cash consideration of $4.3bn at closing, which is expected by Q2 2017, and additional cash amounting to about $500m, based on future performance.
For Aon, total after-tax cash proceeds from the sale are expected to be c. $3 billion, and the company announced it has planned to allocate part of this money for stock repurchase. This move, together with the increase of $5 billion in the buyback plan, aims at increasing shareholders' confidence in the stock, which has underperformed its peers in the past year.

The deal is expected to be accretive to Aon's adjusted EPS in 2018 and to increase the firm's return on invested capital: transaction proceeds, lower effective tax rate and additional savings from operations should make this possible.

Deal rationale

According to Peter Wallace, Senior MD at Blackstone, "Blackstone sees tremendous opportunity for investing in leading businesses within the technology-enabled services sector, where we believe there is a significant opportunity to accelerate future growth". Indeed, the acquisition of Aon's Benefits Administration and HR BPO platform is in line with Blackstone's mission of delivering first-class services to customers while innovating and expanding its service offering. In the context of this transaction, Blackstone will leverage its global relationships and solid capital base to eventually foster the business growth.

On the other hand, Greg Case, President and CEO of Aon, highlighted how the sale of the platform will create incremental capital to foster core operations' growth and will accelerate inorganic growth to meet emerging client needs, while keeping high quality standards. This transaction, together with Aon's acquisition of Stroz Friedberg and Admix and an annual investment of $350+ million in proprietary data and analytics, shows the firm's intention to deliver high-value solutions to clients and to strengthen its global footprint. The sale of the platform allows Aon to disregard the capital-intensive requirements of managing outsourcing platforms and to sharpen its focus on clients' Advice and Solutions. The new business arising from the transaction will operate under Blackstone's ownership and management, and will "reinforce Aon's position as the leading, global professional services firm focused on risk, retirement and health" – as Case added.

The transaction is expected to improve Aon's ROIC and to be accretive to adjusted EPS in 2018. These effects will be the direct consequence of deployed free cash flow from operations, transaction proceeds, improved savings from operations, and a lower effective tax rate. Part of the transaction proceeds will be allocated to increase Aon's share repurchases, according to prevailing market conditions and alternative uses of capital.

Market reaction

Aon's shares rose by 1.6% in the week following the deal announcement, but as of February 25, 2017, they are back to previous levels, trading at $115.85. On the contrary, Blackstone's stock has decreased by 3.3% from the $30.35 price per share of February 10, 2017. In both cases, however, the movement in share price has been minimal and likely unrelated to the transaction hereby analysed.

Advisors

Citigroup, Credit Suisse, and SMB Capital are financial advisors to Blackstone, whilst Morgan Stanley is acting as financial advisor to Aon. Bank of America Merrill Lynch, Barclays, Credit Suisse, Citigroup, Macquarie, Deutsche Bank, and Morgan Stanley are all providers of debt financing related to the transaction.