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Omnicom Group, Inc. (OMC)

Q4 2023 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good afternoon, and welcome to the Omnicom Fourth Quarter and Full Year 2023 Earnings Release Conference Call. At this time, all participants are in a listen-only mode. Later, we will conduct a question-and-answer session. [Operator Instructions] As a reminder, this conference call is being recorded.

At this time, I'd like to introduce you to your host for today's conference, Senior Vice President of Investor Relations, Gregory Lundberg. Please go ahead.

Gregory Lundberg

Senior Vice President-Investor Relations, Omnicom Group, Inc.

Thank you for joining our four quarter and full year 2023 earnings call. With me today are John Wren, Chairman and Chief Executive Officer; and Phil Angelastro, Executive Vice President and Chief Financial Officer. Also joining for the question-and-answer session will be Duncan Painter, CEO of Flywheel Digital; and Paolo Yuvienco, Omnicom Chief Technology Officer.

On our website, omnicomgroup.com is a press release and the presentation covering the information we'll review today as well as a webcast of this call. An archived version will be available when today's call concludes.

Before I start, I'd like to remind everyone to read the forward-looking statements and non-GAAP financial and other information that we have included at the end of our investor presentation. Certain of the statements made

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today may constitute forward-looking statements. And these statements are our present expectations. Relevant factors that could cause actual results to differ materially are listed in our earnings materials and in our SEC filings, including our 2022 Form 10-K and our 2023 10-K, which we expect to file shortly.

During the course of today's call, we will also discuss certain non-GAAP measures. You can find a reconciliation of these to the nearest comparable GAAP measures in the presentation materials. We'll begin the call with an overview of our business from John then Phil will review our financial results for the quarter. And after our prepared remarks, we'll open up the line for your questions.

I'll now hand the call over to John.

John D. Wren

Chairman & Chief Executive Officer, Omnicom Group, Inc.

Thank you, Greg. Good afternoon and thank you for joining us today for our fourth quarter and full year 2023 results. I'm pleased to report our fourth quarter performance was very strong. For the fourth quarter, organic growth of 4.4% exceeded our expectations and full year organic growth was 4.1%.

Excluding acquisition transaction fees related primarily to Flywheel, operating profit margin for the quarter was 16.3%. For the full year, operating profit margin adjusted for certain non-GAAP items was 15.2%.

Earnings per share for the quarter, adjusted for acquisition transaction fees was $2.20, up 5.3% versus the fourth quarter of 2022. For the full year, EPS adjusted for certain non-GAAP items was $7.41, an increase of 6.9% compared to the full year 2022.

In 2023, we generated approximately $1.9 billion in free cash flow and returned $1.1 billion to shareholders through dividends and share repurchases. Our liquidity and balance sheet remain very strong and continue to support our primary uses of cash – dividends, share repurchases and acquisitions.

On January 2, we closed the acquisition of Flywheel Digital. It is the biggest acquisition in Omnicom's history, and bring scaled capabilities in the fastest-growing segments of the industry – retail, media and digital commerce. Flywheel enables brands to sell goods across digital marketplaces such as Amazon, Walmart, Alibaba and more than 100 other marketplaces around the world.

Flywheel opens up an entirely new market opportunity for Omnicom, transforming us from an advertising and marketing-focused company to a marketing and sales-focused company. We can now seamlessly integrate end-to-end services from brand media to precision marketing to e-commerce and in-store commerce, ultimately delivering superior results for our clients.

In January, we began combining Omni's audience and behavioral data with marketplace point of purchase sales data in Flywheel's Commerce Cloud, giving us an unmatched set of data not only to more effectively drive sales for clients, but to be fully able to measure return on advertising spend. It's a unique offering that no one has been able to achieve and our competitors can't match.

I'm also proud to inform you that last week, Flywheel captured its first significant win as part of Omnicom, winning the highly-owned e-commerce business in Europe from one of our competitors. This is a unique partnership and opportunity. In January, we welcomed CEO, Duncan Painter and more than 2,000 Flywheelers around the world to Omnicom, and we are excited about what we can achieve for our clients together.

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In the fourth quarter, we acquired Coffee & TV, a UK-based creative studio that specializes in CGI and visual effects. The acquisition is part of our strategy to leverage the scale of our production operations and launch a holistic suite of global content and production services under a single unit, Omnicom Content Studios.

Omnicom Content Studios creates content for brands across all consumer experiences and touch points from long and short-form videos to social, experiential, digital and everything in between. In addition to these acquisitions, we continue to invest in high-growth areas through internal investments and partnerships.

Last month at CES, we introduced several new ways to offer planning and measurement in the booming area of influencers. We announced several first of a kind partnerships with TikTok, Google, Amazon and Meta to optimize the use of influencers, seamlessly integrate creator assets in campaigns, and measure influencer-driven commerce.

In November, we announced the first-mover collaboration with Getty Images that provides us early access to this new generative AI tool. It pairs Getty's library of creative content with Omni's data and AI technology. So our agencies can produce commercially safe and legally indemnified customized images for our clients.

In 2023, we launched Omni Assist, a virtual assistant our people use to create, plan and execute ad campaigns using the trove of data in Omni. Omni Assist accesses OpenAI's GPT models through Microsoft.

As the first holding company and second company overall to be given full access to OpenAI models in Microsoft's Azure environment, we have a significant first-mover advantage, allowing us to experiment, prototype and launch applications within our platform before any other organization.

Historically, we've invested tens of millions of dollars in AI. Going forward, Generative AI investments and partnerships to enhance our platforms and educate our knowledge workers are expected to require greater resources. These investments will result in increased productivity and success for our clients.

From e-commerce to influencers to Generative AI, we are investing in all the areas that will shape the future of our industry. When these capabilities are combined with our legendary creativity, we remain positioned at the forefront of change and innovation.

In new business, we had a very successful 2023. We secured record business with Amazon, Beiersdorf, HSBC, Jaguar, Land Rover, Novartis, Phillips, Telstra, Uber, Under Armour, Vans and Virgin Voyages among others. And we closed the year with exciting news that BMW consolidated its US creative, digital and CRM and its media accounts with us.

Before I discuss our outlook for 2024, I want to welcome the newest member of our board of directors, Casey Santos, who was recently appointed as an Independent Director and a member of the Finance Committee. Casey joins one of the most diverse boards within the Fortune 500. Now at 11 members, our Board is proud to have seven women and six diverse members. Casey's deep expertise in technology makes her a valuable addition to our board.

I also want to thank our people around the world for helping us successfully close out 2023. Your dedication and commitment to do outstanding work allow our agencies, clients and Omnicom to succeed.

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We entered 2024 from a position of strength, supported by our solid financial performance and balance sheet, new business wins, and key strategic investments in the areas that will drive significant growth in the years ahead.

While we continue to plan cautiously, given the uncertainties in the macroeconomic and geopolitical environment based on current marketing conditions, we are targeting a 2024 organic revenue growth between 3.5% to 5%.

Our range of organic growth during the year will be impacted by new business won in the fourth quarter which doesn't positively impact us until the second quarter and Flywheel's growth, which is typically stronger in the second half of the year.

I'll now turn the call over to Phil for a closer look at our financial results. Phil?

Philip J. Angelastro

Executive Vice President & Chief Financial Officer, Omnicom Group, Inc.

Thanks, John. We finished the year on a strong note in terms of revenue growth and profitability, even though the business environment was uncertain in 2023. As we look towards 2024, we're optimistic about the performance of our agencies and an improving economy. Let me spend a few minutes reviewing the financial details of the quarter, and then we'll open the lines up for questions and answers.

Let's start with a review of our revenue performance on slide 4. Organic growth in the quarter was 4.4%. The impact from foreign currency translation increased reported revenue by 1.2%. If rates stay where they are currently, we estimate the impact of foreign currency translation will be close to flat in Q1 2024 and for the full year.

The net impact of acquisition and disposition revenue on reported revenue was negative 0.7%, primarily reflecting the sale in Q2 of 2023 of our research businesses. In 2024, we expect a positive contribution beginning in the first quarter with an increase of about 1.5% and about 2% for the full year, reflecting recent acquisitions and our having moved past recent dispositions.

For the full year, organic revenue growth was 4.1%. This was in line with our revised guidance of 3.5% to 5%. We made some good progress toward this target despite a challenging comparison to 9.4% growth in 2022 and an uncertain macroeconomic environment during the year. As John discussed, organic revenue growth outlook for the full year 2024 is between 3.5% and 5%.

Now, let's turn to slide 5 to review our organic revenue growth by discipline. During the quarter, Advertising and Media growth was very strong at 9.3%, once again driven by global media performance which was partially offset by softer results from our advertising agencies.

Precision Marketing growth contracted 1.1%, reflecting a difficult comp to 11.5% growth in Q4 of 2022 and cycling some client spending reductions from earlier in the year. As we look forward to 2024, we expect this to once again be one of our fastest-growing disciplines. Commerce & Branding grew by 1% compared to growth of 7.5% last year driven primarily by growth in specialty production to offset reductions in the quarter at our branding and commerce agencies.

Experiential was down 8%, reflecting a difficult comp of 17% growth in Q4 of 2022 with the FIFA World Cup in Qatar, primarily offset by strong growth in Europe in the quarter. While quarterly results can be choppy based on

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the timing of certain client events, Experiential remains a solid business and is important to our clients' marketing plans.

Execution & Support declined by 0.4% with mixed results that included a solid performance in field marketing. Public relations declined 2.9% in the quarter due to difficult comps related to the US midterm elections of 2022 when growth exceeded 12% as well as softness in certain international markets. Finally, Healthcare continued its steady growth of 3.6% during the quarter.

Turning to geographic growth on slide 6. We saw growth in our five largest markets offset again by declines in Canada and the cyclical impact of experiential revenue in Middle East and Africa. The US was up 0.6% in the quarter on solid performances by Advertising & Media, led by media and our healthcare businesses, offset primarily by Execution & Support, Public Relations and Commerce & Branding.

Slide 7 shows our revenue by industry sector for the full year and the quarter. Looking at the full year, which tends to eliminate the volatility of client changes in the quarter, we saw a notable increase of 2 points in automotive and 1 point increases in both food and beverage and financial services. Weaker markets in technology and entertainment, which have been discussed widely in the industry over the course of the year, resulted in reductions of 3 points and 1 point, respectively.

Now, let's turn to slide 8 for a look at our expenses. In the fourth quarter, salary and related service costs were higher due to increased staffing levels but were down as a percentage of revenue year-over-year driven by our repositioning actions earlier in the year and through ongoing changes in our global employee mix.

Third-party service costs increased in connection with the growth in our revenues. We generated profit on these costs and the higher levels in the fourth quarter of 2023 compared to 2022 were driven primarily by strong growth in our media business. Our disposition activity during the quarter and the year did not have much of an impact on this cost category. Third-party incidental costs were close to the same level as last year and reflect client-related travel and incidental out-of-pocket costs that are billed to clients directly at our cost with no profit.

Occupancy and other costs were down in both dollar amount and relative to revenue driven by ongoing rationalizations in our real estate portfolio. SG&A expenses were up primarily due to $14.5 million in professional fees related to acquisition costs incurred in the quarter, the majority of which related to Flywheel. Excluding these costs, quarterly SG&A levels were comparable to last year.

Now let's turn to slide 9 and look at our quarterly and annual income statement. To make the numbers more comparable, the table and footnotes describe some of the other adjustments that were made during this year and last year that we discussed on prior calls.

Our operating income margin was negatively impacted by $14.5 million of costs in connection with the Flywheel acquisition as I just discussed. Adjusting for this amount results in an operating income margin of 16.3% and an EBITDA margin of 16.8%.

For the full year, our adjusted operating income margin was 15.2%, within our expected range of 15% to 15.4%. As a result of the Flywheel acquisition, we'll have higher levels of amortization expense than past years and we will be focusing our margin expectations on EBITA.

We continue to expect integration costs as well as operating synergies related to the Flywheel acquisition during 2024 and the acquisition will be accretive to diluted EPS adjusted for amortization expense by the fourth quarter.

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For the full year 2024, we expect adjusted EBITA, as a percentage of reported revenue, to be close to flat with last year. Also in this slide, you can see that our non-GAAP adjusted income tax rate of 26% for the full year 2023 was comparable to 2022.

We do not expect the Flywheel business to change our tax rate outlook for 2024 but the 2024 rate will be negatively impacted primarily related to increases in the statutory rates of certain international countries. For full year 2024, we expect our rateour to approximate 27%.

Acquisition costs related to Flywheel and better performance at agencies with minority shareholders contributed to a decrease in reported net income of 1%, but an increase of 2.1% on an adjusted basis. Lastly, adjusted diluted EPS of $2.20 for the fourth quarter increased 5.3% from last year. For the year, adjusted EPS increased by 6.9%.

Slide 10 is our cash flow performance for the year. We define free cash flow as net cash provided by operating activities excluding changes in operating capital. Free cash flow for 2023 was $1.9 billion, an increase of 6.5%.

This increase was driven in part from operational improvements compared to 2022 and the use of operating capital which we expect to improve further in the future. Regarding our uses of cash, we used $563 million of cash to pay dividends to common shareholders and another $71 million for dividends and non-controlling interest shareholders.

Our capital expenditures were $78 million, similar to last year. We expect 2024 levels to be higher due to growth investments at Flywheel. Total acquisition payments were $249 million. Although we closed the Flywheel acquisition on January 2, 2024, using cash on hand of approximately $845 million, it remains our intention, as we stated in the October 30 announcement, to finance two-thirds of the purchase price with new debt which I'll discuss in a moment.

Finally, our stock repurchase activity, net of proceeds from stock plans, was $535 million year-to-date, within our expected range. Our capital allocation in 2024 will be consistent with our practice of returning cash to shareholders through a healthy dividend, making strategic acquisitions that lead to accelerated growth and using a portion of residual cash to repurchase common stock. Since 2024 began with the closing of a larger-than-normal acquisition, we expect the total share repurchases in 2024 will approximate 50% of our recent average.

Slide 11 is a summary of our credit, liquidity and debt maturities. At the end of the fourth quarter of 2023, the book value of our outstanding debt was $5.6 billion. There were no changes in outstanding balances during the quarter other than foreign exchange translations. Our $2.5 billion revolving credit facility, which backstops our $2 billion US commercial paper program, remains undrawn, and our cash equivalents and short-term investments were $4.4 billion.

We will continue to monitor the credit markets throughout 2024, and we expect to enter the debt markets to finance approximately $550 million or two-thirds of the $845 million we spent on the Flywheel acquisition. And during the year, we will refinance the $750 million of 3.625% senior notes which are due November 1, 2024.

Financing the Flywheel acquisition will increase our interest expense in 2024. It's also likely that refinancing November notes will increase interest expense by some amount, but it is too early to estimate. For 2024, we expect that our internal financing of the Flywheel acquisition in early January with cash on hand prior to an expected financing of two-thirds of the purchase price, coupled with a decline in global interest rates, will lead to lower interest income in 2024 compared to 2023.

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Slide 12 presents our historical returns on two important performance metrics for the 12 months ended December 31, 2023. Omnicom's return on invested capital is 26% and return on equity is 41%, both reflecting very strong performance. Healthy returns like these reflect the strength of our industry, our operating discipline and the preservation of our conservative balance sheet.

Operator, please open the lines up for questions and answers. Thank you.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Our first question comes from the line of Cameron McVeigh with Morgan Stanley. Please go ahead.

Cameron McVeigh
Analyst, Morgan Stanley & Co. LLC

Q

How are you guys thinking about the cadence of growth in margins over the course of 2024 from what you can see now, the comps ease as the year progresses and you have the Summer Olympics and the US election in November? So curious any color you can provide on how you expect the year to shape up. Thanks. And then I have a follow-up.

John D. Wren
Chairman & Chief Executive Officer, Omnicom Group, Inc.

A

Sure. Well, the comps in the first quarter remain probably the most difficult comps that we have going into the year, but it's not that as much as it is Flywheel which we closed on January 2 is just seasonally natural at least stronger in the second half than the first. So that's one point. And as I said in my prepared remarks, a number of the new business wins we had late in the third quarter, early in the fourth quarter or throughout the fourth quarter, whilst we won them and we have to ramp up our expenses in order to handle them with the notice periods, the companies that lost those accounts, we don't start getting revenue really until the second quarter or so. So, the additive tailwind for that won't happen until then.

You're absolutely correct that as we go through the year, if all goes well, the Olympics will add something to the revenue as will the US elections add something as we get a little bit later into the second quarter than the third quarter. And there'll be a tail to it also in the fourth quarter. So, that's kind of reflected in the range that we have given you, and we want to emphasize that whilst we expect this to ramp, it didn't start ramping on January 1.

Philip J. Angelastro
Executive Vice President & Chief Financial Officer, Omnicom Group, Inc.

A

Yeah. I think I would just add that, I think it's probably logical our margin expectations would kind of mirror that as the year goes on. And as performance builds, as John had said, you'll see some consistency in the performance of the margins.

Cameron McVeigh
Analyst, Morgan Stanley & Co. LLC

Q

Great. Makes sense. And a question for Duncan. As you ran Ascential and built Flywheel, what are you excited about now that you're part of Omnicom, I'd love your thoughts.

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Duncan Anthony Painter
Chief Executive Officer, Flywheel Digital

A

Yes. So well, firstly, Cameron, it's a pleasure to be here on the call and I'm delighted to be part of the leadership group at Omnicom. We had the chance to work alongside Omnicom for a long time for me 12 years.

And we always admired the pride and the quality that they focus on, always leading with the best-in-class quality products and services in the market. It was always very, very clear and having built a platform in Flywheel that focused on exactly the same, that was very important to us.

And since we've been here, it's really clear how this company really focuses on high-quality products and great service to customers. So there's a natural fit there. That all saying, form is temporary, but class is permanent, is showing in the company.

The other thing from our side is, we really do think the scale of clients and the very early engagement we've already had with the clients that Omnicom has where they clearly have very trusted relationships with them is giving us great access to not just maintain our growth rates but to have some sense that we've got a chance to accelerate them, and that's exciting for us. And we're great to see that come through, and just the quality of our ability to just expand across a range of really high-quality clients.

And then finally, and perhaps the most exciting for us and the thing that we – that John alluded to in his presentation is that there's no doubt from our diligence of Omni, it's a modern next-generation platform that has, by far, the largest scale trading data on the marketing side and having built on the Flywheel side, the biggest trading data platform on the marketplaces, we're really excited about the ability to combine that information. We think it's a unique opportunity and it really is for the first time ever going to give clients the real ability to measure marketing sales in one go. So that's definitely the most exciting element we see.

Cameron McVeigh
Analyst, Morgan Stanley & Co. LLC

Q

That's great. Thank you.

Operator: Next question will come from the line of David Karnovsky with JPMorgan. Please go ahead.

David Karnovsky
Analyst, JPMorgan Securities LLC

Q

Thanks for taking the question. John, some of your peers have pushed AI to the front of conversations recently and highlighted potential competitive advantages around data or tech. I'm interested, first, do you think as AI is integrated into the holding companies that real differentiation and execution is going to emerge that will be visible to clients? And then secondly, for Omnicom, how do you think about the time line of moving from testing AI capabilities to deploying it in a way that is going to be visible to investors on the top line or in cost?

John D. Wren
Chairman & Chief Executive Officer, Omnicom Group, Inc.

A

Sure. There's a lot there. First of all, AI is just AI. We've been investing in that for close to a decade. More seriously in the last five years, you see it reflected in Omni Assist. What they're really talking about is the impact of Generative AI, I think, and what it's going to do to the entire landscape. And we've taken a view that it's going to

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make us more productive and make what I refer to as our knowledge workers better, faster, able to come up with better answers and insights for our clients.

It's unknown territory. One of the immediate concerns we had, and it's reflected in comments that I made earlier and it was released in November, when you look at AI and technology always travels faster than society's ability to absorb it and the laws and regulations that generally follow it. So making certain that we don't expose our clients to anything that can be – create a problem because it was handled improperly is key. And the first move we made there was entering into a deal with Getty images. So we're capable of accessing those and teaching our programs and platforms how to utilize that in a fast and efficient way.

And more of those type of arrangements are going to occur as we go forward. Also, I think because governments will be late in catching up with how they want to protect the consumer, we're going to have to tread very carefully. So I think our ability to do things will exceed whether or not we will use them to do things. And we're going to put the clients' interest and safety above all in that consideration set.

In terms of the Beta-ing of products and things that we're doing, we already have a few clients who we're Beta-ing products with, who are very aware of the risks associated with it that we're going to break a few things, we're going to – but at the end of the day, we're going to create a better, more efficient way.

I'm going to throw the question to somebody who's sitting here as well. My colleague, Paolo, who has been, first and foremost, and heads committees that look at this. So, Paolo?

Paolo Yuvienco
Executive Vice President & Chief Technology Officer, Omnicom Group, Inc.

A

Hey, David. Thanks for the question. So just to get back to the first part of your question, I think the short answer is, yes. And it's precisely the reason why artificial intelligence has been pervasively deployed across our industry-leading operating system, Omni, since we created it well over five years ago. And more specifically around Generative AI, we spent the last 18 months working with really the titans in enterprise-ready Generative AI including the likes of Microsoft, Google, Amazon, Adobe, John mentioned Getty. We're having – we've had first mover advantage with all of these partners really in testing and integrating their models to change and optimize the way we are delivering outcomes for our clients. So with over 50,000 people across Omnicom, both clients and our employees kind of using and have been provisioned access to Omni, we've already started to bring these capabilities to life, as John mentioned, on several clients and select accounts.

And actually, to the second part of your question, we've actually launched these capabilities back in June of 2023 with Omni Assist. Omni Assist is utilizing those large language models, those diffusion models. And they're already starting to make the jobs of our people easier and, frankly, the work for our clients better.

David Karnovsky
Analyst, JPMorgan Securities LLC

Q

Great. Thanks. And then maybe one more. Just on the technology vertical, it's been a headwind across the industry for some time now. I think there's been some investor optimism that this could improve with easier comps for the year, at the same time, we keep seeing layoffs in the technology space. I know it's been generally less an issue for Omnicom, but interested to know what you're seeing here and whether there's any read-through to business lines like Precision Marketing.

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John D. Wren
Chairman & Chief Executive Officer, Omnicom Group, Inc.

A

Certainly, there'll be easier comps. But as you suggest, I don't think in our prior calls we've been moaning too much about the impact that technology has had whereas I think our competitors have had much greater hits, which probably means that have much easier comps going forward. But, yes, we expected an uplift from the base of technology clients that we have in the forecast as it rolls through the rest of the year.

David Karnovsky
Analyst, JPMorgan Securities LLC

Q

Okay.

Operator: And the next question comes from the line of Adam Berlin with UBS. Please go ahead.

Adam Berlin
Analyst, UBS AG (London Branch)

Q

Hi. Good evening. I'll ask two questions, if I can. The first one is, can you say a bit more about why Advertising & Media was so strong in the fourth quarter? Was it to do with account wins? Can you quantify how big the account wins were? And can you say something about how much was media and how much was creative within that segment? Thanks.

John D. Wren
Chairman & Chief Executive Officer, Omnicom Group, Inc.

A

Well, I'll answer the second part of your question first. Media certainly was stronger than advertising, but we choose to treat it as one reporting entity when we put both of those numbers together because quite often they've come together. More specific than that, I don't think it's a productive way to look at the business.

Yes, there are a lot of strength in the fourth quarter in media. There are a great number of projects and spending that was conservatively held back and then released into the fourth quarter, and we benefited from it as you can see in the numbers. And I would say that was through the West including Western Europe.

Adam Berlin
Analyst, UBS AG (London Branch)

Q

And can I ask one more question then about working capital. I know you exclude it from your free cash flow but it was still quite a large number, $460-so million. Do you expect that to come down in 2024? Or can you say a little bit about why it's still so high?

Philip J. Angelastro
Executive Vice President & Chief Financial Officer, Omnicom Group, Inc.

A

Sure. For the year, certainly, the change in working capital was positive, almost a $400 million improvement which we're pretty satisfied with. I think relatively speaking though, the overall negative reflects the fact that the actions of the Fed and, over time, global treasuries have obviously made it a more challenging area to manage.

I think the fact that we cut the change in half or we cut the number in half in 2023 is really reflective of good performance all throughout the organization. It's really a matter of three yards and a cloud of dust in terms of blocking and tackling to improve those numbers. We're certainly going to strive to get the number back to neutral, if not positive, as we go, but that isn't going to happen overnight.

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I think as the economic environment changes and as the rates eventually come down, I think you'll see some continued improvement. It's certainly an area we're very focused on and we're not done in terms of improving our performance. But it has been more challenging in the last few years than in the past.

Adam Berlin
Analyst, UBS AG (London Branch)

Q

Thank you very much.

Philip J. Angelastro
Executive Vice President & Chief Financial Officer, Omnicom Group, Inc.

A

Sure.

Operator: And the next question comes from the line of Steven Cahall with Wells Fargo. Please go ahead.

Steven Cahall
Analyst, Wells Fargo Securities LLC

Q

Thanks. Maybe the first just to expand on the question around Advertising & Media. So, I think you talked about how creative has been lagging, and then you've had a lot of strength in media, and you've definitely showed off strong capability there and won a lot of business.

John, I'm just wondering if there's anything bigger to read about how the industry is changing and the acceleration in media with the slowdown in creative. Do you think that's a change in the way marketers just think about the future of marketing and marketing spend, as much more about the delivery than the content? And if so, are there any other changes that you might think about to your business longer term if that is, in fact, the case?

And then just in Q4, your organic growth was pretty similar to what you've guided to for 2024. The EBIT margins were solid. They weren't necessarily up year-on-year. I know there's a lot of moving pieces then this year with Flywheel. But can you just talk about what's holding those margins a little flattish, like the guidance that you gave? And is there anything that could drive more margin expansion in the future? Thank you.

John D. Wren
Chairman & Chief Executive Officer, Omnicom Group, Inc.

A

Sure. There's a lot there. You bring up an interesting point, and I probably won't do justice to it in my response. But creative is our IP at the end of the day. What you see in a reflection or your guess as to the impact on the way that the business has been organized and then reported, what you see is technology has probably had a greater impact on the traditional setup of an agency in terms of how we can utilize great ideas and through algorithms and through automation deliver those ideas to the right venue to present them to reach customers. And so that has an impact. That, in fact, is why we don't separate the two because they feed off each other. But I think one of the things that has always differentiated us is actually the quality of our creative products and the quality of our agencies and people that we're able to attract. And that's not to be diminished because some is trying to do an analysis which doesn't – is not really reflective of what we're trying to accomplish.

And so you do have to look at them jointly. And we fully expect that it's going to continue to shift but to our benefit, as we bring other technologies and benefits to the client because any time we can save $1 and prove that we've saved it effectively for a client, it's been my experience that the client expands their relationship with us. So I'm

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very confident about that. I would never want to lose that creative IP because of shift in the way that I'm organized. The second question...

Philip J. Angelastro
Executive Vice President & Chief Financial Officer, Omnicom Group, Inc.
A

Yes, I'll give [indiscernible] (00:41:13) on margins and expectations. I think as we've said in the past, we certainly strive over time to make steady progress on margins and make improvements. Certainly, in our two of our largest expenses, salary and service costs and occupancy and other, we see future opportunities. Certainly, on the salary-related side, there's still quite a few initiatives – we have benefit from offshoring and automation. There are strong initiatives that we're pushing, and we'll continue to push in those areas. And we continue to go through a real estate rationalization and expect to benefit from that over time as well, and we continue to make some improvements there.

I think, however, we talked a lot about AI on this call. That will be part of what helps us be more efficient and generate some of these benefits. But at the same time, it requires investments that we're going to continue to make in the business that, as we've talked about in the past, many of the investments we've made have run through the P&L. It's the right thing to do to make sure that our platforms are ready to give us the sustainable growth that we've been able to achieve and expect to achieve in the future.

So it's a continual balance that we go through in terms of making those investments and generating the appropriate returns from a margin perspective and benefits for our shareholders ultimately as well. So I think that's a balance that we continue to manage. We look at it every year. We look at it every day. It's both. So hopefully, that's helpful.

Steven Cahall
Analyst, Wells Fargo Securities LLC
Q

Thank you.

Operator: And the next question comes from the line of Michael Nathanson with MoffettNathanson. Please go ahead.

Michael Brian Nathanson
Analyst, MoffettNathanson LLC
Q

Thanks. I have one for Duncan and John and one for Phil. Duncan, can you give us a sense of your client mix, you see Omnicom listed – kind of you know their clients and their exposures. Can you talk a bit of your biggest clients or verticals you serve? And then John, this is a big deal to you obviously. Anything you can say about channel conflict, client conflict when you look at Duncan's list and yours and perhaps either the ability to upsell your common list of clients or any kind of challenges? And then Phil, over the years, we've asked you about media and then third-party service costs. This quarter looks like you grew media or the media line very, very quickly organically. But your service costs were actually pretty flat on a constant currency basis. Can you talk a bit about what's happening on the ground on margin when you dig into that sector between organic and service costs? Thanks.

John D. Wren
Chairman & Chief Executive Officer, Omnicom Group, Inc.
A

Sure. Conflicts really are not. It's been quite a while since it really has become a topic or an item that concerns us. Most clients are very sophisticated these days and they're more interested in the teams of people that are

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servicing them on a consistent basis. And I think you'd see this experience throughout the industry have been able to cope very comfortably with that because those people never meet, it's only at the holding company level that they get consolidated.

With respect to sectors, there will be challenges and all, and there will be benefits in some, and some will have low comps, and some will have more difficult comps. The one area that has never been strong or as strong maybe as it could be for Omnicom is in CPG. And I think that with changes that we made first to the Commerce Group in terms of leadership, and then with the addition of Flywheel and the expertise that it brings, Omnicom now has thousands of more people who are confident in addressing the needs of CPG type of clients. And I think we'll be more competitive than we've been historically in that area as a result. So I'm very excited about that. I don't know if Phil is doing the second question.

Philip J. Angelastro
Executive Vice President & Chief Financial Officer, Omnicom Group, Inc.
A

I think maybe, Duncan, if we turn it over to you first, if you want to comment on – or add some commentary on your side.

Duncan Anthony Painter
Chief Executive Officer, Flywheel Digital
A

Yeah. So yeah, thanks for the question. Flywheel has always been very strong in CPG. We serve already 50 of the top 100, and we're already seeing opportunities for us to combine, as John says, both our capabilities and Omnicom's capabilities to further enhance those clients' experiences. And also Omnicom does have a client mix that helps us expand into a number of the other CPGs we haven't served. So it's – there's a good combination there. But actually, what's exciting for us is other categories where we've seen strong potential over time and Omnicom are very strong. And clearly, electronics is a big area. Tech and electronics, Omnicom has very good relationships there and primarily with the high-quality providers in those customers in those segments certainly, our ability to now work with potentially a number of the top 20 brands that actually sell through Amazon, for example, is very exciting.

And then in addition to that, opportunities that are definitely coming through the business transformations for these industries, particularly around areas like automotive, where if you look at the secondary parts markets and secondary service markets of automotive, marketplaces are becoming – it's one of the fastest growth segments in marketplaces. And of course, Omnicom is perfectly positioned to position us in with those kind of organizations trying to work out how they really maximize that opportunity. So yes, we can see both strength in our existing segments but actually opening up beautifully some new segments for us.

Philip J. Angelastro
Executive Vice President & Chief Financial Officer, Omnicom Group, Inc.
A

And then on your last question, I think certainly, media experienced very strong growth in the fourth quarter and had a great year. That growth was pretty consistent and strong across most of the media businesses and agencies we have in most markets for a number of reasons. And certainly, some of what you see in third-party service costs is a result of the gross media businesses performing well also. There is a bit of a mix difference between those businesses within our media operation but they complement each other quite nicely. And I think we certainly have an offering that clients are very attracted to and find very helpful and useful and valuable to meet their needs.

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Michael Brian Nathanson
Analyst, MoffettNathanson LLC

Q

Thank you.

Operator: And our next question comes from the line of Tim Nollen with Macquarie. Please go ahead.

Tim Nollen
Analyst, Macquarie Capital (USA), Inc.

Q

Hi, everyone. Thanks very much. I've got a numbers question and a broader question as well. The numbers question is, if you could please comment a bit further on the shift in growth rates between the US slowing in Q4 and a lot of international markets, it looks like accelerating Europe, Asia Pac. Just kind of curious, I heard what you said about the US side, just maybe a bit more color on that. And then why conversely some of those international markets have accelerated year-over-year?

And then the broader question is about cookie deprecation and all the changes that Google is perhaps bringing about this year. I just wonder what your take is on the likelihood of cookies ending up being fully deprecated by year-end or some of the recent news flow is perhaps holding up progress there and just curious how engaged Omnicom agencies may be in the Privacy Sandbox. Thanks.

John D. Wren
Chairman & Chief Executive Officer, Omnicom Group, Inc.

A

Sure. When you look at where the strength was, the fourth quarter really has three components to it. It's clients releasing projects, new business wins and its impact, and then if you've lost anything where you're feeling that impact as you net down to what we report as organic growth. I'd say that – the project work came in very strong, stronger than we expected in some parts of Western Europe. And we have a thesis about why, but it's certainly not something we planned for. It came in decently in North America. But North America, is where we were cycling through a number of losses that occurred in the advertising sector over a year ago.

And when you lose something that's bad news, but then you have to live with it as you cycle through it. So all that is the alchemy of how you get to organic growth and as a result, that makes us – we're still cautious about this year because of all the unrest and the Fed hasn't really started reducing rates yet. But in terms of what issues we had, they're for the most part, behind us. And some of the new business wins have not – we haven't started benefiting from yet. So I'm very comfortable that 2024 will probably wind up looking more traditional than 2023 did. In terms of cookie deprecation, that's something we've been fully expecting for a very long time, but I could chat about it, but I'm going to throw it to Paolo because he's more of an expert and more closely deals with it on a day-to-day basis.

Paolo Yuvienco
Executive Vice President & Chief Technology Officer, Omnicom Group, Inc.

A

Yeah. So as John said, we have been expecting it for a very long time. And to predict if it's going to actually happen at the end of this year, I mean, frankly, your guess is as good as ours, but we've been preparing for it, and we're ready for it. In fact, Omni has been purpose-built to actually address a cookie-less world just with respect to third-party cookies on Google.

So in addition to that, we've been preparing in other ways like some of the deals that we've struck with clean rooms and the integration into various clean rooms that are helping us to facilitate first-party data. And then, of

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course, the acquisition of Flywheel and all the data that they bring directly from the marketplaces, that is helping to drive a better understanding of consumers without the need of those third-party cookies.

Operator: And the next question comes from the line of Craig Huber with Huber Research Partners. Please go ahead.

Craig Huber
Analyst, Huber Research Partners LLC

Q

Great. Thank you. John, I wanted to hear your thoughts, if I could, on two sectors: your pharmaceutical healthcare area, what your outlook is for this upcoming year. It's obviously been very steady growth for a number of years. And also your thoughts on the auto sector. It looks like you had a very good year last year. You won the BMW account recently and stuff. How optimistic are you about auto sector for you guys this upcoming year? And I have a follow-up for Phil. Thank you.

John D. Wren
Chairman & Chief Executive Officer, Omnicom Group, Inc.

A

Sure. Pharma, we remain very optimistic on. The only headwind I think we face as we go into 2024 with Pharma was earlier in the year, we lost Pfizer, so we'll be cycling through that. But the only limitations we are currently looking through, not things that we haven't won or we haven't been asked to work on, but have they gotten through the FDA. Because pharma and just the simple science of things and the advances that are occurring give us tremendous opportunities to continue to grow. And I think that'll be not only 2024, but 2024 and beyond a very strong sector for us.

Autos, what it comes down to is we're very well-represented in autos, and I think we have the best clients one could ask in the sector. There is this tension going on in the marketplace that most auto OEMs are dealing with in terms of what's the mix between the electric cars that we're going to put out in the market, more conventional cars, and hybrid. And there's a lot of decision-making and a lot of long lead times that go into that. But in terms of the sector itself, there's no question. It becomes an information platform for the OEMs as we go forward and the more, the merrier from my perspective.

And as Duncan mentioned, now with the addition of Flywheel, there was a whole sector of aftersales parts that we could do a modest job on, but now we can do a much more robust job when you look through how those goods are distributed to the ultimate consumer, which is, in many cases and increasingly in marketplaces. So it's been a strong sector. It should even get stronger for us as we extend to that over the coming months and years, and we're very comfortable with it.

Craig Huber
Analyst, Huber Research Partners LLC

Q

And then, Phil, if I could just ask two quick housekeeping things. How would you sum up how your project-related work did for the whole company in the fourth quarter versus a year ago? And then a nitpick question, your amortization for a number of quarters here has been sitting around $20 million. How much do you think it's going to go up here with this Flywheel acquisition? Do you have that handy?

Philip J. Angelastro
Executive Vice President & Chief Financial Officer, Omnicom Group, Inc.

A

We don't have the final number because there's a number of steps that we have to complete, given the acquisition just closed in early January. So we have some valuations and other things to do on the intangible

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assets, which aren't complete. I would say it's going to be a meaningful increase, no question in amortization expense. And we obviously think the value of the Flywheel asset and team are going to prove to be a very wise investment. But amortization is going to go up in a meaningful way. We just don't have a number yet to guide you with, but that's something we're working through and we'll be working through quite diligently over the next few weeks and months before we finalize it.

And then as far as project spend goes, I think similar to Q4 of 2022, project spend was quite strong but probably not as strong as 2022. 2022, for sure, was a much more robust timeframe. I think when we were – when we were having discussions in late 2022 and early 2023 and probably on our call in February of 2023. Yeah, there were a lot of clouds that people saw on the horizon in the short term that actually turned out not to be as dark as some had expected. But the fourth quarter environment in 2022 is certainly much more robust than it was this year. But we're happy with the performance of our agencies as far as capturing project spend in Q4 of 2023. But relative to 2022, certainly 2022 is more robust.

John D. Wren
Chairman & Chief Executive Officer, Omnicom Group, Inc.

A

And don't lose sight of the fact that in 2024 as we get into it, we do have the Olympics. We do have a presidential election, and it's been my experience that presidential election years are generally very good one way or the other for the economy, and there gets to be some tension in the media marketplaces, especially in the US as you get later in the year. So that makes people – forces people to make decisions sooner. And if the Fed comes through and starts to cut, that will be the beginning of, I think, fuel to aid in the outcomes that I just suggested will be there. So we're cautious, but we are optimistic.

Craig Huber
Analyst, Huber Research Partners LLC

Q

Great. Thank you, both.

Operator: And with that, at this time, there are no other further questions. That does conclude our conference for today. Thank you for your participation and for using AT&T conferencing service. You may now disconnect.

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