Omnicom Group
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# Executive Summary

Omnicom Group, a strategic holding company, was formed in 1986 by the merger of several leading advertising, marketing, and corporate communications companies. By providing professional services to clients around the world, Omnicom has grown to be one of the largest global advertising and marketing companies. Omnicom's agencies provide traditional media advertising, customer relationship management, public relations, and specialty communications. The company's business model is focused on client relationships and clients' needs are the central focus in how Omnicom structures its business offerings and allocates its resources. As a company providing services, Omnicom organizes its various agencies in formal and informal virtual networks in order to deliver consistent brand messages.

This report represents Vector Strategy Group's strategic advice for Omnicom Group. Vector's Media Division researched Omnicom's history, business model, industry landscape, competitors, and financial statements to provide the company with a thorough strategic analysis. The following briefly introduces the key issues facing Omnicom in today's market, and summarizes Omnicom's findings and strategic recommendations.

Omnicom operates in all major markets of the global economy and has a large, diverse client base. In 2009, Omnicom's revenue declined 12.3% due to a difficult global economy, declining consumer spending, and rising unemployment in most major markets. These factors led clients to reduce spending on advertising and marketing, negatively impacting Omnicom's revenue and operations results for 2009. An additional factor was the weakening of major currencies against the U.S. dollar.

Omnicom's primary operating expenses are in two distinct cost categories: salary and service costs, and office and general expenses. Salary and service costs are composed primarily of employee compensation costs. Office and general expenses are comprised of rent and occupancy costs, technology related costs, and depreciation and amortization.

Overall, in the short-term, Omnicom must overcome declining revenues by striving to increase its client base, keep expenses low, and maintain business with current clients. In the long-term, Omnicom should position itself so that it can take advantage of the evolution of the advertising and marketing industries. As digital media and mobile marketing gain importance, Omnicom should focus on expanding its business offerings or pursuing M&A activity that would allow for greater reach and diversity of services. Additionally, Omnicom could benefit by updating its debt financing strategy. By taking on more debt in order to fund investments, Omnicom could employ more capital to acquire companies and enhance operations.

# Company Overview

## History

### Early History: Incorporation in 1986

Omnicom Group, Inc. is a holding company that operates primarily in the advertising industry. It provides a wide spectrum of services including advertising, marketing services, specialty communications, interactive/digital media and media buying services. Omnicom was incorporated on August 29, 1986 in New York, NY and trades on the New York Stock Exchange as OMC[1]. The company was created to combine three leading advertising agencies into a single group that could compete in the global market.

The first agency, BBDO Worldwide, was founded in New York in 1928 as Batten, Barton, Durstine & Osborn. From 1928 to 1957 BBDO steadily grew to become one of the leading ad agencies in the United States, with annual billing increasing from $20 million in 1939 to $200 million in 1957. BBDO's extensive portfolio of creative advertising included a large account with PepsiCo and was responsible for developing the Pepsi Generation campaign, making it an attractive component for Omnicom Group.

The other two advertising agencies enhanced Omnicom's global reach. Doyle Dane Bernbach Group (DDB) had created the *fahrvergnügen* ads for Volkswagen, and had strong ties in Europe. Needham Harper Worldwide offered ties to Asia and a strong history, including creating the "You Deserve a Break" commercials for McDonalds. Shortly after the creation of Omnicom Group, DDB and Needham Harper merged to form DDB Needham Worldwide. BBDO remained a separate agency, although the public relations firms and direct marketers of each of these companies were managed by the Diversified Agency Services (DAS) arm of Omnicom Group[2].

In 1989, Bruce Crawford became chairman and CEO of Omnicom Group. Mr. Crawford, who had just finished a stint running New York's Metropolitan Opera, was a former chairman of BBDO. Under his direction, the DAS arm of Omnicom was transformed from a disorganized group of shops into an integrated marketing giant. Crawford ran Omnicom Group as a holding company of independent operating units that benefited one another through a system of cross-referrals. Crawford also helped Omnicom endure the 1990-1991 recession by keeping interest costs low.

### Mergers and Acquisitions in the 1990s

Throughout the 1990s, Omnicom Group added more companies as the string of mergers continued. In 1992, the company acquired Goodby, Berlin & Silverstein, a leading U.S.-based national advertising agency. In 1994, Omnicom purchased WWAV Group, the largest direct-marketing agency in the UK.

Also in 1994, Omnicom acquired TBWA Advertising, which had been founded by Bill Tragos in Paris in 1970. The following year, Omnicom combined TBWA with Chiat/Day, a company founded in 1968 by Jay Chiat and Guy Day to create TBWA International Network. TBWA joined BBDO and DDB Needham to give Omnicom three separate global advertising brands.

By the middle of the decade, Omnicom had grown from a fledgling combination of former competitors to a dominant force in the advertising industry. In 1996, Omnicom purchased Ketchum Communications, which had strong business segments in traditional advertising, telephone directory advertising, and public relations. The company finished 1996 with sales of $2.6 billion, up from $1.2 billion during the 1991 recession.

In 1997, Omnicom Group reached an important milestone as DDB Needham won back its McDonalds account after a 15-year hiatus. That same year, Omnicom President John Wren became the CEO as Bruce Crawford stepped down. Crawford kept his position as chairman, which he still holds today.

Mr. Wren continued to expand Omnicom's services by making numerous acquisitions across varying business spheres. His first move as CEO was to begin to move Omnicom into high-tech interactive marketing by acquiring multiple firms including Razorfish, Think New Ideas, and Agency.com Ltd. He integrated these firms into Omnicom's Diversified Agency Services (DAS) unit. Omnicom's general successes in the advertising industry, along with its incredible expansion of services, resulted in its being selected as Fortune magazine's most respected advertising group in 1997.

To round out the decade, Omnicom also purchased London-based GGT Group and merged it with TBWA International Network to create TBWA Worldwide. In 1999, Omnicom fully purchased U.K.-based Abbot Mead Vickers, merging it into BBDO. Lastly, Omnicom reorganized DDB Needham and renamed it DDB Worldwide Communications Group.

Entering the 2000s, Omnicom seemed to be poised to continue its incredible ascent to the top of the advertising world. BBDO scored a major victory in 2000 by landing the $1.8 billion DaimlerChrysler account over rival FCB Worldwide, while CEO Wren began to pursue the Hollywood marketing sector by purchasing Santa Monica-based David Brown Entertainment[3].

Throughout the mid-2000s, Omnicom carried on its acquisitions of companies and repeated successes over its competitors. In 2005, Omnicom gained accounts including Disney, Bank of America, and 7-Eleven stores. The next year, Omnicom acquired St. Louis agency Rodgers/Townsend, giving Omnicom yet another regional presence in the United States. The mergers that created Omnicom foreshadowed the development of global communications groups as providers of a variety of marketing services, far beyond simple advertising. To this end, the fused operation included an entity called Diversified Agency Services (DAS) to take care of activities like direct marketing, public relations and sales promotion, which do not employ traditional advertising techniques.

Following this long period of acquisitions, Omnicom Group is seeking to re-organize the holding company by focusing on full-service communications firms and integrating its more specialized firms into its global agencies. Omnicom Group is still growing, and made 12 acquisitions throughout 2008.
In 2008, Omnicom Group had approximately $13.4 billion in revenue, making it the largest corporate media sales conglomerate in the world[4]. The company's relatively good fortunes throughout the recession have been buoyed in large part by its consistently strong agency networks, as traditional media advertising accounts for more than 40% of revenues[5]. The bulk of Omnicom's growth, however, is tied to its ability to provide an ever-expanding menu of services to its clients. Specifically, areas such as customer relationship management (CRM) and specialty communications will be increasingly important looking forward[6].

## Business Model

Omnicom Group is one of a small group of large international advertising agencies. The multi-national, multi-agency holding company business structure has proved to be successful in the advertising and marketing industry for a number of reasons[7]. There is pressure driving advertising agencies into international expansion to accommodate their clients' multinational marketing goals. In recent years, the agency side has undergone significant consolidation and now consists of a few giant multinational organizations and a multitude of small local and regional makers of advertising.

By placing multiple agencies under an umbrella holding company, Omnicom is able to take advantage of its size and scope to gain a foothold in the international market. The company's central management serves as a single point of contact for coordinating marketing activities and allows the company to achieve improved cost efficiencies. By organizing and coordinating the various agencies under Omnicom's management, the company can attain greater coherence in marketing voice between the separate agencies. Each individual firm, which range from small agencies serving local clients, to global agencies serving Fortune 500 companies, benefits from the holding company arrangement. Each agency can rely on Omnicom's strong brand reputation and can have access to the CEO in times of crisis.

In addition, Omnicom's business structure offers one-stop global communication services without conflicts of interest. Member agencies are allowed to function autonomously and handle competing accounts without compromising client confidentiality.

Omnicom Group's holding company structure also gives the firm the advantage of economies of scale. Especially in today's economy, many clients are demanding lower rates. By offering a wide breadth of services, Omnicom can guarantee a certain annual volume of business and offer discounted rates to clients that bring in a lot of revenue. The firm's structure also gives clients access to specialized and emerging services that may be difficult or more costly to seek elsewhere. Currently, the digital media services industry is a growing business that offers diversification to the holding company while mitigating a decline in the traditional advertising business. A global network communication agency like Omnicom Group was created primarily to achieve greater profitability and to have the opportunity to carry out defensive or aggressive moves to counter competing agencies. Due to its holding company structure, Omnicom Group has the ability to design, implement, and manage global campaigns[8].

# Competitive Analysis: Porter's Five Forces

## Overview

| Force | Strategic Significance |
|---|---|
| Internal Rivalry | Moderate |
| Entry & Exit | Moderate/Low |
| Supplier Power | Moderate |
| Buyer Power | Moderate |
| Substitutes & Complements | Moderate/Low |

As a global marketing and advertising holding company, Omnicom is in the SIC Group 7311: Advertising Agencies. According to the U.S. Department of Labor, Omnicom would be under Division 1: Services and Major Group 73: Business Services. Omnicom's Industry Group code is 731: Advertising[9]. According to the North American Industry Classification System (NAICS), Omnicom falls under the code for advertising agencies, 541810[10]. Companies in this industry provide a full range of services including advisory, creative services, account management, production of advertising material, media planning, and buying.

## Internal Rivalry

In the advertising industry, Omnicom Group faces a moderate amount of internal rivalry. Rivalry is the extent to which firms compete on price. Generally, the key advertising and marketing giants like Omnicom Group, Publicis Group, and WPP Group are not rivalrous because they focus their competitive efforts on quality[11]. The quality of services provided is the major competitive battlefield in the advertising industry, rather than price. The major forces that reduce rivalry are natural industry leadership, increasing variable costs, switching costs, and low exit barriers. The advertising industry displays some of these factors limiting rivalry. For example, the global advertising industry has few competitors. Following decades of consolidation, the advertising market is now dominated by a number of multinational marketing-services groups. In an industry with a small number of firms, price competition is less important. The dominance of the key players in the global advertising industry means that there are fewer companies in the market overall. In addition, the leading players in the market, though of similar size, can differentiate themselves in various ways. Although Omnicom is similar to its competitors, it can differentiate itself from competition by its client list, advertising and marketing campaign records, and range of services offered. These factors can weaken rivalry by creating switching costs. Overall, rivalry is of moderate importance for Omnicom Group.

## Entry & Exit

Overall, entry into the advertising industry is unregulated but constrained by the large investments in time and resources that must be made in order to build up brand reputation and name recognition. Although the players in this industry do not heavily rely on physical assets, they do focus on knowledge and creativity. The time and money required to formulate knowledge of consumer's demand patterns and media offerings presents a type of entry barrier. Although there are no explicit governmental barriers to entry in the advertising industry, there are regulations on certain types of advertising in specific countries. For example, advertising for tobacco companies is limited in the United States. These types of limitations can lessen potential profits for advertisers and make entry less attractive.

The most profitable client accounts come from Fortune 500 companies and multi-national firms that seek out the best marketing and advertising agencies to fulfill their needs. In this sense, it is not possible for a small advertising industry to enter the market and directly compete with Omnicom Group. Since Omnicom is one of the top multi-national multi-agency holding firms, the type of client it serves is drastically different than a small client served by a local “mom and pop” advertising agency. However, the aspects of the industry that do pose a threat of new entrants to Omnicom are the development of new technology and the rapidly changing nature of advertising. Small firms can enter the market to capitalize on unique advertising and marketing opportunities, like advertising within video games. It can be hard for Omnicom to compete with such specialized firms, and each time a new segment of the market is created, there are more potential entrants with whom Omnicom must compete. Overall, the threat of entry is of moderate importance to Omnicom Group.

Exit costs in the marketing and advertising industry are typically not high. As a holding company with many agencies, Omnicom has minimal investment in capital because it primarily rents office space and does not own substantial physical assets. Therefore, this poses a small threat to Omnicom Group.

## Supplier Power

Suppliers to advertising agencies include IT and office equipment manufacturers. Other firms supplying goods and services to Omnicom Group include software and Internet service providers, real estate landlords, and owners of office space. Leading advertising agencies, such as Omnicom and its competitors, tend to locate in big cities, where property values and rent are high. Prime office space is a necessity for companies such as Omnicom because they must provide their clients with an appropriate space. Although advertising and marketing agents must negotiate with television, magazine, newspaper, and other media companies, such firms are not considered suppliers. Since Omnicom Group can pass on the cost of advertising space to its clients, media companies providing ad space are not direct suppliers to Omnicom. Staffing costs are another important component of Omnicom’s financial relationship to suppliers, because employee salaries are provided to workers supplying labor to the firm. Since success in the advertising business is closely related to the experience and talent of a company's workforce, employee compensation must reflect this. Overall, supplier power is of moderate importance in the advertising industry. Although there are important suppliers to companies like Omnicom, the firm's success largely depends on the talent of employees and less on the goods and services provided by suppliers.

## Buyer Power

In the global advertising industry, advertising agencies are the players while corporate clients are the buyers. Buyers can range from large multinational businesses to small local businesses. In today's market, advertising content can be delivered in many formats through diverse channels. Due to the increasing fragmentation of consumers, it is costly and difficult to reach mass audiences. Corporate clients are then faced with a dilemma: whether to do "in-house" advertising and marketing, or whether to seek the services of a global advertising firm such as Omnicom Group. By soliciting the advice and consultation of an external agency, corporate clients can often reduce expenditures. However, market players must exhibit strong differentiation in order to meet the needs of individual buyers. One common strategy among the players in the advertising industry is to offer a strong brand identity that corresponds with a reputation for niche or traditionally innovative campaigns. Overall, buyer power in the advertising industry is considered to be moderate.

## Substitutes & Complements

The key players in the advertising industry, such as Omnicom, WPP, and Publicis, offer quality advertising and marketing services to corporate clients. In order to substitute away from the large multi-agency firms, clients would have to consider a number of alternatives. One alternative would be to integrate backwards in order to reduce the costs associated with hiring external agencies.

This would mean companies would be relying solely on “in house” advertising and marketing, which could possibly require capital expenditure in order to build up these departments. Additionally, finding a suitably qualified team within the company could be difficult.

Another alternative to employing the services of a company like Omnicom Group would be to use a different marketing approach, such as advertising and marketing online through Google. Most companies in today’s market have established an internet presence. By advertising online through a direct service such as Google AdWords or AdSense, companies could eliminate some costs from employing a full-service firm. Clients could also substitute away from established brands and firms, focusing instead on low-cost, regional firms with less experience, brand strength, and name recognition. Different agencies have different pricing structures—some firms charge a flat commission fee on media space purchases, while others use variable rates. By successfully locating a lower-fee agency, a client could find a less costly alternative to Omnicom’s services. Overall, the threat of substitutes in the advertising industry is considered to be moderate.

The impact of complements to Omnicom’s business model is limited because there are few complementary goods that relate to the consumption of advertising and marketing services. One aspect of the industry that can be discussed is the diversification of the services offered by the key players. Target audiences are becoming increasingly fragmented due to technological advancements and changing consumer habits. In a sense, new and innovative forms of advertising and marketing can be considered complements to traditional media advertising. Social media networking offered by companies like Facebook and Twitter could present a threat to Omnicom because corporate clients might take advantage of the new companies and spend less money on Omnicom’s services. Mobile marketing offered by Google and smaller specialized firms could also present a threat to players in the global advertising industry. However, the overall impact of complements to Omnicom Group is low because the company is in a position to easily enter the smaller niche marketing and advertising markets. Omnicom could either enter the market with an existing agency, or strategically acquire a new firm to take advantage of its position in a growing industry segment.

# Financial Analysis

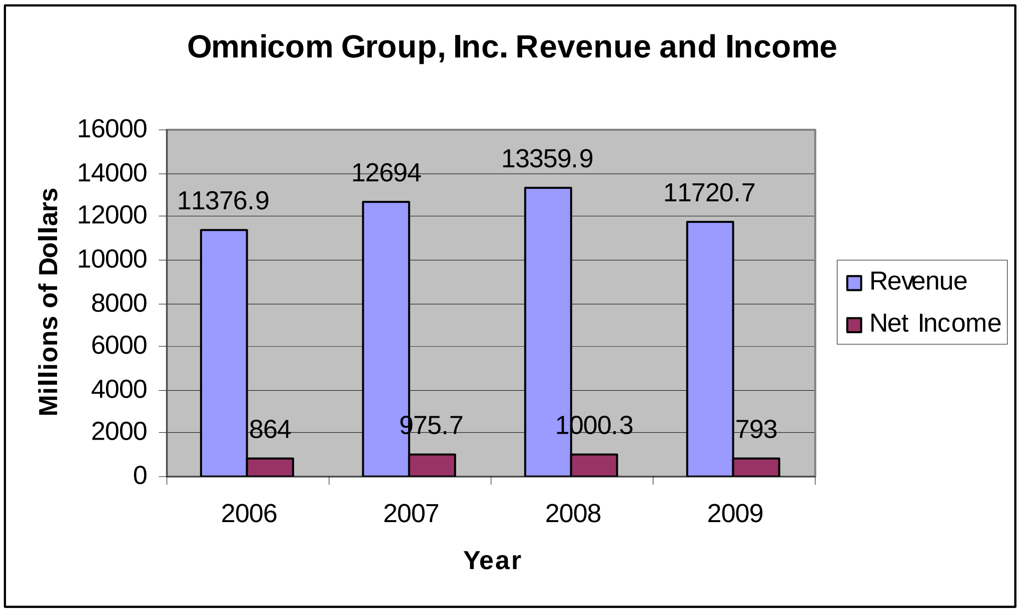
## Overview

In today's current financial climate, most companies are facing difficulties due to the economic slowdown. However, Omnicom Group has maintained a strong financial position despite lagging revenues from the recession. An evaluation of key financials can highlight Omnicom's financial strength as a multi-national, multi-agency conglomerate in today's market.

Omnicom Group is a publicly traded company listed on the New York Stock Exchange under ticker symbol OMC. In 2009, Omnicom earned revenue of $11,720.70 million and net income for the year was $793.0 million (see Figure 1). In the fourth quarter of 2009, Omnicom's net income decreased 15.3% to $229.6 million from $271.0 million in the fourth quarter of 2008[12]. Omnicom's diluted net income per common share in the fourth quarter of 2009 decreased 16.1% to $0.73 per share from $0.87 per share in the fourth quarter of 2008[13].

Omnicom's largest client represented 3.1% of the firm's revenue for 2009 and no other client accounted for more than 2.5% of revenue in 2009. The top 100 clients accounted for 50.4% of Omnicom's 2009 revenue. The business is spread across industry sectors, with no single industry compromising more than 16% of Omnicom's 2009 revenue from its 1,000 largest clients[14]. In general, Omnicom's revenue is balanced between the U.S. and international markets.

**Figure 1**




As a media and advertising conglomerate, Omnicom earns most of its income from client fees. This revenue is derived from fees for services or a rate per hour. Some of Omnicom's business lines earn a portion of their revenue as commissions based on performance in accordance with client arrangements. In the future, Omnicom can maintain its position over competitors by increasing profitability through an expanding client base, service diversification, and competitive pricing.

## Financial Statement Analysis

In order to evaluate Omnicom Corporation's financial position, it is helpful to examine various financial ratios that can be used to monitor company performance. Financial ratios evaluate the relationship between financial statement elements. They are most useful when compared to previous years' results, competitor company results, industry averages, or benchmarks.

The fist ratio is the current ratio, which measures the ability of a company to use liquid assets to extinguish or retire its current liabilities. The current ratio indicates a company's market liquidity and its ability to meet creditor's demands.

The quick ratio, also known as the acid test ratio, provides a more rigid analysis of a company's ability to pay its current obligations as they become due because it only includes those current assets that can easily be converted into cash in the numerator. The debt-to-equity ratio indicates the relative proportion of debt and shareholders' equity used to finance a company's assets[15]. The return on assets (ROA) ratio measures the percentage return on the asset employed by a company. Finally, the return on invested capital (ROIC) ratio measures how well a company generates cash flow relative to the capital it has invested in its business.

Figure 2 depicts Omnicom Group's key ratios for fiscal year 2009, and provides a comparison between Omnicom and two of its largest competitors, WPP Group and Interpublic Group.

**Figure 2**

| **Key Financial Ratios[16]** | | | |
|---|---|---|---|
| | **Omnicom** | **WPP** | **Interpublic** |
| **Current Ratio** | 0.87 | 0.90 | 1.1 |
| **Quick Ratio** | 0.71 | 0.90 | 1.1 |
| **Debt/Equity** | 0.53 | 0.91 | 0.83 |
| **Return on Assets** | 4.4% | 2.6% | 1.0% |
| **Return on Invested Capital** | 12.4% | 6.7% | 2.9% |

These financial ratios indicate that Omnicom's current and quick ratios are slightly below the two competitors, meaning Omnicom is slightly less able than WPP and Interpublic to repay current liabilities from current operations. However, Omnicom's debt-to-equity ratio, at 0.53, is well below that of WPP (0.91) and Interpublic (0.83). This could be interpreted as a positive quality by investors, because as the debt-to-equity ratio of a firm increases, the market's perception of the riskiness of investing in the firm's stock also rises. Since Omnicom uses a lower amount of debt financing relative to its competitors, its stock should be less risky and therefore required to provide a lower return. However, one recommendation for Omnicom would be to take on more debt in order to increase leverage. Since Omnicom is not as highly leveraged as its competitors, the company could stand to gain more from undertaking more debt and reinvesting the borrowed money.

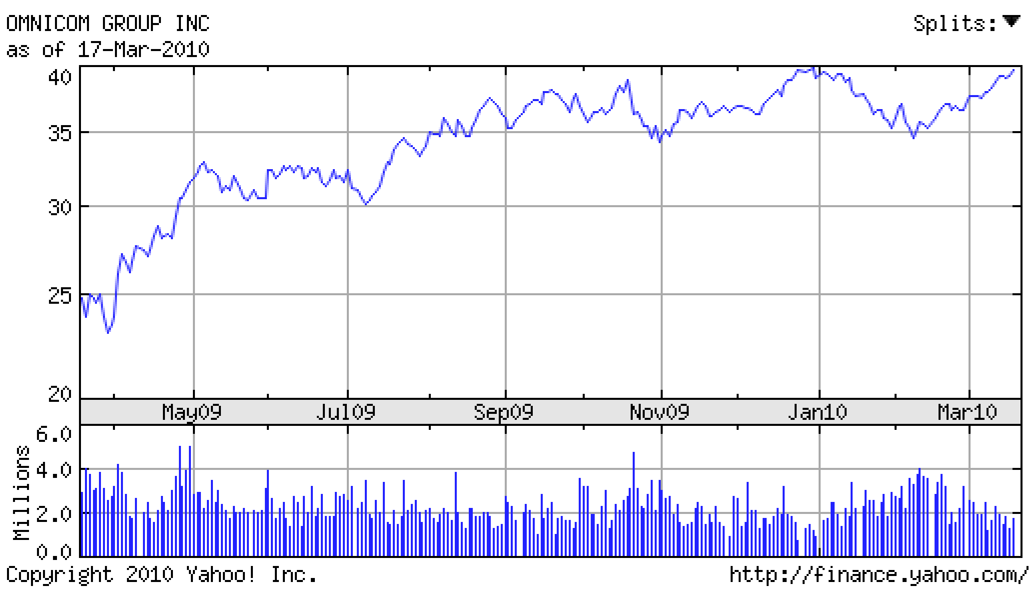
In addition, Omnicom's return on assets and return on invested capital ratios are higher than those of the two competitors. Omnicom's return on assets is 4.4%, which means that earnings from total operations are 4.4 times greater than total assets. Since Omnicom has a higher ROA than WPP Group and Interpublic Group, the company derives more dollars of earnings from each dollar of assets it controls relative to competitors. Omnicom's return on invested capital is 12.4%, meaning that earnings are 12.4 times larger than invested capital (long-term debt plus common stock equity plus preferred equity). This indicates that Omnicom is creating more value than its competitors and shows that the company is using its assets and invested capital wisely.

In 2009, Omnicom's diluted earnings per share (EPS) was $2.53, and the company's net income totaled $793.0 million. Worldwide revenues totaled $11.7 billion in 2009, and this revenue was balanced between brand advertising (44%) and marketing services (56%), and also between the United States (53%) and the rest of the world (47%)[17].

## Stock Price Analysis

Omnicom's stock price has remained fairly consistent over the past 10 years. The stock traded between $30 and $40 for most of 2000-2010, although the stock price steeply declined in mid-2008. This drop in stock price coincided with the global economic crisis. Omnicom's share price continued to fall in December 2008 when the company announced that it would cut 4 - 5 % of its global workforce. At that time, the stock was trading for $26.78. Since then, Omnicom's share price has been steadily climbing due to improvements in consumer confidence and the global economy. This upward trend has been aided by Omnicom's strategic acquisition of various marketing and advertising agencies, and the creation of Omnicom Digital in September 2009. Recently, Omnicom achieved advertising success by creating 5 of the top 10 ads in the 2010 Superbowl. As of April 6, 2010, Omnicom's stock is trading at $39.40, just below the 52-week high of $39.99[18].

**Figure 3**



## Industry Comparison

One metric commonly used in the advertising industry is organic growth. This term is a measure that factors out the impact of currency fluctuations, acquisitions, and related items. In the fourth quarter of 2009, Omnicom Group's revenue dropped 6.3 percent in terms of organic growth. CEO John Wren said that three sectors accounted for this decline in growth: the automotive, sports/event marketing, and recruitment businesses.

Omnicom Group's main competitors are the remaining top three advertising agency holding companies: Publicis Groupe, based in Paris, Interpublic Group of Companies, based in New York, and WPP Group, based in Dublin. Of these top advertising and marketing conglomerates, Omnicom has the second-largest market capitalization, with $11.72 billion in worldwide revenue in 2009. The largest advertising holding company in 2009 was WPP Group, with a market capitalization of $12.14 billion. Figure 4 shows a comparison of some key metrics of the world's top four agencies by worldwide revenue. Below, Figure 4 depicts a comparison of Omnicom Group and competing companies' adjusted ratios for fiscal year 2009.

**Figure 4**

**Financial Ratios: Industry Comparison[19]**

| | OMC | IPG | PUBGY | Industry |
|---|---|---|---|---|
| **Price/Earnings** | 15.47 | 38.84 | 13.18 | 54.6 |
| **Price/Book** | 2.88 | 1.82 | 1.12 | -3.1 |
| **Net Profit Margin** | 6.69% | 2.01% | 8.91% | 2.50% |
| **Return on Equity** | 20.31% | 4.11% | 18.16% | 4.40% |
| **Dividend Yield** | 2.05% | 0 | 1.97% | 1.50% |

These financial ratios largely depict Omnicom's strong return on equity, which is much higher than the industry average. However, Omnicom's price-to-earnings ratio is below the industry average. This is not necessarily negative, as price-to-earnings illustrates the amount investors are paying for a share relative to the annual net income of the company. A stock that is in high demand will have a higher P/E ratio; however, other financial information should be considered before making a decision about a company's financial strength based on this ratio.

Omnicom's net profit margin indicates that the company is profitable relative to the industry average and Interpublic Group. As an indicator of a company's pricing policies and its ability to control costs, Omnicom's net profit margin of 6.69% shows that the firm is profitable.

From analyzing the above financial ratios and taking into consideration the overall financial climate, it is clear that Omnicom displays financial strength. Omnicom outperforms the industry and its closest competitors, WPP, Interpublic, and Publicis, in a number of key areas. Omnicom has a lower debt

level and a higher return on assets, equity, and invested capital. Looking into the future, Omnicom must increase revenues to improve its financial performance. Omnicom should also work on improving its liquidity so it can have more cash available to cover current liabilities. However, Omnicom's low debt-to-equity ratio suggests the company is in a good position to take on more debt in order to leverage operations to optimize its financial strength.

# SWOT Analysis

## Strengths

### Extensive operations with strong portfolio of brands

Omnicom Group operates through various companies and agencies across the globe. It carries out business through three global advertising brands: leading U.S.-based national advertising agencies, media services, and the Diversified Agency Services Company. Omnicom's global advertising brands include BBDO Worldwide, DDB Worldwide, and TBWA Worldwide. BBDO Worldwide is the second largest global advertising network, providing advertising and marketing services in 79 countries through 287 offices. DDB Worldwide has operations in 90 countries with over 200 offices. TBWA is one of the top ten U.S.-based agency networks, serving prominent clients such as adidas, Apple, McDonalds, Michelin, Nissan, Sony PlayStation, and Visa.

Omnicom's national advertising agencies include Arnell, Element 79, Goodby, Silverstein & Partners, GSD&M Idea City, Martin/Williams, Merkley + Partners, and Zimmerman Advertising. The company's media service unit, Omnicom Media Group (OMG) consists of three full-service media companies and several media specialist companies. The agencies under OMG include Novus, one of the largest U.S. media buyers; Full Circle Entertainment, the industry leader in branded entertainment; and Singer Direct, the largest U.S. provider of insert media buying and management services.

Omnicom's customer relationship management, public relations, and specialty communications businesses operate through Diversified Agency Services (DAS), which includes more than 160 companies. These companies operate through a combination of networks and regional organizations. Overall, Omnicom's large-scale operations and strong portfolio of brands enhance the company's image and provide it with the advantage of economies of scale.

### Comprehensive acquisition strategy

Omnicom Group has a long history of mergers and acquisitions. In order to create a media conglomerate with the right balance of firms, the company developed an acquisition strategy to guide its formation. The strategy is focused on acquiring companies with an assembled workforce that has expertise in a specific area. This allows Omnicom to continue to build upon the core capabilities of its various strategic business platforms and agency brands. Expanding its geographic reach and service capabilities allows Omnicom to better serve its clients.

Key factors that Omnicom considers when pursuing a potential acquisition are the competitive position and specialized knowledge of the acquisition target. Accordingly, like most service businesses, a substantial portion of the intangible asset value that is acquired is the knowledge of employees. This is treated as part of goodwill and is not valued separately. In the case of the companies Omnicom looks to acquire, professional practice goodwill arises from the strong branding and knowledgeable employees. The majority of intangible assets are derived from customer relationships, including related customer contracts.

For each of Omnicom's acquisitions, management undertakes a detailed review of the target company and performs a comprehensive valuation of the target's assets. It can be difficult for Omnicom to value intangible assets because there are many assumptions that must be made in the valuation process. Omnicom typically uses an income approach and considers comparable market participant measurements. Omnicom's comprehensive acquisition strategy is one of the many strengths of the company. Well-researched acquisitions benefit the company as a whole because the gains from acquisitions are typically shared across multiple agencies. As new companies are integrated into Omnicom's central operations, they add to the client service strategy and help increase the scope and geographic presence of Omnicom's operations.

### Wide geographic presence

Omnicom generates revenues from markets in more than 90 countries. Omnicom has a presence in the U.S., the UK, Eastern and Western Europe, Asia, Australia, Latina America, and some regions in the Middle East and Africa. In FY 2008, Omnicom generated 57.2% of its revenues from the Americas. It generated 36.5% of revenues from Europe, the Middle East, and Africa (EMEA) and 6.3% of revenues from Asia and Australia. The portion of revenues derived from international regions has been increasing in recent years, representing Omnicom's geographic expansion. Revenues from EMEA and Asia and Australia increased 7.2% and 11.6%, respectively, from 2007 to 2008. Omnicom's diversified geographic presence reduces risks associated with adverse economic and political developments in any of its markets. Omnicom's wide international presence also enhances the company's financial position.

### Broad range of services

Another important part of Omnicom's business structure is its broad range of service offerings. The company provides an extensive range of services through various client-centric networks that are designed to meet specific client objectives. Omnicom monitors revenues across a bread range of services and groups them into four key disciplines. First, traditional media advertising offers the creation and production of advertising, print media, and strategic media planning and buying. Next, customer relationship management provides customer service and support, marketing, and social media. Public relations services include reputation consultancy and crisis management. Finally, Omnicom's specialty communications services include healthcare communications, recruitment communications, multicultural marketing, and financial and corporate business-to-business (B2B) advertising. This wide range of services enables the company to generate revenue from different streams. In 2009, traditional media advertising represented about 44.3% of Omnicom's total revenue. Customer relations management represented about 37.4% of total revenue. Public relations and specialty communications generated 9.2 and 9.1% of total revenue, respectively. Omnicom's broad range of services enables the company to provide comprehensive solutions to clients and supports its growth.

### Technology Infrastructure

Omnicom Media Group (OMG) unifies more than 140 locations and 5,000 clients in 100 countries under a single enterprise management and technology infrastructure. By employing a single technology foundation for its consolidated environments, OMG provides an example for how Omnicom organizes and coordinates the activities between its various agencies and companies.
Goals of OMG's unified technology system include achieving management efficiencies and economies of scale. OMG was founded in 2002 in New York City. By 2004, the company had laid the groundwork to combine its IT operations into three regional data centers. This merging of data presented a challenge because OMG's data grew from two terabytes to 15 terabytes in a short period of time, threatening to overwhelm the organization's backup solution. In order to ensure that backup jobs met allotted time windows and performed reliably, CIO Kenneth Corriveau decided to implement Veritas NetBackup[20]. This software enables OMG to consolidate backup monitoring and services to the point where a single employee, only a few hours a week, is able to handle the backup tasks for all of North America. Previously, 2.5 full-time employees were required for the task.

The CIO notes that his focus is on consolidating commodity technologies. The organization is moving in a data-centric direction. Omnicom has also recently established a global document retention policy for email and other electronic documents. To support this, the company employs Symantec Enterprise Vault to help ensure compliance for all its network companies. Enterprise Vault allows OMG to ingest user emails contained in PST files throughout the network into the Enterprise Vault archive repository. This allows the company to require less disk storage, reduce duplicates, minimize data that does not need to be kept, and manage document retention on a global basis. OMG also uses Altiris Client Management Suite to streamline help desk workflow and asset tracking.

In a holding company structure, it can be difficult to implement broad initiatives. Through the example of OMG and its efficient technology infrastructure, it is clear that Omnicom excels at organizing and managing its member companies from a technological standpoint. This is an essential strength of the company because the advertising and marketing industry is driven by data and information.

## Weaknesses

### Declining revenues

Omnicom's revenues have been declining in recent periods. Industry forecasters estimate that global advertising spending will continue to fall, as it did in fiscal year 2009. Liquidity concerts with Omnicom. Potential liquidity needs could exceed the unused capacity on Omnicom's $2.5 billion revolving line of credit. Significant potential liquidity needs could exist in a downside scenario from put-able bonds through 2010, which is two-thirds of Omnicom's debt structure.
In 2009, Omnicom was hit by declines in its automotive, sports and event marketing, and recruitment businesses in the fourth quarter[21]. Profit fell 15.3 percent to 229.6 million in the fourth quarter of 2009 compared to the same quarter a year earlier. Earnings per share dropped from 87 cents to 73 cents[22].

Omnicom CEO John Wren said that those three sectors accounted for 100 percent of the 6.3 percent drop in the company's fourth quarter revenue compared to the same period in 2008. When viewed in terms of organic growth, a measure that factors out the impact of currency fluctuations, acquisitions, and related items, these business areas were entirely responsible for Omnicom's falling revenue. Regardless of the cause, Omnicom's declining revenues impact the company's financial position and its future investment plans.

## Opportunities

### Growth in mobile marketing and interactive advertising

New forms of advertising and marketing are emerging quickly, and companies like Omnicom are well-positioned to take advantage of this growth. The new forms of advertising will be driven by technology, and create incremental opportunities for agencies as marketers attempt to navigate a media and marketing system with a wide array of opportunities. Despite the global economic slowdown, mobile marketing budgets are forecast to grow about 25% in 2010. Total mobile marketing spending is expected to grow from $1.7 billion in 2009 to $2.2 billion in 2010, due to growing mobile internet access. Additionally, mobile advertising revenues in the U.S. and Canada are expected to grow from $208 million in 2008 to $1.5 billion by 2013[23]. Omnicom offers mobile marketing services through its global advertising agencies. Omnicom also started a new agency, Mobile Behavior, in November 2008. This new agency will permit advertisers to better understand consumers' mobile phone behavior patterns and allow for more effective marketing strategies. In the near future, growing demand for mobile marketing services will provide Omnicom with revenue growth and new customer additions.

Another industry segment forecast to have positive growth in the near future is interactive advertising. Interactive advertising most commonly uses online video content as a delivery medium. Revenues from interactive advertising grew 10.6% from 2007 to 2008, reaching $23.4 billion in 2008. The proportion of spending on interactive advertising is projected to rise from 12% to 20% of overall advertising spending over the next five years[24]. Omnicom currently provides interactive marketing services through its digital marketing companies. Growth in the interactive marketing market represents an opportunity for Omnicom to increase its revenues in coming years.

### New business units

Omnicom has been developing new business units in recent periods. In September 2009, the company created Omnicom Digital, a new unit that is charged with leading strategic initiatives across all its digital properties. Omnicom Digital will focus on M&A strategy and technological innovation and development. Omnicom Digital is researching specialty companies as potential acquisition targets, such as firms involved in social media and analytics. In addition, Omnicom Digital signed an agreement with Fox Audience Network (FAN) to develop an online ad targeting and buying platform called Living Segments. This deal will improve Omnicom's digital business. Overall, the formation of Omnicom Digital as a new digital strategy unit seeking beneficial partnerships will allow the company to capture new growth opportunities.

In July 2008, Omnicom announced the formation of G23, a strategic consultancy that addresses the unrealized potential of the global female economy[25]. G23 was created as a high-level strategic solution for clients seeking to make relevant connections with women, whether as consumers, stakeholders, employees, or others. The new consultancy, comprised of preeminent female communications leaders, is an innovative service that highlights Omnicom's commitment to developing original and groundbreaking services and solutions for its clients.

Overall, the development of new business units and the offering of innovative services enhances Omnicom's service portfolio and provides the company with a competitive advantage relative to competitors.

## Threats

### Economic slowdown and international business risks

In 2009, the worldwide economy experienced a slowdown and many companies, including Omnicom, suffered due to declining consumer spending. Contraction in the global economy led to reductions in advertising, marketing, and corporate communications services spending by Omnicom's American and international clients. The decline was broad-based across most industries and geographic areas.

In 2008, Omnicom derived about 48% of its revenue from international operations and the company expects international sales to account for a majority of revenues in the near future[26]. International sales can pose risks including uncertain economic and political conditions, interest rate fluctuations, and international law and regulation compliance issues. Omnicom is also exposed to risks from operating in developing countries, which can include slower payment of invoices, nationalization, and social, political, and economic instability.

Additionally, Omnicom's international business holdings are denominated in currencies other than the U.S. dollar. Fluctuations in exchange rate between the U.S. dollar and currencies, such as the Euro, Pound Sterling, Japanese Yen, Canadian Dollar, and South African Rand, can affect Omnicom's results. These risks may limit Omnicom's ability to grow and efficiently manage its international operations. Further reduction in client spending could adversely affect Omnicom's business and financial position.

## Market Fragmentation

The ongoing fragmentation of media and rise of advertising avoidance will continue to pressure traditional advertisers and marketers into experimenting with new and emerging media types.

Managers of media holding companies like Omnicom have expressed expectations that broadcast television ratings, which have traditionally been an indicator of the fragmentation of mass media, will continue to erode between 5-8% per year for the next five years[27]. While this can be partially attributed to a transfer to cable television viewing, there are also other factors at play. Highly-educated, affluent viewers have become more difficult to reach due to the development of DVRs and the movement of viewership to TV content available on various internet sites like Hulu.

In addition, influential consumer magazines and newspapers have also lost their ability to aggregate large audiences. Magazines like Time, Newsweek, TV Guide, and Better Homes & Gardens once had the potential to influence large segments of American consumers. It is also important to consider the impact of declining newspaper circulations on the advertising and marketing industry. The attractiveness of newspapers largely revolved around a large audience reach potential, coupled with a perishable media type with quickly renewing marketing and advertising opportunities. However, in recent years, many metropolitan print newspapers have faced double digit circulation declines.

Fragmentation in the global advertising and marketing industries poses a significant threat to companies like Omnicom. In order to recapture revenue from traditional media advertising, Omnicom may have to offer new services like packaged combinations advertising for both the print and online editions of newspapers. Technological advancements and changing consumer preferences are drastically altering the advertising and marketing businesses, and Omnicom could suffer if it does not recognize these threats and take steps to mitigate them.

# Strategic Recommendations

## Overview

Vector Strategy Group has isolated Omnicom's primary challenge as being the changing landscape of the advertising and marketing industry. As innovations in technology and media continue to emerge, Omnicom must alter its strategy to include the changing nature of clients' preferences and the growing demand for digital and alternative marketing and advertising. This strategy can be enhanced by incorporating Vector's short-term and long-term strategic recommendations, as outlined in the following sections.

## Short-term recommendations

In the short-term, Omnicom should focus on preserving revenue streams and protecting against a further decline in revenues in 2010. In order to achieve this goal, Omnicom should reduce costs and focus on updating its business offerings to reflect the changing media environment. As described in the SWOT analysis, Omnicom's technology infrastructure contributes to the company's high efficiency levels and minimizes office and general expenses. By spreading the cost-saving techniques of Omnicom Media Group (OMG) to the rest of the conglomerate, the company as a whole would benefit. Omnicom relies on managing enormous amounts of data, and streamlining the data storage technology for all the company's agencies would reduce labor costs.

Additionally, Omnicom should start exploring new channels to reach its clients. During the economic downturn, advertising spending has fallen as companies attempt to cut costs. In order to remain financially strong while clients pull back their levels of advertising, Omnicom has to branch out and expand its service offerings. As a multi-national, multi-agency conglomerate, Omnicom is a traditionally structured media company that primarily offers conventional advertising services. In order to diversify its offerings and enter new advertising markets, Omnicom has two options: strategically acquiring existing firms or expanding the services of its already-established agencies. In the short-term, Omnicom can research potential acquisition targets and formulate a plan for diversifying service offerings in the future. Omnicom should set goals for entering new service lines and refine its mergers and acquisitions strategy accordingly.

## Long-term recommendations

As the focus shifts away from traditional media advertising, fields such as mobile marketing, digital media, and social media marketing are gaining importance in today's markets. Fragmentation in media continues to affect Omnicom's business. As such, the company would benefit from looking to acquire regional digital advertising agencies and other strategic targets.

By divesting underperforming agencies and strategically acquiring new businesses that add to the diversity of Omnicom's current offerings, the company would be well-positioned to perform well in the industry. One key to Omnicom's acquisition strategy should be to ensure that the potential target would add to the value of the parent company overall. Contemporary young agencies can appear to be innovative, but that quality alone does not mean every new company would be a good fit for Omnicom's umbrella of agencies. Omnicom's mergers and acquisitions strategy should reflect the goal of capturing value above and beyond the amount paid. Although a diversification overhaul might mean risking certain clients, Omnicom would be a stronger industry player overall.

In response to the fragmentation of media, Omnicom should prepare its agencies to provide a complete package of services and advertising solutions for its clients.

Although traditional media advertising is losing ground in today's markets, Omnicom could still capture revenue and market share by creating packaged combinations of marketing and advertising services. For example, Omnicom could provide a single client with television and print ads, online and mobile marketing, and social networking. Omnicom could also offer discounts or special pricing for package deals, and agencies with different specialties within the company could coordinate with one another to provide multiple services. This strategy would enable Omnicom to attract clients seeking a variety of advertising services, and the company's strong brand name would signal a high quality of service to potential and current clients.

A final long-term suggestion for Omnicom is to reconsider the company's debt financing strategy. Omnicom's debt levels are much lower than the industry average. Omnicom's debt-to-equity ratio, at 0.53, is far below that of WPP (0.91) and Interpublic (0.83)[28]. Although a low debt-to-equity ratio corresponds to a less risky investment, this number suggests that Omnicom could stand to benefit by taking on more debt. By increasing leverage, Omnicom could gain by acquiring debt - either in the form of a loan or other borrowings - and reinvesting the borrowed money. Although this plan would correspond with a higher level of risk, it would let Omnicom take advantage of the increased profits that financial leverage can bring. This would optimize the company's debt-to-equity ratio without signaling a weaker company. There is also a theory called debt signaling, which states that an announcement about a firm's debt can be used as a signal of the stock's future performance. If Omnicom were to take on more debt, it would be making a commitment to pay interest on the borrowings. In that sense, Omnicom would be sending a signal that it is in a stable financial situation, which would be reassuring for investors.

Overall, Vector Strategy Group believes Omnicom is well-positioned in the current market as one of the world's largest advertising and marketing holding companies. These strategic recommendations represent modifications that could be made to Omnicom's business plan in order to take advantage of the changing nature of media and the evolution of the marketing and advertising industries.

# End Notes

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