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Omnicom Group, Inc. (OMC)

Q1 2024 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good afternoon, and welcome to the Omnicom First Quarter 2024 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 – 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 first quarter 2024 earnings call. With me today are John Wren, Chairman and Chief Executive Officer; and Phil Angelastro, Executive Vice President and Chief Financial Officer.

On our website, omnicomgroup.com, you'll find a press release and the presentation covering the information we'll review today. An archived webcast will be available when today's call concludes.

Before we 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 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 2023 Form 10-K.

During the course of today's call, we will also discuss certain non-GAAP measures. You can find the reconciliation of these to the nearest comparable GAAP measures in the presentation materials.

We will 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 will open up the line for your questions.

And 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 on our first quarter 2024 results. I'm pleased to report that we're off to a solid start to the year. Organic growth in the first quarter was 4% with strong growth in our advertising and media and precision marketing disciplines.

EBITA margin, which excludes amortization of acquired and strategic platform intangibles, was 13.8% for the quarter and operating margin was 13.2%. Non-GAAP adjusted earnings per share, which excludes after-tax amortization of acquired and strategic platform intangibles was $1.67, up 3.7% versus the comparable number in Q1 2023. As a result of our strong performance in the first quarter, we are increasing our full year organic growth range to between 4% and 5%.

As discussed during the quarter, we raised €600 million through a senior note offering to partially finance the acquisition of Flywheel. Our cash flow and balance sheet remain very strong and support our primary uses of cash flow: dividends, acquisitions, and share repurchases.

The Flywheel acquisition is off to a great start. Flywheel's Commerce Cloud is fully integrated into Omni. Omni audience and behavioral data, combined with Flywheel's digital marketplace point of purchase transaction data provide us with the most comprehensive dataset in the industry.

Across several significant Omnicom clients, Flywheel teams are now fully engaged to deliver the enhanced value of our combined capabilities and insights to them, including new ways to plan and build audiences using Omni audience data and Flywheel's performance benchmarks plus funnel investment management built on Omni and enhanced with Flywheel's data specific to performance across commerce platforms.

Using Omni influencer capabilities and connecting them to commerce and retail outcomes from Flywheel and holistic video measurement and optimization based upon integrating Omni's video viewership data with Flywheel's commerce outcomes. These products and services are helping our clients sell more goods more efficiently across hundreds of digital marketplaces and optimizing their investment across media platforms.

In addition to integrating Flywheel Commerce Cloud, we made important updates to Omni's generative AI functionality during the quarter. This includes completing a first-mover partnership with Shutterstock that allows us to integrate its text to image model into Omni. As part of our first-mover partnership established with Google and their Vertex AI platform last year, we became the first holding company to receive access to the Gemini 1.5 next-generation model. We remain committed to Omni's open architecture and flexibility, leveraging these valuable partnerships.

We've seen notable traction with Omni Assist, the generative AI tool we launched in 2023. Employees from more than 40 markets globally have access to Omni Assist and using it to produce audience intelligence, summarize cultural trends, recommend influencers and much more. Some of our agency teams are also creating client-specific Omni Assist agents. For example, a client dedicated marketing consultant, media consultant and briefing agent to streamline global, multi-brand client agency planning. As we work alongside our clients to explore how these new technologies can transform their businesses, two areas are critical to how we can drive transformation and growth: our digital transformation consulting business and our content production capabilities.

This past month, our highly successful consulting firm, Credera, announced the simplification of its organization to offer clients a more streamlined experience. Its services will now be delivered under a single global brand through two primary business units: Digital with capabilities in MarTech eCommerce and digital platforms, and Consulting with capabilities in management and technology consulting, data, AI and business transformation.

Since joining Omnicom in 2018, Credera has grown from 300 employees in three US offices to over 4,000 people across 17 locations worldwide. This growth is a testament to our track record and success in acquiring and integrating businesses in new high growth market segments. Today, our clients demand more high-quality, personalized creative content delivered across more media channels and at faster speeds. We have developed standardized platforms and processes to automate the development of content and deliver it at the right time and place to consumers by combining Credera's expertise in designing and implementing intelligent content platforms leveraging our Adobe partnership, ArtBot, our content orchestration engine, and Omni's audience and data insights. Our solution provides unmatched outcomes through an open operating system, fueled by customer centricity to some of our most important brands, such as AT&T and Nike.

I'm pleased that our strategy resulted in industry recognition in the first quarter, including Omnicom being named WARC's number one holding company for effectiveness, PHD being recognized as Adweek's Global Media Agency of the Year, Omnicom Media Group being RECMA's leading global media agency for 2023 with nearly $3 billion in net new business. Although risks and uncertainty continue to exist in the global economic and geopolitical environment, we remain optimistic about our position in the industry, our strategies, and our financial performance. I remain confident that our management teams are well-prepared to drive operational excellence even as they monitor and adapt to the changes in the macro environment.

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 began the year with solid results and we're optimistic about the year ahead. Let's review the first quarter performance in detail, beginning with revenue on slide 4. Organic growth in the quarter was 4%. The impact from foreign currency was relatively flat, decreasing reported revenue by 0.1%. If rates stay where they are currently, we estimate the impact of foreign currency translation will be negative 1% for Q2 2024 and flat for the full year 2024.

The net impact of acquisition and disposition revenue on reported revenue was positive 1.5% due primarily to the acquisition of Flywheel this January. Based on transactions completed to date, we expect a positive contribution of approximately 2.5% for Q2 and 2% for the year.

Now, let's turn to slide 5, to review our organic revenue growth by discipline. During the quarter, Advertising & Media growth was very strong at 7%, driven by excellent performance at our global media businesses. Precision Marketing, which now includes Flywheel, grew 4.3%. We expect this to continue to be one of our fastest-growing disciplines in the future.

Public Relations declined by 1.1% in the quarter. We expect this discipline will improve the rest of the year and benefit from the 2024 US elections. Healthcare grew 2.1% during the quarter, as we continue to cycle through some client losses from 2023, which we expect to lap after Q2.

Branding & Retail Commerce declined by 3.8%, driven by a challenging environment for our branding agencies that are more aligned on project-based engagements, and faced a difficult comparison to Q1 of 2023 when they grew by 9%. You'll note that we've updated the name for this discipline, which was formerly called Commerce and Branding.

Experiential grew a strong 9.5%, led by the US, which offset a small reduction in revenue internationally. We expect this discipline to benefit later in the year from the Summer Olympic Games in Paris. And Execution & Support declined by 4.3%, with mixed results that overshadowed continued strength in field marketing.

Turning to geographic growth on slide 6. We saw growth in six of our seven regions, led by the US and Europe and a strong growth in Latin America, driven by Advertising & Media.

Slide 7 shows our revenue by industry sector. First quarter results were very similar to last year.

Now let's turn to slide 8 for a look at our expenses. In the first quarter, salary and related service costs grew as a result of increased staffing levels, primarily as a result of our acquisition of Flywheel Digital, but they were down as a percentage of revenue year-over-year, driven by our repositioning actions last year and through ongoing changes in our global employee mix.

Third-party service costs increased in connection with the growth in our revenue. The third-party incidental costs increased somewhat, primarily as a result of increases in reimbursed travel and incidental out-of-pocket costs.

Occupancy and other costs increased primarily due to our acquisition activity during the period, but were essentially flat as a percentage of revenue due to lower rents as a result of our prior year real estate rationalizations. And SG&A expense was down both in dollar amount and as a percentage of revenue.

Now let's turn to slide 9 and look at our income statement in more detail. Our operating income increased 2.8%, and the related margin was 13.2%, down slightly from the prior year adjusted margin of 13.5% arising primarily from our acquisition activity, including Flywheel. As you may recall, our margin estimate this year is based on EBITA, which we have and continue to use as a measure of operating performance.

Similar to our peers and in response to requests from investors, this reflects an adjustment for the amortization of intangible assets. The adjustment now reflects amortization expense related to both acquired intangible assets and internally developed strategic platform intangible assets. Strategic platform intangible assets relate to the costs we are required to capitalize and amortize over future periods in connection with the ongoing development of the Omni platform and the future ongoing development of the Flywheel Commerce Cloud platform.

The amortization expense added back to calculate EBITA does not include amortization expense for internally developed software related to administrative and back office operations tools, such as ERP or workflow platforms.

For the first quarter of 2024, this amortization was $21.5 million, and we expect the remaining quarters of 2024 to approximate this amount. For comparability purposes, we've included a slide in the appendix of this presentation, and it reflects the prior year amortization related to acquired intangible assets and internally developed strategic platform intangible assets for the four prior year calendar quarters of 2023 and the full year for 2023 and 2022.

EBITA in Q1 2024 of $500.4 million increased 4.1% year-over-year, and the related margin was 13.8%. We continue to expect our fiscal year 2024 EBITA margin to be close to flat with our 2023 adjusted EBITA margin of 15.6% for the full year.

Moving down the income statement, our income tax rate of 26% was similar to the rate for the first quarter of 2023. For full year 2024, we continue to expect our income tax rate to approximate 27%. Changes in income from equity investments and income attributed to minority interest investments were not significant.

As you can see at the bottom of this slide, we have also provided a new line item, non-GAAP adjusted net income per diluted share. Similar to EBITA, this also excludes the amortization on an after-tax basis that I just discussed related to acquired intangibles and internally developed strategic platform intangibles.

This new reporting more closely measures the performance of our operating businesses year-on-year, and is similar to our peer group's approach of adding back after-tax amortization expense when calculating non-GAAP diluted earnings per share. For the first quarter of 2024, this metric increased to $1.67 or 3.7%, compared to the non-GAAP adjusted diluted earnings per share of $1.61 for Q1 2023.

Now let's turn to cash flow on slide 10. We define free cash flow as net cash provided by operating activities, excluding changes in operating capital. Free cash flow for 2024 was $415.1 million, a slight decrease of 3.2%. Regarding our uses of cash, we used $139 million of cash to pay dividends to common shareholders, and another $13 million for dividends to non-controlling interest shareholders.

Our capital expenditures were $23 million, similar to last year, although we still expect fiscal year 2024 levels to be higher due to growth in capital investment at the newly acquired Flywheel. Total acquisition payments were $812 million, which reflects the $845 million acquisition of Flywheel, net of cash acquired.

Finally, our stock repurchase activity, net of proceeds from stock plans, was $178 million in the quarter, which is in line with our estimate of total repurchases for the year of approximately half of our historical average, given our Flywheel acquisition.

Slide 11 is a summary of our credit, liquidity and debt maturities. At the end of the first quarter of 2024, the book value of our outstanding debt was $6.3 billion, up over $600 million from funding a portion of the Flywheel purchase price.

As previously disclosed, we issued €600 million senior notes due March 2032, with a coupon of 3.7%. Net proceeds in US dollars were approximately $643 million. Our cash equivalents and short-term investments were roughly flat at $3.2 billion. We also have an undrawn $2.5 billion revolving credit facility, which backstops our $2 billion US commercial paper program. We continue to monitor the credit markets with regard to our $750 million of 3.65% senior notes due November 1, 2024.

At this point, given where interest rates are and our financing activity early in 2024, we expect that net interest expense for the full year 2024 could increase by approximately $45 million relative to full year 2023.

Slide 12 presents our historical returns on two important performance metrics for the 12 months ended March 31, 2024. Omnicom's return on invested capital was 22%, and our return on equity was 44%, both reflecting very strong performance.

I will now ask the operator to please open up the lines for questions and answers. Thank you.

QUESTION AND ANSWER SECTION

Operator: Thank you. We will now begin the question-and-answer session. [Operator Instructions] Your first question comes from Cameron McVeigh with Morgan Stanley. Please go ahead.

Cameron McVeigh
Analyst, Morgan Stanley & Co. LLC

Q

Thank you and congrats on the numbers and closing Flywheel. Maybe if you could talk more to the Flywheel acquisition potential value that unlocks both from a short-term and a long-term perspective, and then the expected margin impact this year over the long term. Thanks.

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

A

Sure. I'll cover part of it, and Phil can chime in.

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

A

Sure.

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

A

Flywheel is important in a number of areas. First and foremost, they are the only fully integrated retail commerce cloud platform that's out there. Everybody else can do a piece or two, but the company we acquired that Duncan put together, he did it over a six-year period and integrated quite a number of component companies, and it came together shortly around the time that we announced it.

What they have is an incredible amount of knowledge and information about how people transact and do business on an online e-commerce basis. And not only here domestically in the United States with things you're probably familiar with like Amazon, Walmart, Target, but also in China, in Alibaba, and I forget the other one, but – and they – so they have a global presence. They are right at the cutting edge of people buying online and using e-commerce. And that area is, according to forecasts, scheduled to just grow exponentially over the next several years.

What it allowed us to do as well is to combine the Commerce Cloud, which looked at the retail sales aspect of what happens when you're trying to market something to someone, it enables us to connect to Omni Assist. So we can go all the way from identification, brand building, audience building, all the way through to the actual sale that occurs in a local e-commerce environment. And there's no one else can do that. And I think based upon our study and our due diligence prior to the deal, we don't think there is anyone out there who even competes with the information that Flywheel has and the platform that they are operating in.

That gives us tremendous opportunities to grow with the market as it grows. It also has turned our attention to how do we optimize this information for the benefit of our clients, and you'll see occasionally, we now refer to ourselves as a marketing and sales company rather than simply an advertising and marketing company. And that's because we can go end-to-end legitimately for the very first time.

In terms of its growth, because e-commerce, we're focused primarily here in North America, tends to be a fourth quarter – third quarter, fourth quarter company. The fourth quarter is classically the weakest quarter for them, and it accelerates as we go through the balance of the year.

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

A

First quarter is the weakest.

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

A

I'm sorry. I said fourth, I'm sorry.

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

A

Yeah. So just on – Cameron, on margins short term and long term, the integration process continues. It's going very well, integrating Flywheel into all of Omnicom's operations. And as we've said back in the call in February, we expect Flywheel's margins will approximate Omnicom's average margins by Q4 of this year, and we expect overall results to be accretive, excluding the amortization that was added as part of the deal, also by Q4. Longer term, we expect the deal or the business to be accretive to Omnicom's overall average margins over the long run for sure.

Cameron McVeigh
Analyst, Morgan Stanley & Co. LLC

Q

Got it. Thanks, John and Phil. And if I could ask one other, curious if there are any other specific types of strategic acquisitions you're focused on in the near term. Thanks

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

A

There's areas we're focused on, I don't think I'll discuss targets until I'm done negotiating for them. But, yeah, as I said in the call, there are a few areas that are showing exceptional growth. It's in MarTech and transformation, and also in content production, automation of content production, and opportunities which geographically fill out our services in that area, and also from [ph] Omni's (00:25:45) point of view.

In terms of specific big Flywheel-type acquisitions, we're not looking at anything of that magnitude at this moment. So we are focusing in on growing and also transforming much of our own business for the opportunities that we see the new technology and the marketplace offers.

Cameron McVeigh
Analyst, Morgan Stanley & Co. LLC

Q

Great. Thank you.

Operator: Your next question comes from Adam Berlin with UBS. Please go ahead.

Adam Berlin
Analyst, UBS AG (London Branch)

Q

Hi. Good evening, everyone. It's Adam Berlin from UBS. I've got three questions, if I can. The first question is on Precision Marketing. Now that Flywheel has been integrated into that segment, can you give us any guidance of what you think the medium-term growth potential of that? Do you see that as a mid-single digit, high-single digit, double-digit business?

Obviously, it might take a few quarters to get there, but just what do you think is possible for that business segment once the integration is fully done? That's the first question. And maybe you can tell us, just kind of part B, what the organic growth of Flywheel was in Q1, just to help us figure out what the original business did in Q1.

Second question is, would the group adjusted EBITA margin have been up without Flywheel?

And my third question is on Advertising & Media. Advertising & Media delivered good growth in Q1 of 7%, but it was a little bit slower than in Q4. Can you just tell a little bit about the moving parts there? And what moved faster or slower than what happened in Q4? Thank you.

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

A

There's a lot to unpack, so I'm going to ask – re-ask some of your – define some of your questions. In terms of Precision Marketing, at this moment, included in our forecast is probably low-double digit growth for that area. But that's subject to opportunities.

Specifically with Flywheel, it's – as I said, stands alone. It's a component part of that. And the marketplace itself, clients' online activity, e-commerce is all growing. So, we look further than this quarter, next quarter, this year into the future and what it can do for us, and we're very bullish about its contribution to this whole process. That was, I guess, the first question. The second one?

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

A

The Flywheel growth number, Adam, we're not breaking it out...

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

A

Yeah, we don't.

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

A

...individually. I think the underlying Precision Marketing discipline, prior to Flywheel being added to it, certainly grew this quarter. Flywheel also had very good growth this quarter. But in terms of breaking out the business itself, we haven't and aren't going to break out individual businesses going forward either.

Adam Berlin
Analyst, UBS AG (London Branch)

Q

That's helpful. Thanks. Yeah, that's helpful. Thank you very much. [indiscernible] (00:29:16).

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

A

Sure. And then, you had a margin question without Flywheel, what would the first quarter margin have been, or would it have been flat? I think there's a lot of moving parts to operating profit and operating margin and EBITA margin, etcetera. Certainly, Flywheel's margins are lower than the Omnicom average margin, and there's certainly some integration costs in the first quarter.

We didn't go back and do the actual calculation, so – of how much was the impact of Flywheel or the negative impact of Flywheel on our EBITA margins. But I think it's hard to say would they have been flat, I think they are down about 30 basis points. It's not that big of a number. So the answer is probably, yes. Certainly, there are a bunch of costs associated with the integration. And I think the last...

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

Hold on. I just wanted to – and on that, Adam, we're not focused at all on what the margin impact is in the first quarter that they joined our company. We're incredibly pleased at speed in which and the progress we've made in integrating, because we're looking at the benefit that it is going to bring to the Omnicom Group moving forward. So we don't do that kind of – waste time really on that type of activity.

And the third question, if you could repeat it for me. I think I know what it is, but...

Adam Berlin
Analyst, UBS AG (London Branch) Q

Yeah, just what was the difference between the 9% growth in Q4 and the 7% in Q1 for Advertising & Media?

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

I'm just going to make a general statement and Phil can fill it in. We're very happy with the growth that we've seen, for sure. And that group has been growing very strongly for the last two years every quarter. So, in any particular quarter, it's up against very difficult comps, and we expect it to be – continue to grow throughout the balance of this year. So...

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

Yeah. When one of the disciplines goes from 9% growth to 7% growth, it doesn't bother us all that much, certainly, because the 9% was quite a performance, and 7% is also very strong performance. We're happy with that as well. So we haven't spent a lot of time trying to pick out the differences between that 2 percentage point swing between Q4 and Q1.

But a lot of times, Q4 is unpredictable. There's a lot of project spend in Q4 for the Media business as well as all the disciplines. So it isn't that surprising for Q1 to take a little bit of a step-down from Q4 in our history.

Adam Berlin
Analyst, UBS AG (London Branch) Q

Okay. Thank you very much.

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

Thank you.

Operator: Your next question comes from David Karnovsky with JPMorgan. Please go ahead.

David Karnovsky
Analyst, JPMorgan Securities LLC

Q

Hey. Thanks for taking the question. John, just on the decision to raise guidance, your result in the quarter was near the midpoint of the prior outlook. So just wanted to understand better the increase. Had you assumed a more cautious view for Q1, or are you just seeing better indicators for the rest of the year?

And then, on Precision Marketing, I know you stated previously, you maybe expected an improvement in 2024. We had heard some cautious commentary recently from some of your peers or IT services firms. Just wanted to see if you could update a bit on what you're seeing here in terms of moving projects forward. Thank you.

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

A

Sure. In terms of the forecast, I think what we said in the fourth quarter was that we're giving you the range of 3.5% to 5% saying that we're – the first quarter, we were still cycling through some client changes from the prior year; and that once we get into the second quarter and beyond, we were far more confident that we weren't facing any significant headwinds as we continue to grow the business.

And as it turned out, the fourth (sic) [first] quarter came in at 4%. So it seems very logical for us to remove that bottom end caution, I guess, at this point and still feel that, subject to macroeconomic changes in the world, I've seen a lot of them in the last couple of weeks, we're confident that we have the right product, right approach towards clients. And our management teams are very strong and focused. So we have more confidence, and that's why we lifted the bottom end of the guidance up at this point.

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

A

The other question was the outlook for Precision in 2024 as you go from quarter-to-quarter.

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

A

Well, I wouldn't forecast it for you quarter-to-quarter. And I think I said in the previous answer that we expect it to be low-double digits at this point, and that was included in coming up to our overall guidance of 4% to 5%.

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

A

Yeah. We certainly see – especially as John had referenced earlier in the call, Flywheel is kind of weighted towards the end of the year in terms of its performance relative to the retail cycle. Certainly, we see it improving as the year goes on in terms of the growth rate.

David Karnovsky
Analyst, JPMorgan Securities LLC

Q

Got it. Yeah, I was really asking about sort of the non-Flywheel part of the business, right, digital business transformation and whether you had started to see more movement on some of the projects there.

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

A

That business is healthy at this point. I think we haven't seen any headwinds at all. If they occur, others are referencing to, it probably has more to do with their specific clients' plans and impact economy is having on those clients than an industry or a segment type of answer.

David Karnovsky
Analyst, JPMorgan Securities LLC

Q

Thank you.

Operator: Your next question comes from Tim Nollen with Macquarie. Please go ahead.

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

Q

Hi, great. Thanks very much. I feel like I'm going back many, many years with this. But could you please remind us what your organic growth calculation is, i.e. your organic growth in the quarter, obviously your organic growth, does that include Flywheel's organic growth as well? And then, when does it become part of your reported growth? Is it 12 months after, I think that's right, or do you actually go a full year after it has been already integrated? Hope you understand that question.

Secondly also, I'd like to – just to ask another Flywheel-related question. Your Branding & Retail Commerce number was down, I think, 3.8% organic in the quarter. I think you pointed to particular items on the Branding side. I'm just wondering if there is any Flywheel business in that Retail Commerce portion, and then tying that to the first question, if there was organic growth there. Thanks.

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

A

Sure. I'll start with the organic growth, Tim. So we've always done the calculation consistently. So when we do an acquisition, and in this case, Flywheel, we spent over $800 million of capital to acquire the company. We're responsible for the results, and we're measured on the results post-acquisition.

So included in the results is Flywheel's organic growth. The acquisition revenue number reflects their prior – or in the calculation, the acquisition revenue from the prior year is used as a measure to determine what the growth is, based on the current year's revenue. So, yeah, you take the current year revenue and compare it to the prior year revenue. If it grew, it's part of the organic growth; if it's negative, it's part of the organic growth.

We've never excluded acquisitions from that calculation, and we don't see why you would exclude them for the first year in any way. I think we're responsible for the growth as part of the calculation. So we haven't changed the calculation and how we go about doing it.

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

A

So Tim, as Phil explained it, just another way to look at it is if Flywheel did, hypothetically, 102 this first quarter and last year before we owned it, it did 100 million, the 2 would be an organic calculation, [indiscernible] (00:39:18) just the 2.

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

A

Right. [indiscernible] (00:39:24) last year was 104, they'd be negative 2 of organic growth.

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

A

Right.

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

Q

Right. It's been a long time since you've done an acquisition of this size, so I'm forgetting how you do the accounting for it. So thanks for that explanation.

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

A

Yeah, no. The one thing you can count on, Tim, is I've been here longer than you, and we've always done it the same way.

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

Q

Consistency. Thanks. And then, remind us again, if relatedly then, when does Flywheel become part of reported growth, not acquisition growth, as an organic reported growth, not acquired growth?

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

A

So it's in the reported growth. And...

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

Q

Obviously, yeah.

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

A

...the incremental growth over the prior year, the two in John's example, that's what's on the organic growth line.

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

Q

Right. And then...

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

A

The balance is on the acquisition line. So on the acquisition – if you're looking at the chart in the presentation, the acquisition revenue is the 100, and the organic growth number is the 2.

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

Right. And then, is it 12 months after acquisition that there's no more acquired revenue from the company? It's just all organic?

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

Yeah.

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

Yeah. Yeah, that's correct. Yeah.

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

12 months after acquisition close, okay. Got it. Thanks.

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

Yes. Well, it's – yes, one year, yes.

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

Okay.

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

Yes.

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

Great. And then lastly, on the Retail Commerce proportion of the branding number, is there Flywheel in that or is that all in Precision Marketing?

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

Yeah, all the Flywheel's in Precision Marketing.

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

Okay.

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

Trying to split up an operating company between disciplines is certainly very challenging and especially Flywheel's business.

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

Got it. Okay. Perfect. Thanks very much.

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

Thank you.

Operator: Your next question comes from Steven Cahall with Wells Fargo. Please go ahead.

Steven Cahall
Analyst, Wells Fargo Securities LLC Q

Thank you. So, John, with the removal of the lower end of the guide, the way you talked about it, moving to the 4% to 5%, is it fair to say that the year is off to a stronger start in terms of what you're seeing in client activity? Or is it just that it's off to the start you kind of expected and that has removed some risk and so that gives you that confidence to move up the range a little bit?

And maybe within that question, I think in the prepared remarks, Phil, you mentioned that Advertising & Media was solid and media buying was called out as the piece of that. Creative is obviously still a big business, and I think it was a little choppy across the industry in 2023. So, it also just look to understand if there's any inflection points or trends in the creative part of that business? Thank you.

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

I'm sorry. I didn't write your first question down, sorry. Repeat the first one, I'm sorry.

Steven Cahall
Analyst, Wells Fargo Securities LLC Q

Yeah. I'll break it into two, it will be easier. So, the first one is just with the change to guidance.

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

Right.

Steven Cahall
Analyst, Wells Fargo Securities LLC Q

Is it just the things are kind of performing in line? Or are you actually seeing better client activity than you expected early on?

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

Well, things are in line for certain. And things are – certainly things that we expected to grow are growing. And so the confidence is every week passes just gets more reassured as we go through the year. And at this point, looking at the new business activity that's in front of us for the next several months, we're defending very little at this point, and we have opportunities on quite a number of big brand names. And if our batting average holds up as we go into the future, we'll take our fair share of that, which won't have too much of an impact as we get later in the year in terms of 2024 numbers. But overall, it helps the health of the business, our confidence. And it will certainly give us a wind at our backs for next year as we move into the end of the year and into next. So, all the signs at the moment are very constructive, and we're making a lot of progress on a lot of different fronts.

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

So, your question on creative versus media. Creative, this quarter was roughly flat. We expect the rest of the year to improve in the advertising – creative advertising agencies. It's still core to what we do and it's really Omnicom's DNA. It does go beyond – creative does go beyond advertising, though. And they are certainly very different agencies than they were just few years back as they continue to adopt new ways of working using current technology and some of the things we talked about and John talked about on his – in his prepared remarks in terms of the content supply chain, et cetera, they are a big part of that. So, we're optimistic that they'll be in a growth mode as we go through the rest of the year.

Steven Cahall
Analyst, Wells Fargo Securities LLC
Q

And Phil, could you put that roughly flat just in the context of whether you think that's an industry trend related to macro and/or technology? Or is any of that related to account wins or loses?

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

I think it's probably a combination of each of those just – even though that it's a lot of different things, but there's certainly been a lot of change in those businesses recently. And I think we're probably not that much different than anyone else.

Steven Cahall
Analyst, Wells Fargo Securities LLC
Q

Great. Thank you.

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

Sure.

Operator: Your next question comes from Michael Nathanson with MoffettNathanson. Please go ahead.

Michael Brian Nathanson
Analyst, MoffettNathanson LLC
Q

Thank you. Following up on Steve's question about creative. Can you talk a bit about gen AI and what you're doing on the creative side? What have you learned? And is there a risk that as these tools that get more sophisticated that it could be cannibalistic to your creative service businesses as maybe it becomes more efficient for other people to do it or new entrants form? That's one.

And then, two, Phil, you talked a bit about the capital intensity of Flywheel, you mentioned a little bit of higher CapEx down the road. How much more capital intensive is that business than the rest of Omnicom? Thanks.

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

A

Sure. I'll start your answer. With respect to technology in the advertising sector, and then I might ask Paolo is working most closely on AI has joined with us today, if he wants to add anything before Phil gets to answer.

Michael Brian Nathanson
Analyst, MoffettNathanson LLC

Q

Okay.

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

A

The single largest benefit of AI- generative AI as we're using it is it makes it simpler for highly creative people to come up with different executions, different applications of their ideas across many different mediums and using the specific Omni data that we have in Flywheel Commerce data to help understand where the consumer is and the messaging that we have to create in order to reach that consumer. So, as this goes forward, automation affects every single part of the business, AI will affect every single part of the business. And the programs and the things that we're doing are to take that on board to evaluate and shift up as a market leader and even in events of testing things that are available or hopefully will become commercially available at some point in the future.

I guess if there's a downside to it, it's a lot of the things that in the past might have – be done manually and somebody got paid to do that execution work, which was typically pretty boring and repetitive, that gets eliminated. So you're not seeking to hire those level people to do that level of job and therefore get reimbursed at a profit for them. But what you are doing is, you're able to come up with better, cleaner, sharper ideas, which can either succeed fast or fail fast. And all that at the end of the day, benefits the client and makes the ROI on a marketing dollar spent greater. And that's where I think the contribution of generative AI is going to come in.

And it's been my experience over my career, the more clarity I can bring to a client in explaining what the ROI is on the next dollar of marketing he's going to spend or she's going to spend means that we probably are going to benefit from that and servicing it in some fashion. So, philosophically, and there's a lot of moving pieces that are going on all the time and have been for quite a while now. But pretty intensely, adjusting to and exploiting where we can, the things that generative AI does.

But Paolo, who you've met before in previous calls I think, is really the guy that I depend upon, among others on this, and he works very closely with all of our suppliers and vendors. Paolo?

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

A

Yeah. Sure. Hi, Michael. So...

Michael Brian Nathanson
Analyst, MoffettNathanson LLC

Q

Hi, Paolo.

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

...look, I think you've heard us talk about this in the past that we really believe that generative AI strictly is going to empower our people and really give them super powers for the skills that they already have. I think we look at it through the lens of a maturity model with respect to how they are executing their tasks. In the past – in the recent past, generative AI has really just been a tool. Today, it's more of an assistant or co-pilot, if you will. And really, tomorrow, it becomes a true partner, whether it be a creative partner, a strategic partner, a planning partner for every one of our employees. So that is effectively how we're approaching it and how we're building it into Omni to provide that partner for everyone.

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

Yeah. And It's a much longer conversation. But if you think the technology, if you're in a competitive industry and the tech is way further than it is today, the competitors simply ask the same questions to reach the same consumers, they are all going to get the same answer. So it's not going to differentiate anybody. What brings the difference to this is the creative minds that we're able to attract in Omnicom and apply to those client challenges and objectives.

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

And then your second question, Michael...

Michael Brian Nathanson
Analyst, MoffettNathanson LLC
Q

Thanks.

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

...similar – how intense is the CapEx commitment? Similar to the Omni platform, we need to continue to develop the Flywheel Commerce Cloud platform, and we intend to do that certainly with Flywheel in lead. But in terms of scale, while it's similar to Omni, we expect an increase in CapEx spend. But we wouldn't say that we expect it to be dramatic. It's going to be an increase, but a very manageable increase because, as we said before, Flywheel went through a significant period of time, probably 12 to 18 months, to integrate its back-end platform or platforms, some of which are part of prior acquisitions into one integrated Flywheel Commerce Cloud platform. The vast majority of that work was done prior to when we announced the deal in October of 2023.

So most of the work at this point going forward, similar to Omni, is on building enhancements, incorporating new technology and keeping the platform at the leading edge. So we don't expect, as you, to be dramatic, but certainly it's an investment that's well worth making for us.

Michael Brian Nathanson
Analyst, MoffettNathanson LLC
Q

Okay. And Phil, can I ask a quick one on the add-back of amortization?

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

Sure.

Michael Brian Nathanson
Analyst, MoffettNathanson LLC
Q

I understand the intangible amortization. But what was the thinking on the internally developed strategic platform asset amortization? So that's – so how is that – why did you guys include that in the EBITA definition versus pure amortization from goodwill?

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

Sure. So as we've done for well over 10 years, we built out the Omni platform. We built it out through internal investments. And some of our competitors actually went out and did acquisitions, bought somewhat similar assets in terms of data analytics and other technologies similar to the Omni platform. And in terms of comparing what amortization gets added back or not, we think the reality is whether we acquire it or we build it ourselves, you'd want to look at that amortization of the investments that you've made, and that would be the appropriate amount to add back.

In terms of rough order of magnitude, if you look at the total of the add-back related to acquired intangibles and internally developed strategic platform amortization, that's about 75% of the total. And the non-acquisition amortization is about 10% or 15% of that. So it's not a large proportion of the number. But about 25% of the total relates to administrative amortization expense related to administrative intangibles, things like ERP systems and workflow systems, et cetera. So we think that's an appropriate and probably most comparable way to look at the numbers compared to some others in the marketplace.

Michael Brian Nathanson
Analyst, MoffettNathanson LLC
Q

Thank you as always, Phil. Thank you.

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

Sure.

Operator: Your next question comes from Craig Huber with Huber Research Partners. Please go ahead.

Craig Huber
Analyst, Huber Research Partners LLC
Q

Thank you. John, if we could just go back to Flywheel for a little bit here. You guys have obviously cleaned up your portfolio of your performing assets and at least there's quite a bit for [indiscernible] (00:55:58) Flywheel acquisition here. But curious, does that change your outlook long term, the potential for organic revenue growth here to maybe accelerate off this roughly 4% to 5%, you're talking about [indiscernible] (00:56:14) last year. Do you feel increasingly optimistic longer term about accelerate growth rate? I realize there's a law of larger numbers here. You're a much bigger company now than you were 10, 15 years ago. Your thoughts, please.

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

Sure. Yeah. I'd answer it a little bit differently. Because we've cleaned up the portfolio, and there's always work to do, but not nearly as much work as we've done in the past. Because we've cleaned up the portfolio, I think the products and the offerings that we have today are really market-leading. And as we expose them to the marketplace and our clients and probably do a better job, actually, of marketing Omnicom and its products to the world, I do think that it will sustain our organic growth going forward. I have enough difficulty giving you guidance for the balance of this year, so I don't want to get too far ahead of my shoes. But I'm very confident that we're going to be the most appropriate supplier in the marketplace with the type of activities that clients are looking to buy from a group like ours.

And so, with that confidence, that's just not me and what we buy or what we integrate; that is really reflective of the management teams that work on the various aspects of Omnicom and are executing and delivering our products worldwide. But at the end of the day, it comes down to those people, the products that we make available to them, but the creative genius and innovation that they bring to improving that product on a constant basis. So yes, I'm bullish, I guess.

Craig Huber
Analyst, Huber Research Partners LLC

Q

Thank you for that, John. And Phil, if I could just ask you real quick. In terms of the margins for this year, I think you're talking about roughly flat margins for the year. Just walk us through a little bit about the costs in your mind that are holding that back from actually going up. And you talked about the integration costs of Flywheel, Flywheel being dilutive, I think, you said the margins the first three quarters, but what else should we think about, please? What are the internal investment spending you're doing, et cetera?

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

A

Sure. So the approach in margins hasn't changed much over the years. We're always trying to find the right balance between growing the business in a sustainable way, making the appropriate investments in the business for the future. So Omni and the Omni platform is a great example of that and balancing that with an appropriate margin and return to shareholders.

So as it relates to 2024, certainly, we've got an integration process to go through with Flywheel, as we said going really well, but more to be done. We do expect to continue to make the investments we've been talking about with respect to the Omni platform and ongoing investments in Flywheel and Flywheel Commerce Cloud and ultimately, we see some opportunities with our cost structure being flexible to be part of the equation and how to maximize margins overall.

We're looking at the long-term health of the business continuing to make those investments. That's part of what goes into the ultimate end result when it comes to margins because really, we're trying to grow operating profit dollars, not just hit a percentage. So, I think the Flywheel transition and integration certainly a big part of it, along with continued investments in Omni and the Flywheel Commerce Cloud platform and AI, balanced with some benefits coming from other initiatives we continue to pursue, whether it's the real estate portfolio, offshoring, nearshoring, et cetera. All of that is factored into the equation. And that's how we reach the expectations we have as we look out at all of 2024.

Craig Huber
Analyst, Huber Research Partners LLC

Q

Great. Thanks, guys.

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

A

Sure. Thank you.

Operator: There are no further questions at this time. This will conclude today's conference. Thank you for your participation. You may now disconnect.