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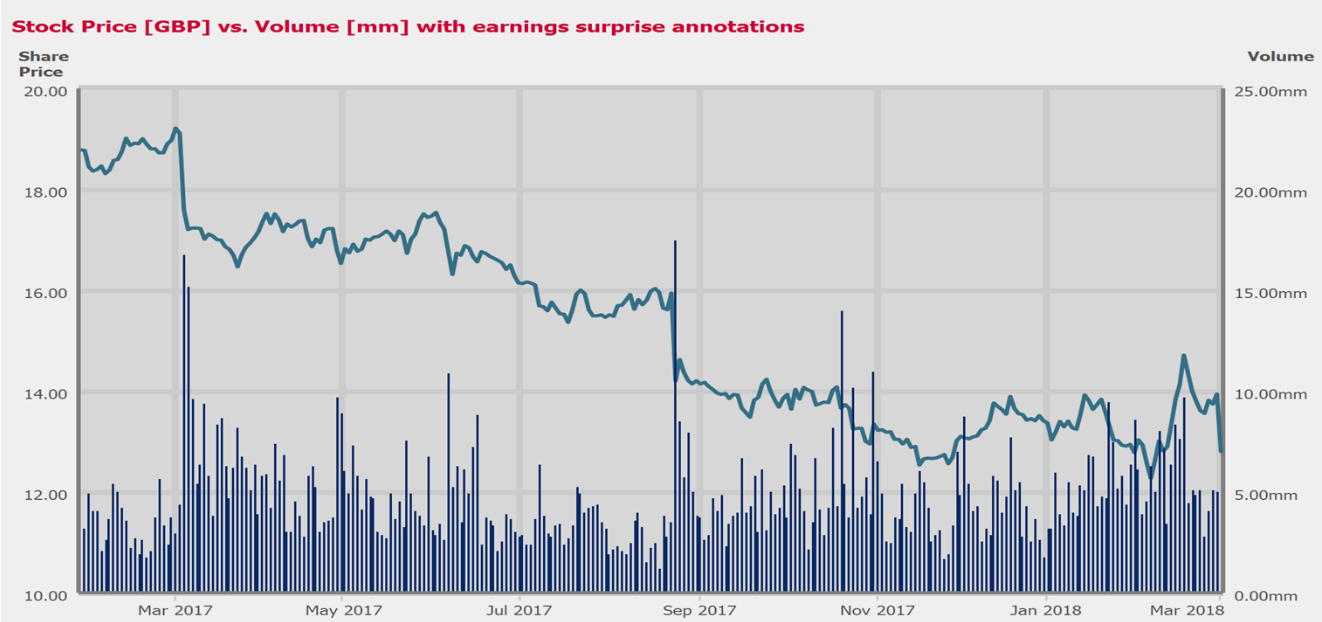
FY 2017 Earnings Call Transcripts

Thursday, March 01, 2018 9:30 AM GMT

S&P Global Market Intelligence Estimates

	-FQ4 2017-			-FQ1 2018-		-FY 2017-			-FY 2018-
	CONSENSUS	**ACTUAL**	**SURPRISE**	**CONSENSUS**	**SURPRISE**	**CONSENSUS**	**ACTUAL**	**SURPRISE**	**CONSENSUS**
EPS Normalized	-	-	-	-	-	1.21	1.20	▼(0.83 %)	1.20
Revenue (mm)	4273.00	4212.80	▼(1.41 %)	3599.00	▲9.20	15279.74	15265.40	▼(0.09 %)	15458.42

Currency: GBP
Consensus as of Mar-01-2018 9:12 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FY 2017	1.21	1.20	▼(0.83 %)

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Call Participants

EXECUTIVES

Adam Smith

Carla C. Hendra
Vice Chairman, Chairwoman of Ogilvy Global Strategy & Innovative Practice & Chairman of Ogilvyred

Irwin Gotlieb
Former Chairman

Mark Read
CEO & Executive Director

Martin S. Sorrell
Founder

Paul W. G. Richardson
CFO & Executive Director

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Presentation

Martin S. Sorrell
Founder

Good morning, everybody. So welcome to our 2017 preliminary results. As usual, we've got an extensive presentation for you. We are going to cover the results. Paul is going to cover the results for 2017 in summary, then Adam Smith, as usual, will look at this year and next year. We'll then cover what we believe are the most commonly asked questions about the industry and ourselves, and then maybe some uncommonly asked questions as well. We'll talk about our structural response to those issues, and then outlook and conclusions.

And we're joined by Mark Read here in London, who leads Wunderman. I think we have Carla Hendra in New York at some unearthly time, who is part of Ogilvy, Ogilvy consulting, based in New York; and Irwin Gotlieb, who I think is on the West Coast, so slightly better for him, but not much better, obviously, who is Chairman of GroupM. So we have a group of people, 2 on the phone and the 4 of us here. So firstly, over to Paul.

Paul W. G. Richardson
CFO & Executive Director

Okay, thank you, Martin. So I will cover around half an hour, just the results for 2017.

Just before I start, there are some definitional changes we've had to make, and actually, it's footnoted on the bottom of Page 1, where instead of the term net sales, we are using revenues less pass-through costs. It's calculated in exactly the same way. It is just a preferred definition of the same measure. So I'll just say that before we start.

So on a reported billings basis, we were up 0.6% at GBP 55.5 billion, down 3.9% on constant currency, and down 5.4% on a like-for-like basis. On a revenue basis, our reported revenues are up 6.1%, at GBP 15.265 billion, up 1.6% on a constant currency basis and down 0.3% on a like-for-like basis. Revenue less pass-through costs, not easy to say and is exactly the same as net sales, was up 6% on a reported basis, 1.4% on a constant currency basis and down 0.9% for the year on a like-for-like basis.

Reported headline EBITDA was up 4.7% at GBP 2.534 billion and up 1.2% on a constant currency basis.

Reported headline PBIT was up 4.9% at GBP 2.267 billion, up 1.5% on a constant currency basis and reported revenues less pass-through costs margin was 17.3%, down 0.1 margin points from the 17.4% reported last year, but was flat on a constant currency basis because when you adjusted last year's 17.4% at current exchange rates, you did get to 17.3% and was flat on a like-for-like basis. It was in line with our revised forecast in the second half of last year.

Headline diluted earnings per share were up 6.4% at 120.4p and up 2.7% on a constant currency basis. And dividends per share of 60p, i.e., approximately a 50% payout ratio, was up 6%, in line with our target of a 50% payout.

Our net debt on a constant currency basis was up GBP 584 million to just over GBP 5.1 billion, reflecting significant net acquisition spend in the back end of 2016, specifically Triad, where we did spend GBP 300 million in November 2016 that didn't have an effect on the '16 average but obviously had a full year effect on the '17 average. Share buybacks and dividends, in line or greater than last year, and average net debt therefore coming in at 2x EBITDA, which is the top end of our 1.5x to 2x range. Our share buybacks of GBP 504 million or 2.5% of share capital was up from the 2% purchased last year and our target each year is to purchase or repurchase between 2% and 3% of shares, considerably more than dilution, which is 1% or less each year.

Net new business billings at GBP 6.3 billion in the year continued the good overall performance seen in the first 9 months and was leading positions in the net new business tables for last year.

Return on equity was up strongly, at just under 17% or at 16.9% to be precise, up from 16.2% a year ago. And compared to a similar weighted average cost of capital to last year, just lower at 6.3%.

So turning now to some of the headline performance versus consensus, we were slightly light versus consensus on the full year revenues less pass-through costs at down 0.9%. That did lead to about GBP 50 million behind consensus on the revenues. That flowed through to the PBIT numbers. The finance cost, we did actually achieve exactly the same interest cost and finance costs as last year, slightly better than consensus. And at the PBT level, our PBT of GBP 2.093 billion was slightly [high in] consensus of GBP 2.109 billion. With a benefit of slightly less minority interest and good share buybacks having an effect on the shares in issue, the diluted EPS of -- at 120.4p was very much in line with consensus of 119.8p. As I mentioned, the margins, on a constant currency basis, was flat with last year, but down 0.1 on a reported basis.

So again, a summary of some of the headline numbers. Revenues, GBP 15.265 billion on a constant currency basis up 1.6%. Revenues less pass-through costs, about GBP 2 billion less at around GBP 13.140 billion. Margins, I've mentioned; EBITDA, I've mentioned. Tax rate has gone up, principally due to the changes in the U.K. tax legislation. You'll see later we are taking a tax credit for the U.S.A., but in fact, the change in corporate tax rates is having a negligible effect on our U.S. taxable or taxes paid in future years.

Overall then, the diluted earnings per share of 120.4p and a dividend paid of 60p for 2017. Average net debt I discussed, and headcount actually throughout the year was down, both on average, 1.5% and on the closing headcount, down 1.7% compared to a year ago.

So in terms of the revenue growth, this is the bridge from last year. On a like-for-like basis, revenues were down 0.3%. Acquisitions added 1.9%. Foreign exchange added 4.5%. So overall, revenues were up 6.1%. For revenues less pass-through costs, previously known as net sales, started the year at GBP 12.4 billion, was a decline on an organic basis or like-for-like basis, was minus 0.9%. Acquisitions throughout the year added 2.3% to revenues, less pass-through costs and foreign exchange added 4.6%. So overall, revenues less pass-through costs for the year grew from GBP 12.4 billion to GBP 13.1 billion.

In terms of foreign exchange, we've had 2 years where it has been a benefit to the group's results. So in 2016, it was approximately a 10% benefit to revenues and revenue less pass-through costs. In the first 3 quarters, it was a benefit of this year. And in the final quarter, it was a headwind of around 3% to 3.5%. But overall for the year, it was a benefit of around 4.5% to revenues, and 4.6% to revenues less pass-through costs. Taking the current exchange rates and looking out at 2018, we are expecting around a 4% headwind or minus 4% impact on foreign exchange to the 2018 results.

So the second change, which I'll come on to is the way we are presenting the very top of our profit and loss account on a statutory basis only. There is a slide to explain, but what you'll see here now is revenues of GBP 15.265 billion and what is called cost of services of GBP 12 billion, which are those costs directly attributable to generating that revenue. So a very strict definition. This leads to a gross profit number of GBP 3.175 billion. And then in general and admin costs, which on average are around 7% of revenues, we have to show separately. The operating profit of GBP 1.908 billion is a statutory operating profit. You see the strong improvement to the income from associates coming through in 2017. And on balance, my view is that in 2018, that will not be significantly different, given what we know about 2018 and our associates.

On PBIT, we're looking at on a statutory basis of GBP 2.22 billion. On the finance cost, there is a schedule in the leave-behind that breaks out the finance cost and all the various changes to financial instruments that we have to put through in that particular line as well, explained in detail for you.

Tax, as you see there, there's a credit of around GBP 206 million compared to the prior year. That's a credit on deferred tax liabilities, because our future liabilities under U.S. GAAP are now measured at 21% as opposed to 35%. It has led to a one-off credit to the tax charges here. I'd say in underlying terms, I'm not expecting the change in U.S. tax legislation to make a material difference to the group's tax rate.

So in a statutory reported basis, you have reported diluted earnings per share of 142p, up nearly 27% compared to a year ago.

So the change in the format or the presentation of the P&L, we've had -- we've moved from a nature of expense, which is the right-hand side of the page, or the old format, where we showed revenues less direct costs or pass-through costs, which were, as we previously explained, those costs directly associated where we act as principal on media buying and the pass-through costs of market research, where we came out with a subtotal of net sales. And then we had the other operating costs, leading to an operating profit for the year and PBT.

You can see on the left-hand side, the new display that we'll follow going forward, which is called a functional approach to the nature of the P&L. But actually, all the numbers are identical at the operating profit and the PBT level. So it's just a reclassification of costs between direct and operating in the old format, between those and cost of services and general admin in the new format. Purely presentational, no other changes.

So in every other respect, either revenue less pass-through costs, i.e., the net sales number, is the same; headline PBIT is the same; the margin is the same. What you have below and broken out for you is in the headline G&A, you have what are called the underlying cost of general and administration, which is around 6.7% of revenues of the group, and other items, like intangibles, goodwill and exceptionals, get dumped into that GBP 1.267 billion number. Again, we have a slide in a second on exceptionals. So that's a change, format only, nothing material.

So in terms of the headline income statement, this is how we will continue to display it, very similar to how we displayed it in the past. So revenues of GBP 15.265 billion on a constant currency basis growing by 6.1%. Revenues less pass-through costs, previously known as net sales, of GBP 13.140 billion. Operating profit, GBP 2.154 billion, was down 0.5% on a constant currency basis and the PBIT level at GBP 2.267 billion, constant currency PBIT was up 1.5%.

Finance costs were flat with last year. Taxes were up from 21% to 22%, leading to profits after tax on a constant currency basis of GBP 1.633 billion, up 4% on a reported basis and up 0.5% on a constant currency basis. Non-controlling interests were slightly lower. Therefore, profits attributable to shareowners grew at 1.1%, and then with the benefit of the share buybacks, diluted EPS grew at 2.7% to 120.4p.

So in terms of exceptionals, we had gain on disposal of investments and subsidiaries at Asatsu, and again, you will see in the footnotes, of the GBP 129 million, the principal gain related to Asatsu, which is a gain of GBP 92 million. And in addition, we had a gain on Infoscout and others. That in total was GBP 129 million. We have taken some investment write-downs, the principal one being comScore, again identified in the back at around just over GBP 50 million. And then we have had some restructuring charges taken 2017, in total of GBP 57 million, broken out in the footnotes, were predominantly comprised of severance of GBP 34 million and IT costs, including the impacts of the cyber attack, of around GBP 13 million in total for 2017. So net-net, at the subsidiary level, there is an exceptional loss of GBP 24 million, there was a further GBP 1 million exceptional loss in associates, so at the group level, it was GBP 25 million.

Looking at currency and how we would have performed if we were in the various currencies. So looking at the second column, the revenue less pass-through costs, the like-for-like growth was minus 0.9%. Acquisitions added 2.3%, and therefore, on a constant currency basis, growth was 1.4%. Foreign exchange added 4.6% to revenues less pass-through costs and around 3.7% to headline EPS for the group. So overall, our reported numbers in sterling showed growth of 6%. If we were a dollar-reporting company, our overall reported growth in revenues less pass-through costs would've been 1.6%. If we were a euro-reporting company, our growth in revenues would have been minus 0.7%. And if we were a company reporting in yen, our growth would've been 4.8%.

Turning now to the performance by discipline of the business, showing both the revenues, GBP 15.265 billion and the revenues less pass-through costs, both on a reported constant currency and like-for-like basis. I will focus on the like-for-like performance on revenues less pass-through costs. And I just want to remind you of the shape of how 2017 performed in terms of quarter-by-quarter, then I'll give you the specifics about how the half year was compared to the full year.

So in 2017, the first quarter, the like-for-like growth in revenues less pass-through costs was plus 0.8%. The second quarter was disappointing, it was down 1.7%. So the first half of this year, we reported revenues less pass-through costs on like-for-like basis of down 0.5%.

The second half has been harder. So quarter 3, we saw revenues less pass-through costs down 1.1%, and quarter 4, disappointingly, we saw revenues less pass-through costs down 1.3%. So the second half revenues were down 1.2%, which actually is in line with where we are in January 2018.

So overall for the year, our full year revenues are down 0.9%, not seeing a pickup in quarter 4 that we had hoped for.

Now turning to advertising and media investment management, which is representing 47% of the group, and on a full year basis, had like-for-like net sales or revenues less pass-through costs, decline of 2.3%, slightly higher than the half 1 like-for-like decline of 1.7%.

In data investment management, which represents 18% of the business revenues, we saw a decline in the first half of 1.9%, but an improvement overall and on a full year basis, the decline was 1.3%.

In public relations and public affairs, we saw a full year performance of plus 0.2%, slightly lower than the rate of growth we saw in the first half, where the growth was 1.8%.

And in brand consulting, health and wellness and specialist communications, which represents just under 28% of the business, we saw a full year revenue less pass-through costs of plus 1%, very similar to that achieved at the half year of plus 1.1%. So overall, for the group, the first half we were down 0.5% and on a full year basis, we were down 0.9%.

Turning to do exactly the same analysis by geography. So in North America, which represents 36% of the business, saw overall revenues less pass-through costs decline 3.2% overall for the year, slightly higher than the half 1 rate of minus 2.2%. The United Kingdom continued to perform well, it is 13% of the business, on a full year basis, it had a revenue less pass-through costs growth of 4.8%, having been growing at 3.8% in the first half. In Western Continental Europe, it is just under 21% of the business, we saw flat growth overall for the region, for the full year, very similar to what we saw in the first half, where we were down minus 0.3%. And similarly, in Asia Pacific, Latin America, Africa and Middle East and Central and Eastern Europe, 30% of the business, we saw revenues down 0.8%, similar to what they were down in the first half this year, minus 0.3%.

So turning now to one of the comparisons we make, and we can only really do this on a revenue basis, as opposed to the revenues less pass-through costs. So it is somewhat distorted. But I think there, you can see a consistent trend when you add the 2 half years, the half 1 '16 and the half 1 '17 combined, in our case, on revenues of 4%; the half 2s of '16 and '17, when combined, show revenue growth of 1.5%. You can see the trend across the industry of softening growth and somewhat patchy growth of some of our competitors. So there is a general trend compared to the '15 and '16 run rate and the '16 and '17 run rate, of softening of the revenues.

In terms of margin performance of the business, it is still a strong margin business overall. And looking at the advertising and media investment management business, which is just 49% of the profits of the group, margins were flat at 19% at the full year, similar to where they were at the half year, where they were flat at 15.3%. So we do have a very strong second half. We met the profitability we were hoping for in terms of margin in the second half of the year. The data investment management business, our second-strongest margin business, did see a margin decline at the half year of 0.5 margin points and that has continued to flow through into full year results, the margin is going from 17.6% to 17.1%, representing 15% of the business.

Public relations and public affairs, 8% of the business, traditionally a good margin business as well, it did have a slightly softer second half and the margins overall for the discipline were down from 16.7% to 16.1%.

In brand consulting, health and wellness and specialist communications, overall margins were down 0.1% to 15.3% versus 15.4% a year ago and a fairly mixed performance within some of that division.

In terms of geographies now, again, our strongest margin region is North America. It saw a margin improvement despite the decline in revenues less pass-through costs, improving the margin from 19.4% to 19.5%. The U.K., on the back of the strong performance, has seen an improvement in margin from 16.5% to 16.6%. Western Continental Europe of basically flat revenues, saw margins held or down 0.1 margin points from 14.5% to 14.4%. And Asia Pacific, Latin America, Africa and Middle East and Central and Eastern Europe, I think probably the region where we were most disappointed with the quarter 4 performance, we did see a margin decline of 0.5 margin points from 17.2% to 16.7%.

And talking about how we did perform in the fourth quarter versus the full year. Here's an analysis of our subregions, on a revenue basis first, followed by a revenue less pass-through costs. So revenues can be distorting, as I mentioned here. So in revenue terms, we had a strong -- a better fourth quarter in North America of plus 1.6% despite a difficult year. On a revenue basis, which is affected by those pass-through costs, we had a good performance in the U.K. and Latin America. But overall for the year, on a full year basis, mature markets were down 0.5% and fast-growth markets flat. I think on a meaningful basis, the revenue less pass-through costs, you see here where the fourth quarter performed well and where the full year basis performed in trend. And there is disappointment across our North American business in the fourth quarter on net sales. Latin America, which had, had a good year, was still up, but marginally at 3.6%. And then we're basically flat in Western Continental Europe, down in Central and Eastern Europe in the fourth quarter and down in Asia Pacific. But overall, we were down 0.9% in the mature markets and down 0.8% in the fast-growth markets for the year.

Looking at some of the major markets or the top 6 markets for the year, representing 68% of the revenues. Overall, they were down 1% on revenues and down 1.4% on revenues less pass-through costs. U.S.A., you can see here, the change from growth in '15 to '16, to a decline in 2017. U.K. has continued the good growth. Greater China is actually slightly better than we were at the 9-month stage, where we were down minus 4.6%, but it's not as good as we'd hoped in the final quarter and it was down 3.2% on the full year. Germany has had a fairly tough year all year, partly through client losses, and we were basically flat after 9 months; we are down 1.3% on a full year basis.

AUNZ, we're basically down, but you will see in the reported numbers from the public company, which had a good margin performance and a relatively low-digit but solid EPS performance in WPP AUNZ, reported earlier this week. And in France, actually, we've seen some modest improvement continue this year versus last year and before.

In the BRICs, as we mentioned, Greater China, somewhat disappointing compared to what we'd hoped for, but down 3%. India, definitely affected by GST and demonetization, had a very strong first half. We were up 6% to 7% after 9 months, but had a softer fourth quarter. Brazil returned from decline to growth in '17 versus '16. And Russia is a bit mixed by quarter, to be quite frank with you, and that portrays a sort of mixed quarter-on-quarter performance in Russia.

So overall, here's a summary of our -- the trade estimates of major new business wins throughout 2017. As I mentioned previously, media tends to dominate the absolute billings numbers. And what we've shown here is all the wins and the accounts, those which are shaded have come through in quarter 4 and then you see a number of transfer wins coming through in the fourth quarter, actually, to -- sizable wins of GBP 400 million for media coming -- Mediacom coming, one in Europe, one in North America. And if I turn the page, smaller wins, but some very significant, so the very significant win, Australia, of the Victorian government, again for Mediacom. And actually, they have picked up and expanded their relationship with AB InBev in Latin America in the fourth quarter.

And now turning to losses, but unfortunately, we were not able to hold on to the business in the U.S.A., Australia, India and that has slightly dominated the loss in the fourth quarter.

So the wins and losses in the fourth quarter were fairly evenly balanced. And as we go through our numbers, so this is our internal estimates of business performance, it's a very credible number of GBP 6.3 billion compared to the GBP 6.7 billion last year, but we were strong for the first 3 quarters, but somewhat soft or neutral in quarter 4 on the new business.

Account wins since January 1. Three wins coming through, not major in scale in terms of billings, but all very meaningful: NAFTA is in North America, which includes U.S.A., Canada and Mexico, just for clarification; and 2 global wins, 1 for Bose, 1 for Adobe.

Turning now to cash. We have to start the cash flow we have done traditionally using the statutory profit as opposed to the headline profit, so it is slightly distorting, and I can take people through what the differences are, if necessary. But the key measure is whatever we generate in operating profit, we generate in cash after depreciation and non-cash compensation, interest paid and taxes. So still a very strong flow-through of cash generated versus the operating profit. In terms of uses of cash, we are continuing to up the level of capital expenditure, partly on property through the co-locations and partly through the software applications we're developing using third-party resources, which in certain cases, we do amortize over a 3-year period. So there is considerable expenditure and development going on in that side. On acquisitions overall, there is a major change this year. So last year, we spent in total GBP 697 million. Net initial payments were quite significant at GBP 605 million, earn-outs less so at GBP 92 million. This year, you'll see in more detail our spend on new acquisitions actually was GBP 326 million, but we had disposals where we realized proceeds of GBP 296 million. So overall, a net spend of GBP 30 million. With the earn-outs going through of GBP 200 million, it meant that actually, our acquisition payments net-net were about GBP 400 million less than the year before.

With that, net kind of -- net cash inflow before distributions of GBP 1.3 billion compared to GBP 888 million last year, we basically distributed GBP 1.2 billion through dividends of GBP 752 million and share buybacks of GBP 504 million, leaving a net cash generation for the year of GBP 55 million versus last year of minus GBP 156 million.

So in terms of -- the currency has had a negative effect on the balance sheet loss; it has a positive effect on the earnings. So on a reported basis, the average net debt is around GBP 800 million higher at GBP 5.1 billion versus GBP 4.3 billion reported. However, if you were to take the 2016 numbers and adjust them into 2017 rates, the difference is GBP 584 million, i.e., GBP 5.1 billion versus GBP 4.5 billion, or 13% different. We were better at the end of the year, not simply because, but predominantly because we received GBP 250 million from the sale of our stake in ADK around the 15th of December. That will have a significant benefit on the average net debt in 2018. It also has impacted and benefited the net debt number at the end of the year, which is traditionally strong compared to the average. So our coverage ratios are strong at 13x interest and average net debt-to-EBITDA, as I mentioned, is at 2x and the trend of around GBP 4.5 billion is GBP 300 million to GBP 400 million worse, but in line with the 10% to 7% difference compared to a year ago, after the first 7 weeks of this year.

So if we look at where we are on our range, and we do use the average, which is, I think, the fairest and most appropriate measure of our average net debt-to-EBITDA is at 2x. If I was to use the year-end number, it's at 1.77x. This is the top of the range we prefer to stay within.

And in terms of maturities, just one maturity coming up in the near future, a Eurobond, EUR 252 million, and the bank revolver below is actually an AUNZ facility of AUD 520 million coming up in March '19. But our average coupon is around 3% and average maturity profile is 9.5 years.

So in terms of where we were with our uses of free cash flow, as I explained before, in terms of net acquisition spend or even gross acquisition spend, we kept within the GBP 300 million to GBP 400 million, spending GBP 326 million. But through the proceeds of disposals, the cash flow for the year had a net outflow of GBP 30 million only compared to GBP 605 million the year before. Share buybacks, mid-range of our 2% to 3% per annum, at 2.5%. Dividend increase in line with the growth of EPS and therefore, the 50% payout ratio maintained for 2017.

And with that, I happily hand over to Adam.

Adam Smith

Thanks, Paul. Right. I'm just going to run through our current forecast for ad expenditure, that's a total tonnage of ad investment worldwide. We publish this forecast in December. We do it twice a year. The next one will be out, I think, by the end of June.

So we think that the outturn in 2017 was 3.1% total growth in global ad investment and this had come down a shade from the prior year, from 4.4%, which we'd had an improving global outlook, but with fixed investment looking sluggish and we were sort of neutral on Trump. So by mid-year, we pulled back to this 3% figure, with a bit of a downgrade in China and weakness emerging in some categories. And since then, China has obviously stabilized and the macro has improved, but sort of the micros around advertising pricing power and sales volumes are still under pressure.

So we came into 2018 expecting 4.3% growth, which has been stable despite what one might argue more supportive indicators across business and consumer and trade. Geographically, China and Japan are now strong and then the Eurozone is accelerating. Worries might include wages rising at the expense of profits and the commodities cycle, which was certainly warming up when we made this forecast.

The relationship of GDP to advertising throughout this recovery cycle measured advertising intensity, that is the share of advertising in the global economy has fallen from 0.75 to 0.70. And the growth in advertising is lagging nominal GDP, on average about 1 percentage point.

We saw this convergence, where the lines touch, in 2016, despite personal care falling 5% worldwide, quite a headwind low at time, and the other staples and categories offset this, implying that the divergence which we see again in 2017 was rather more general. And I remember back in August, at this event, we were pointing out that 25 of WPP's top 60 clients were down in the first half. So I wondered whether we might be under-measuring advertising expenditure to explain this gap, and I was looking at the cost of how much working media expense goes in what we call tech tax, how much advertisers are spending now to support and analyze their digital revenue, and we've been doing a little bit more work on that now, and we've come out on an average of 19% on display -- digital display advertising, 19% of the budget, wherever you may choose to take it from, is going on technology. And there's also a little sliver going, which generally has to support search, in the order of about 2% of the working media investment. Now those would probably put $20 billion back into the digital measured ad spend, if we were doing it that way. The other issue is under-measurement in some countries of digital, which is certainly the case. India and Brazil are 2 examples of that. But even allowing for that, conservatively, might add another GBP 10 billion, we are not going to close this gap. So it must be from other causes and perhaps including a sort of compression of legacy ad budgets and some sustained diversion of brand support into promotion.

The shape of the advertising recovery since 2009 in real terms looks like this. And the biggest influence is probably the shift of advertising investment from countries which have a relatively heavy advertising intensity to faster-growth markets, which only have a rather lighter intensity. Those figures are about 0.8% of the economy in developed markets, and in the faster-growth markets, about 0.6%. So the old or the mature world, which is currently 65% of the measured ad economy, by the end of last year, had recovered from at this base point of 2009, to index at 107. It is losing share point of advertising dollars at the rate of about 1 percentage point a year to the faster-growth markets. But the top line here, the orange one, is the faster-growth market, which really has been faster growing, currently indexing at 150 relative to 2009. Putting a little bit more detail into these numbers, I wanted to pick out Japan, where we can see that one effect of Abenomics has been to lift Japan above the developed market average for a good part of this recovery, and Japan is still 8% of measured global advertising, so it carries a bit of heft. The Eurozone has shrunk 1/4 in real terms since 2009. Yes, it's accelerating now, but it is hampered by actually, the lowest advertising intensity in the world, which is 0.43%, part of which arises from the fact it lacks, what I would call, digital density. Only 30% of its ad investment is currently going into digital, versus the global average of 36%.

Now if we look at the main contributors to the growth we expect in 2018. What I notice is the growth has become more simultaneous from last year, we saw 13 countries plus the Gulf states collectively going negative. This year, we only have 6 markets expected to go negative, which also means we are reducing our dependence slightly on this group of markets. The U.S. remains resistant to all macro encouragements, it would seem, with advertisers remaining focused on reducing expense, increasing efficiency, scrutinizing digital. China has steadied. In 2017, the government's priority was to curb financial risk, which included apparently successfully conducting heat away in the real estate market from the bigger cities into the smaller. But demand for consumer goods is becalmed, household income has been slowing since 2012 and GroupM finds that the propensity to try new products, and Kantar also, the propensity to try new products, has fallen markedly.

Auto sales growth is slowing in China and briefly went negative in 2017, although the premium end of that market remains healthy.

So one effect of rebalancing away from exports and investments has helped the percentage of retail sales in the Chinese economy to rise steadily into the higher 40s now. Argentina appears among this group the result, the dividend of political stability and an appreciating peso.

India is seeing past the disruption of reforms, although there are echoes of China's moderation demand for CPG and auto. But generally, urbanization and rising wages support strong consumer growth there, and therefore, the ad outlook. One interesting thing that India raised was the, what you might call the channel shift, the demand of CPG through online outlets as opposed to offline, which is something also China highlighted.

The U.K. market is driven, really, entirely by performance-minded digital advertising. And as a footnote, I would mention Russia, which is growing strongly but not big enough to break into this list quite. Brazil's ad recovery and economic recovery generally is postponed to beyond our forecast horizon of this year, as austerity bears down on the massive population.

This I thought was a coincidence worthy of remarking on. The apparent correlation of digital advertising investment and the volume of e-commerce, which is currently at a ratio of 8%, so 8% digital advertising relative to e-commerce. And if one were to assume that, that ratio holds, then it would imply 14% growth in e-commerce, our digital forecast would imply a 14% growth in e-commerce in 2018. Well, we've just finished specifically forecasting that figure and we've come to 15% in a report we'll be publishing I hope in March. E-commerce, the volume of e-commerce grew 17% in 2017, in line with our forecast, taking it past USD 2 trillion. We're now heading for USD 2.5 trillion in 2018, which would represent about 10% of all retail. In China, 16%, and obviously, something more like 100% of all growth in retail.

The average Internet shopper in 2018 will, we think, spend just a shade under $1,000. That's a 10% increase on the spend in 2017, which was itself a 10% increase on 2016. And what I found interesting about those 2 figures is for the first time, that's substantially faster than the growth in Internet penetration, which is about 5% in the 40 countries that we monitor.

Byron Sharp is telling us that big brands are not dying, but may be wasting money on unproven new media. But against this, obviously, we have plenty of real-world evidence of nimble online challenges, flexitarians and picky millennials delighting at the infinite shelves of online. And why should there be one truth?

In November 2017, Procter & Gamble said it spent close to 1/3 of its budget on digital, but in some markets, 50%, and on some brands, 100%. We might also see a new kink in the product life cycle, as web endemics find limits to what they can sell in the digital domain. SocGen came out with an interesting figure, that there might be a sales ceiling of between $100 and $150 billion before such brands would have to seek reach outside the direct-to-consumer channels to grow sales. In other words, to buy fame elsewhere. And I certainly notice that the web-endemic companies which use TV in the U.K. are all household names. Published ROI results, the few that one sees, suggests that advertising outcomes on digital media may be more polarized than they are in traditional media, which suggests possibly a need for management and perhaps scrutiny of the media mix. There's also inflation occurring in digital media, which is also polarized. We have at the top of the purchase funnel, across the world, video prices warming up in digital as advertisers try and improve viewability scores, essentially quality of audience. And at the bottom of the funnel, we see inflation in cost per click, as the old problem of last-click economics tends to cause advertisers to bid for -- all to bid on the same audience, which is something GDPR may exacerbate, but that might come up later, of course.

Anyway, I will just move on to the question posed: How big can digital get?

Well, what I've done here is rank the world's advertising markets according to their digital advertising intensity, put them into quarters.

And so in 2018, we have the topmost slice, which for the top quartile of the most heavy digital investors, putting a 48% share of advertising budget in digital and they collectively represent about 30% of global advertising. So one might look for points of resistance among this group. And China, GroupM China, put it well. It says that pure online or pure offline bonus is almost gone. The best opportunity is in combination. GroupM China calls this Internet-plus and it's usually just part of a wider retail reform, shortening of time to market and integrating omnichannel better.

So moving to the next quartile down, where digital occupies 30% of advertising investment, this represents half of the global ad economy. In the lower quartiles, the 20% -- the 12% and 21%, the main problem is under-measurement in India, where you measure large advertisers' online spend; and Korea and Brazil, only measure desktop, for instance. So I conclude from this that unless something happens to stop it, then digital global share has a momentum that would reach 50% of global advertising, which at the current rate would take about 7 years. Now one must always caveat these with the qualification that digital is becoming a more blurred definition and there's quite a bit of TV money in there now, which is masquerading as digital. So where might this share come from?

TV's growth in 2018, about 2.2%. Its share isn't shifting very much. It's losing about 1 point a year to digital media essentially, but without China, it's stable. TV hours remain healthy. We've just done another check on TV hours as part of our annual interactions suite. And the viewing hours remain stable. And we also asked our markets to estimate what share of video traditional incumbents were taking, because this is something that is generally not measured. And the figure is averaging about 75% of total video time. And they estimate also that the, what I call the disruptors', share of video time is about 19%, and that's something I'm going to try and generate comparisons on in future years. But essentially, what's happening with the media day is what's been happening for a long time, is that online, the online day is stretching and that's the main dynamic within the market.

However, where might share come from in this loose definition of digital TV and so on? Out of home is becoming more versatile, and therefore, I think more resilient. It's adaptable now for weather and day-part and geo-targeting in its -- in addition to its established virtues, which of course include freedom from editorial context. So it's growing share in 2018, 6.3% of measured advertising, we think, the highest it's been since 1993 and the only medium growing share other than digital.

So one possible scenario is that if digital is to make its way to 50% share, we get 1/3 coming out of TV, 1/3 coming out of print and 1/3 coming out of what you might call the gray TV market. But having said that, the importance of addressability at scale in safe and salient media is as important as ever. And so TV content is going to be part of that story, even if it's called digital, and TV with the most diffused distribution has the youngest profile.

So that wraps it up. And as I say, we will be revisiting these forecasts in June. Thanks very much.

Martin S. Sorrell
Founder

Thank you. We are sort of turning this into a sort of Investors Day or half an Investors Day. I thought it would just be worthwhile running through some of the most commonly asked questions by yourselves and others. And we tried to boil it down to 5.

The first is, just picking up on some of the things that Adam was talking about, the digital companies such as Google, Facebook, Amazon, Alibaba and Tencent, to name probably the most prominent in our context, are they going direct? Secondly, are consultancies eating our digital lunch? Thirdly, are ZBB models, activists and private equity driving down marketing costs? Fourthly, are clients increasingly in-housing marketing activities? And fifth and last, are innovation and branding still important? So we'll try and address all of these in a limited period of time.

The first in relation to the big search social companies, such as Google and Facebook and Amazon and e-commerce companies like Amazon, Alibaba and Tencent, are they going direct? Well, if you look at -- this is an analysis of our media portfolio into segments. And for the first time, Google and Facebook in 2017, the year that's just closed, closed as the top 2 media destinations for us, Google and Facebook together accounting for about $7 billion out of about $75 billion of media spend, remembering, and we talked about this last year, that the long tail constitutes something like 70% of -- to our knowledge, 70% of Google and Facebook's volume.

The third group, grouping and obviously, there's a lot of flux in relation to this group, the 21st Century Fox, News Corp, Sky nexus, and depending on where that ends up, if it does end up elsewhere, either at Comcast or Disney or a mixture of both, those would be really, the third, fourth and fifth destinations. And then you see a number of other more traditional media companies until we get down to number 12, 13, 14, 15, 18 and 19: Twitter, Tencent, Oath, Amazon, Snap and Alibaba. And just for reflection, we look at the top media earners in 2012, only Google really, of those, was prominent 5 years ago.

In that connection, a lot of people say we've talked about Google and Facebook as frenemies and then friendlier frenemies and partners more recently, and I think that's demonstrated by this quote from Philip Schindler, who is Chief Business Officer at Google. This was at a Crédit Suisse conference in November of last year: "We don't want to disintermediate advertising agencies. We're actually working very, very closely with agencies all over the world. It's important to understand that we see ourselves as a supplier of technologies, and we would like agencies to actually apply our technologies and smartly use our technology. We see agencies as trusted advisors to the customers and clients." And just to put a little bit of flesh on those bones, here are 4 examples, and there'll be some more examples in the data area, of where we work very closely with Google, and I'll come on to Facebook and others in a second, where we work very closely with Google on partnerships and partnering with them in addressing some of the client opportunities and challenges that we have jointly. Firstly, the SWARM creative partnership, this creative forum that brings us and Google much more closely together across the world. Secondly, Geode, is a business transformation operation where we marry our marketing services expertise with Google's engineering and technology. Starkiller, which gives us world-class digital media through we're implementing search capabilities that Essence have developed and redefined, and for Google Media Lab, as best practice across the whole of GroupM. And then last but not least, the initiative on the Next Billion Consumers. Everybody's focused on cost, the real opportunities, obviously for our clients, are the next billion consumers, who are not going to come from Western Europe or the U.S. They are going to come from Asia and Latin America and Africa and the Middle East and Central and Eastern Europe and we are focusing with Google on that, too. With Facebook, we have the Creative Ambassadors Program. It's a joint initiative that we developed exclusively and specifically with them for our creative and digital agencies. With Amazon, we've focused on leading the way in providing a unified approach with Amazon, connecting media and e-commerce capabilities in both organizations and Mark maybe can talk a little bit more about that in connection with what's happening with MindShare and POSSIBLE and also Wunderman Commerce, which is located in Seattle, where Amazon HQ is currently based, although they will be adding to their HQs in the U.S. in short order. Alibaba, we have a unique strategic relationship, which combines GroupM's platform, its data capability, with Alibaba's Uni Marketing products. And then with Tencent, we've announced the launch of the China Social Marketing Lab, which is a specialist platform to build platforms and campaigns for Tencent and ourselves.

In addition to that, on the data end, there's a whole host, there are 6 key relationships with partners, with Google, with Facebook, with Amazon, with Crossix, with Mobilewalla and Spotify, where we are using our data and their data to try and develop unique and unprecedented insights. And in addition to that, we're building our relationships with our marketing technology partners, with Adobe, with Salesforce, with Oracle, with Sitecore, with Acquia and with Marketo. And you can see that we are building those relationships at fairly rapid rates and our agencies are being named, for example, Mirum WPP itself have been named as leading marketing technology partners with Adobe and Acquia, last year and into this year as well.

In addition to that, we're using our data insights, the [m]Platform at GroupM, to develop a single source of truth for media activity. That involves optimizing and reporting, analyzing, planning, execution and unifying and identifying data for targeting purposes through the media. And you can see that we're building individual profiles, connecting multiple data points through Zipline and implementing that through [m]Platform's axis, our investment in AppNexus and our relationships with Google and with Facebook.

The second question people talk about generally is are consultancies eating our digital lunch? And again, we provided you with the data that we provided at the third quarter to try and demonstrate where the digital revenue and gravity really is in comparison to the competition, not just the direct competition, but the consultancy competition as well. And we've updated the win-losses ratios that we gave you for the first time, at the end of the first 9 months. This is really is a basis of surveys that we conduct with all our agencies as to where we come head-to-head with the consulting or the digital arms of the major consulting companies, such as Accenture or Deloitte and you can see there, the win-loss ratios are not significant in the realm of things overall, but in terms of establishing trends, a win-to-loss ratio of about 50-to-30. There are about 80 examples there not awarded, a small number, announced number of about 80 projects, involving about $115 million of revenue, the most significant of which was an automotive win for us in Europe in the fourth -- the fourth quarter. So significant activity in terms of -- or significant success in the amount of activity that takes place with the consulting companies.

In addition of that, there's a lot of debate and discussion as to whether we are involved heavily in digital transformation. And these are just some specific examples in the automotive sector, the financial services sector, FMCG, pharmaceutical, personal care and drugs, retail, travel and airline and telecommunications, where we're significantly involved, units of WPP are significantly involved in digital transformation with clients.

The third question was really -- these sort of 5 questions break into 2 fundamental areas: 1 long term about technological disruption, which is affecting production, affecting marketing and affecting distribution; and then the short term, about the particularly the emphasis on cost, and we've been through this with you before, but we have disruptors. We do have activist investors, we do have zero-based budgeters, who are putting very significant emphasis on short-term cost management, and I have to point out that the activist investors, to be fair to them, there are several, but the most prominent probably being Dan Loeb and Nelson Peltz, who do emphasize that what they are interested in is innovation and branding. But in that context, it is having a significant impact on the patterns of growth. And if you look at the leading CPG clients, these are leading WPP CPG clients, and look what's been happening to price -- organic growth, price and volume. The trends are quite significant. We are really seeing volume growth at very low levels, some improvement in Q3 and Q4 over '17, but mild. Obviously, very limited pricing power in a low-inflation environment and organic growth picking up a little bit, but at significant low levels. And on the right-hand side of this slide, slide 61, you can see what's been happening with 2 of the most prominent ZBB companies, which clearly shows that whilst margins have increased quite significantly, volume is a problem and that's starting to have an impact, perhaps as interest rate starts to rise, on stock price and market capitalization. So there is this issue, I think in the longer term. Most people who -- and it has to be admitted, these are people who have been in packaged goods companies for long periods of time, believe that as volumes come under pressure and there's a lack of volume growth, increased investment in 2 things: Innovation and branding. You can't have innovation without branding, but you can't have the branding without the innovation. They go two in lockstep, so you need innovation and branding to make things work.

And in that context, just want to emphasize that when you look at, for example, at the S&P 500, where you're getting the growth, we're talking a lot about synchronous economic growth post-Davos, the optimism of Davos was very significant in a historical context this year, but most of that growth, whether it's a 3% GDP growth or near to 3% as it was last year, or 4% as it looks like it will be this year, with the general sort of flip up in growth. Most of the growth seems to be coming in 2 sectors: 1 is in tech; and the other, to a lesser extent, is pharma. And you have this valuation discrepancy, that you have information technology and these are the updated figures from figures that we showed you before, the information technology S&P 500 growing at just under 10%, their price earnings multiple are about 19x. Consumer staples have come back again in terms of valuation, down about 6%, as you see '18 over '17, as opposed to tech moving up by 1/3. But it's still 3% average growth, and a P/E of just under 18%. So there is that dichotomy or paradox.

And the problem of volumes is exacerbated by what Adam highlighted in terms of the different shares of retail channels. Hyper and supermarkets have by far the greatest share, just over 50%, but the lowest growth. Discounters have a share of about 6%, growing at 5%; convenience, 5% share, growing at 4%; e-commerce, 5% share currently, but growing at 26%. And you see what's happening globally to the traditional trade, with about 26% share and only growing at 3%. So you have multiple channels, omnichannel growth -- development planning programs, obviously, is critically important, but with very significantly different growth rates.

The fourth area that people focus on is the in-housing and marketing activities. And it is a mixed picture on this. Hogarth, we've announced today that Hogarth will be, which is our production management platform, digital production management platform, which is growing very significantly in the last 3 to 4 years, it's tripled its revenues over that period of time with a number of very significant clients. Hogarth is now being rolled out across the whole of our enterprise. So it's a good example of the in-housing phenomenon not taking hold and we're seeing production management being increasingly out-housed. And we are seeing programmatic and performance agencies continuing to grow. Xaxis is gaining traction. It has over 4,000 clients, as effectiveness and efficiency becomes critical. And there is an issue here, there are the demands for improved performance and cost management and in a model like Xaxis, we are seeing greater traction as divisions of companies, categories of companies, are looking for improved performance and better yields in terms of online management. And that's reinforced by performance agencies such as we have with plista and Essence in digital media, media planning and buying.

The third point here is that we do cooperate, there's sort of feeling that it's either/or. We do cooperate with clients on building in-house facilities. We've cooperated with them in content studios with media investment management, with data with the data investment management and in content studios through our public relation agencies as well. And we participate in building and supporting those data, studio and programmatic capabilities. And recent examples, recent data as we put it here, do indicate that in-house programmatic and content studios may be going out-house as much as in-house, and there is, it's true, some to-ing and fro-ing in both areas. But the trend is not clearly defined. It's certainly not clearly defined as in-house.

And the final point to make in relation to these trends, is that we have developed specific ZBB marketing models which are much more agile, much more responsive, much more cost effective and agile to deal with the ZBB phenomenon.

In terms of innovation and branding, whatever we say about the environment and the technological disruption and the short-term pressure on costs, the general environment, the new normal, where that GDP growth is at 3% or 4%, is really basically low GDP growth in the sense of subtrend to what we saw pre-Lehman. There is little or no inflation, I know it's the issue that people are preoccupied, certainly, from a market part of view and interest rate point of view, but basically, it's very limited inflation, at least to date since Lehman. And therefore, clients have very little pricing power and they're still very focused on costs. Tenures are short term in terms of management. And if you look at what's actually happening, so the distribution of earnings, it's still, we are seeing, and this is the S&P 500, we're still seeing dividends and buybacks and distributions to shareholders being close to, if not over, 100% of earnings. So again, management is distributing back to shareholders virtually all the earnings and that obviously has an impact on investment.

And on this question of investment in brands and indeed, in innovation, there's clear evidence, not our evidence, but evidence in this case from Morgan Stanley Research in November of last year, that investors in marketing do better than cutters. They've analyzed -- Morgan Stanley analyzed A&P spend and it is A&P spend. I mean, we're -- we don't know the distribution often between advertising, which is brand-building, and promotion which is around -- that's the P -- which is around price, but analyzing 40 global FMCG companies. Morgan Stanley have been consistent -- or come to the view that these 40 brands have been consistently increasing brand -- those that have been increasing, consistently increasing brand investment, have an average 50% faster growth rate than peers that haven't. And the secondary point, which is equally or maybe even more important, is not only does A&P spend boosts sales, it also builds barriers to entry, which allows FMCG companies to earn returns far in excess of their cost of capital and ultimately drives valuation. This is going to become critically important as Amazon, in particular, and Alibaba and Tencent as well, start to build their platforms, and particularly Amazon, according to some estimates, the advertising platform last year was up to about $2.5 billion, $3 billion, so it's a tiddler in relation to Google and Facebook, who were at $100 billion and $40 billion, respectively. But it is growing very rapidly. And of course, in search, Kantar has already pointed out that 55% of product searches in

America are generated through Amazon in one way or another. So the threat to Google or the challenge to Google from Amazon is going to become more and more important and Amazon, of course, with voice-activated devices, is going to be an increasingly important phenomenon. So building brands through innovation and through branding becomes critically important.

And our own data, we've updated the data that we have been in the habit of giving you for the last couple of years, this is data where we value brands globally and regionally, latest in Italy and in France, clearly shows that the top 10 brands, for example over the last few years, have out -- clearly outperformed the S&P 500 by 60% and the MSCI by, which is probably the real comparison index, by over 3x over the last 10 or 11 years. So clear evidence that investment in A&P works in terms of long-term sales growth, building the moat and in terms of value for shareholders.

Now given this, there's no good moaning about this, for all the analysis, what do we do in response? And this is where it's critically important. So there are 4 things that we're doing. And I don't think this is a different direction to what we've been doing over the last 5, 6, 7, 8 years. We have been certainly going in the direction of integrating our offer more effectively. But because of the things that we've just gone through just now and these questions that are being asked, one way or another, some of them long term and more structural and some of them short term and therefore more cyclical, we have to do, in our view, 4 things: Simplify our verticals, and Mark is here and he can give you a view of what's been happening at Wunderman and that's been significant in terms of a number of brands that we've consolidated with Wunderman. But we've been doing it at Ogilvy; we've been doing it at GroupM; we've been doing it in our public relations operations this week with Burson and Cohn & Wolfe, and prior to that, with Finsbury; in brand consulting; in health and wellness; and last but not least, in our digital operation. So the first is to simplify the verticals. The second is stronger client coordination, which we've been in the forefront of doing across the group. We have 50, 51 client leaders cover about 1/3 of our business, integrating our offer across clients throughout the group.

Thirdly, appointing country managers and subregional leaders to try and integrate at a country level, but also to respond to the local or regional piranha, some call them piranha, the West tends to call them piranha, the Chinese tend to call them gladiator brands, that are building at a local level. So we've made recent appointments in Taiwan, in France, in the U.K. and Brazil, that are just 4 more examples of where we are focusing on country management.

And finally, horizontalizing, for want of a better word, certain function systems and platforms. I mentioned Hogarth already in terms of digital production, but it may well be that we'll start to do more of that at an enterprise-wide level not just in digital production, but in digital transformation, e-commerce and shopper. And that leads you to a structure with our functional, let's call them 7 functional areas, that's advertising, media, data, brand consulting, public relations, health and wellness and specialist communications, which is basically our digital capabilities. Those are the functional areas of the business. And the horizontals are the production management platform that I mentioned, which is built around Hogarth. And then you'll see the hatch line around digital transformation, e-commerce and shopper. The further development will be the horizontalizing, if you like, of our digital capabilities as a platform or system or function across the whole of the enterprise. There are, of course, the shared services we've had that we've been in the habit developing. And core tech in the IT area is a good example of the initiatives we're taking there. But in talent, in finance property, procurement, information technology and indeed in practices, we're building and have built horizontal connections.

Just on the right-hand side of that Slide, Slide 72, we focus on some of the client P&Ls that's part of the 51 client P&Ls and the country P&Ls that we've been building.

So finally, in terms of outlook and conclusions. Reported revenue and revenue less pass-through costs, growth last year was 6%. Like-for-like revenue less pass-through cost was just under minus 1%. Reported margin was down 0.1 margin points, but flat in terms of constant currency in like-for-like. Reported headline diluted EPS growth was at 120.4p was up over 6%.

Return on equity was up to 16.9%, against a slightly lower WACC, weighted average cost of capital, of 6.3%. Dividend was increased to 60p, up 6%, which represents a 50% payout ratio. Average net debt-to-EBITDA ratio was 2x at the top of our 1.5x to 2x range. The tailwind -- the ForEx tailwind reduces and becomes a headwind from Q4 of 2017, plus 14%. Q1 is plus 10%. Q2 is plus 2%. Q3 was minus 3%. And Q4, 4.5% for the full year coming at the end of 2018.

Net new business is good GBP 6.3 billion and continues the performance that we've seen in the first 9 months, and a leading position in the net new business tables. A slow start to 2018. When you view the January figure, revenues were flat. Revenue less pass-through costs were down by just over 1%, but above budget. And there's a focus, as I've said, on the simplification of structure, including the verticals, client and country management an enterprise-wide alignment of our digital systems, our platforms and our capabilities.

In terms of the financial model, we made a significant change here. We've talked about -- always talked about organic revenue and revenue less pass-through cost growth of 0 to 5%, in line with market growth. Margin improvement of 0 to 0.3 margin points, given the flatness that we see in the top line in 2017, certainly in the last 3 quarters of 2017, and 0 to 0.3 margin points or more before currency movements. And that depends, as I've said, on revenue less pass-through cost growth and staff cost to revenues less pass-through costs ratio improvement of 0.2 margin points or more. So that's the staff cost to revenue -- or revenue less pass-through cost reciprocal to overall margin.

We continue to use our substantial cash flow to enhance EPS through acquisitions and share buybacks and debt reductions. The balance remains the same at GBP 300 million to GBP 400 million on acquisitions. Share buybacks at 2% to 3%, and a payout ratio of 50%. If you do the calculations of that, if you assumed, for example, flat revenues, flat margins, 2% to 3% buybacks and acquisitions for about 1% to 2% revenue gains, we're talking about the low end of the 5% to 10% EPS growth. If you make more extravagant assumptions about revenue growth or margin improvement, you get, obviously, a result that's closer to the upper end of that range. So instead of the 10% to 15% that we saw in previous years as being the model, we now see it at 5% to 10% EPS growth.

Now if I -- in terms of the budgets, there've been a number of questions before we started about the budgets for 2018. We encouraged, if that's the right word, our operating companies to budget extremely conservatively. Obviously, we're sort of embarrassed by what happened in the last 3 quarters of the year, where we were overoptimistic or we accepted overoptimistic forecasts on the top line. And we're budgeting flat like-for-like revenue and revenue less pass-through cost growth for the whole of 2018, but with a slower first half and a stronger second half. And that reflects, to some extent, the comparators, remembering that Q1 of '17 was the strongest quarter of that flat 2017 year. We're also budgeting a flat constant currency operating margin to revenue less pass-through costs, and we're budgeting acquisitions that add about 2% to 3% to revenue and revenue less pass-through costs through the year.

At current exchange rates, the full year currency impact is 4%, a 4% decrease to revenue and revenue less pass-through cost. And our prime focus is going to be on growing revenue and revenue less pass-through costs faster than the industry average, driven by leading position in horizontality and integrating our offer, the faster-grow markets and digital and the creative and effectiveness position that we have and the new business with strategically targeted acquisitions. We're going to meet that operating margin objective by managing our absolute costs and increasing the flexibility to adapt our cost structure to these significant market changes that we tried to go through in this presentation.
We've included in your takeaway some of the history and other data. You can see that all in the leave-behind you have. So we'll now open it up for questions. We'll start at the front and we'll work all the way back.

Question and Answer

Martin S. Sorrell
Founder

Ian, yes?

Ian Richard Whittaker
Liberum Capital Limited, Research Division

It's Ian Whittaker from Liberum. Three questions, please. I think it was Interpublic, who mentioned sort of on their call, that in terms of net new business wins, they gave a very specific sort of statement that, that would drive organic revenue growth in 2018. You've obviously had a very strong organic -- sorry, the net new business wins will drive stated organic revenue growth. You've obviously had a very strong 2017 in terms of net new business wins. They've been concentrating the first 9 months, so there shouldn't really be any timing issues. Sort of in terms of why that net new business wins is not translating into organic revenue growth into 2018, could you just outline sort of what's happening there? The second thing is just in terms of the targets. The longer-term target used to be, as you said, 10% to 15% earnings growth per annum. I think sort of without being flippant, that was always something that was seen as it were a sort of way in the future and sort of people didn't have them in their forecasts. But sort of why have you actually taken it down to 5% to 10% now? So what has been the specific trigger? And what would you say to people that would say that the fact that you have taken down your earnings growth target in the longer term would suggest that actually you do think there are structural impacts coming through and they are impacting your business? And the third thing is just in terms of the sort of 2018. So virtually, all your peers have said that the second half of the year will be stronger than the first half. Now sort of if you look at your comps, they are easily in the second half, but you haven't given that in your statement. So just wondering, sort of it may be implicitly in there because you said January's sort of down. But sort of can you make a statement now that you would expect sort of the position to actually pick up in the second half of the year and things will be second half weighted?

Martin S. Sorrell
Founder

Well, I'll give a go, and then Paul can respond as well. On net new business -- well, let me just try and answer all 3 questions in 1 way. So we do our budgets bottom-up. Well, I'll put it like this. The budgets came in with some degree of revenue growth for -- on a bottom-up basis for 2018. Given what we saw -- and I alluded to this in the presentation or the formal part of it. Given what we saw in the -- particularly in the last 9 months of 2017, we didn't think it would be appropriate for us to accept those budgets as is, and we basically went back and said in the course of the iterative process that we do. We went back and said we don't -- it's not we don't believe it, but we think that given what we saw in -- and irrespective of the new business, Ian. We think that's been too optimistic in the environment that we saw in 2017. And indeed, we gave you a figure for the first month of 2018. I don't know whether anybody else has as well, but we didn't see as -- revenues were flat. But what we used to call net sales, revenue less pass-through costs were down 1.2%. So it wasn't -- January is a small month of the year. But if that's indicative, we just felt that it was best to be cautious. So we said to the operating companies "Take down your top line." And that, of course -- again, because in the last 9 months of last year, if you look at headcount for last year, we were down about 1.5%, if I remember rightly, on headcount. So you would normally expect that to exhibit some significant restraint on the staff costs to revenue ratio, but it didn't. Why? Probably because the most easy explanation for it will be an expansion in freelance. I mean, if you're doing new business, there will be more freelance costs. There will be more temporary costs as a result. You can explain it that way. But you put all that lot together and you say given what's happening in the marketplace and given -- it's invidious to talk about specific clients, and they don't want us to talk about individual clients. But you've seen enough public announcements on what's been happening to agency costs to know that there is pressure in the system. So it really answers your net new business question. I think it's just -- maybe it's once bitten twice shy. But why -- not the impact in net new business. I mean, if you went back a year, we had some -- we had 2 big losses to deal with, which, actually, our businesses have done a very good job in picking up new business not on the scale of those 2, some wins approaching that scale, but basically filled the gap and gave us a little bit more room to maneuver. But you take that on the model, that 10% to 15% to the 5% to 10%, again, given that -- and it may well be cyclical, right, given that situation. We think it's the sensible thing to do to take down people's expectations. I mean, we couldn't have left it at 10% to 15%, in which case you'll be sitting there with an even bigger grin on your face, saying, "How can you get there?" So I think it was a more realistic view about what could take place. The other thing is -- and so -- and then on the second half, we are indicating, I had to say a few seconds ago, it will be, in our view, if we look at the budgets, a better second half. So I think it sort of accommodates all 3. Do you want to add anything, Paul?

Paul W. G. Richardson
CFO & Executive Director

Yes. I mean, I'd say on new business also, what the trade report is obviously the -- mainly media wins or losses because of scale. And one of the businesses I think we do see a significant pickup in performance is the media business, quite frankly. So within our view of 2018, we are expecting an improved media business. And I think the other reason why, to a certain degree, we're cautious, we've had a number of budgets in over the years where we've seen a very strong third quarter. And quite frankly, it hasn't panned out. And yes, it's difficult to be absolutely precise in January about what new business you're going to win in quarter 3. So we really have wanted them to not put on the costs in expectation of winning it, in the knowledge that if, say, if it doesn't come in, we're in the right cost base. So I think partly, it's the caution around what we're trying to achieve. And a lot of the adjustment, to be fair, that we wanted businesses to make was in quarter 3 and quarter 4, or quarter 3 particularly. So that, to my mind, is the main thing. The second thing in my mind is we are looking, in our case, I think a pretty strong performance will bounce back in our Asia Pacific, Latin America, Africa and Middle Eastern market, which turns to be very, very solid for us, very good. I think on balance, a disappointment to us in how they -- what they achieved in 2017. So one of the core drivers for our improved performance in '18, the balance is our faster-growing markets. They tend to be a little bit back end weighted in terms of when their revenues flow through. So those are the 2 reasons why I think there's caution around -- and why the budgets have come out where they've come out.

Martin S. Sorrell
Founder

Yes, just we'll move back. Tom?

Thomas A Singlehurst
Citigroup Inc, Research Division

Tom from Citigroup. 3 questions as well. I apologize. Fourth quarter, I think I'm right in saying that you'd commented that October and November were sort of okay. I don't know what okay means, but it's -- the numbers suggest that December was a lot weak, and I was just wondering whether that's -- whether there was a budget flush or whether it's specific to certain activities or certain advertisers. Second question, I think in the past, you've mentioned the growth rates of the top 20 clients, whether you can either give us that number or at least directionally indicate whether the big clients are spending at a faster or slower rate than the group average. And then final question, one -- actually, specifically with P&G. Obviously, you talked about reducing sort of overall agency spend, but they've also talked about reducing the amount of spend with agencies of record and then leaving more of the budget left for sort of ad hoc project-based work. I'm just trying to get a sense of whether that's a good or a bad thing if it develops into a trend more broadly for WPP.

Martin S. Sorrell
Founder

Okay. When you say budget flush, that indicates to me people flushing out. You mean the reverse budget flush? Okay. Well, I think David would say probably December was not the usual December. I'm trying to think back to December '16. I think December '16 was not as strong as probably we would see in December of '15 or '14, would you? Yes. So Dave is nodding on that. So I think you -- the pattern was

December '16 probably was not as strong as we've seen. We tended to see surges in the fourth quarter. Other people refer to them as not budget flushes, but project-driven quarters, which, yes, I wouldn't say that we see Q4 as being more project-driven than any other quarter. So I -- was there anything -- reverse budget flushes, that would seem to suggest that the pressures that we saw had more of an impact in that final quarter, in that final month than historically. On the top clients, I think it's fair to say that the top 20 clients probably were down further than the group average if you looked at revenue and revenue less pass-through cost. I think that show you -- you can check the number, Paul. I think that's the case.

Paul W. G. Richardson
CFO & Executive Director

Yes. Not so easy to check on the spot, but yes, I would agree with you. And I think if I look at the top 30, it's fairly evenly balanced between those that are growing and those that are declining.

Martin S. Sorrell
Founder

And then it's wrong for us to comment on specific clients. But despite the pressure, I think P&G commented specifically on the number of agencies they had and that they had consolidated down the number of agencies to 2,500, I think was the figure that they close it, and that's not a dissimilar situation to other situations. So there is an opportunity for us as clients to consolidate their agency roster. It depends on which way they consolidate it, obviously. But talking about it generically, there is an opportunity for us if they consolidate for us to carve out a greater share despite the fact that the top line may be coming down. Do you want to add anything more on that, Paul?

Paul W. G. Richardson
CFO & Executive Director

No.

Martin S. Sorrell
Founder

No? Okay. Is that right, Tom?

Thomas A Singlehurst
Citigroup Inc, Research Division

Yes.

Martin S. Sorrell
Founder

Okay?

Adrien de Saint Hilaire
BofA Merrill Lynch, Research Division

It's Adrien from Bank of America Merrill Lynch. So a few questions, please. First of all, on margin, a bit of a short-term question and long-term question. So for 2018, you're talking about a flat margin I think in 2017. So you were up -- well, I mean, you were flat or down 10 basis points reported, but that was assisted by associates. Of course, in 2018 you don't have that benefit of associates. Incentives in '17 were already quite low. You've got wage inflation in the U.S. So what makes you confident that you can deliver that? And in the long run, I mean, I know accounting differs from one company to the other, but your margins are quite significantly higher than others. So why do you think you can stick to the 17.5%. So that's first topic. Second topic on consultancies margin. You said that you had won over most of the pitches. But I mean, I can see that they've won a few recently, Maserati, the Vatican and so on. Would you expect more pitches to involve consultancies in '18 versus '17? And then lastly, I mean, usually we have a bit of a slide around Xaxis, the revenue growth, billings growth. Can we have a bit of an update on that and your outlook for Xaxis?

Martin S. Sorrell
Founder

Okay. Do you want to talk about margins?

Paul W. G. Richardson
CFO & Executive Director

Yes. So on associates, I think one thing you should have a look is the majority of our associates are in Asia Pacific and Latin America, over half of them. So actually, I'm not as negative as the Street seems to be on what our associate income will be in 2018. In fact, I think it'd be very solid despite what has happened because some of our strong contributors are not names that you're familiar with and actually have done very well. So in that sense, it's going to be a much more steady-state to the associate income in 2018. In terms of margins and bonuses, I think it was one of the questions, yes, there was a reduction in bonuses last year. It was down about 13%. But the good news is we have built most of that back in to the budget for 2018. And so the margin performance or the performance of the underlying business is going to be what counts in terms of the underlying management of revenues versus staff cost, as simple as that. So those factors that we've had, let's say pressure in '17, are accounted for in '18 and would say that associates is more even. I'll give you a flavor of Xaxis if I -- if you allow me a second to get some pages out in front of me. If I recall the slides from a year ago, we said we had billings of around GBP 1.1 billion and good sort of mid- to high digit-single figure growth for the business. We did say it was weak in the U.S.A. That has continued throughout the year for Xaxis. It's ended up with mid- to single high-digit growth, specifically through very strong performance in Asia Pacific and Latin America and good sort of, I'd call, B-plus performance in Europe, quite frankly. So the revenues and billings have grown on a combined basis to about GBP 1.4 billion. And then in '18, we're looking at close to double-digit growth. Return to growth in the U.S.A., and strong -- and continuing strong performance in Asia Pacific and Latin America. Billings in total, we're hoping to be around GBP 1.5 billion. And as we mentioned in the press release, we've gone from around 3,300 clients signed up to over 4,000. So I think it is gaining momentum. It's solid and is a good performer for the group.

Martin S. Sorrell
Founder

On your Vatican and Maserati, I think we work for the Vatican, too, and I think we work for Maserati, too. So I wouldn't comment further. And I think this speaks for itself. I draw your attention -- we can't say it's confidential on the top 2, but I draw your attention to the first one, which you might be surprised if you knew what it was. Okay. Yes, Patrick?

Patrick Thomas Wellington
Morgan Stanley, Research Division

Patrick Wellington at Morgan Stanley. A couple of quick ones. The buyback doesn't get a mention in your outlook. Are you going to carry on with the 2% to 3% buyback? That's good. Secondly, market research has again underperformed the group and on organic revenue terms. Normally, you answer this by saying it's there to support advertising and media investment management, which, however, has been the worst performer of the group this year. So where are we on market research. And there's been some talk of maybe disposing or partnering parts of market research. Is that still part of your plans?

Martin S. Sorrell
Founder

The mention of the disposal or parts of market research, what we call data investment management.

Patrick Thomas Wellington
Morgan Stanley, Research Division

But in Europe, you've sometimes talked about maybe partnering parts of that business in Europe. Partnering.

Martin S. Sorrell

Founder

Partnering? I thought you said disposal.

Patrick Thomas Wellington
Morgan Stanley, Research Division

Or disposal. You tell me.

Martin S. Sorrell
Founder

Okay. So going back, buybacks, we'll continue it at that level. Data, we've always talked about linkage, Patrick, not to the advertising business so much, but to the media business. And we think it is critical. I think when we were asked I think in the third quarter whether we would dispose -- I think it was either you or somebody else asked whether we would dispose of the data investment management business, I said we would not dispose of it. So sell it outright. If you could find some way with the data business, to answer your question head on, by making it more effective, we would seek that out or develop it. But we think it's extremely important. And again, just sort of back up for a minute. If you said to me, "What are the big things that we see going on where differentiation counts?" It would be the in-house production, outhouse production. That area where Hogarth is in, we've seen very rapid growth. We see very rapid growth, obviously, in digital and digital media. And the last area that we've seen significant growth has been the marriage of data with media, and we've alluded that -- to that in the presentation as well. So I think disengaging from data in the way that you're suggesting, or your question is suggesting, is -- would probably be weakening. And I think the fundamental premise that you started with, which is it links to the advertising and media business, it's -- what's happening in the advertising and media business is the traditional creative business is where the pressure is. The media business, all parts of the business have some -- have pressure in some way, shape or form, but I would say less on the media business than the advertising. So I think it's very important to maintain that connection.

Patrick Thomas Wellington
Morgan Stanley, Research Division

And finally, just on forwards announcement at the end of last year. Is that a risk or an opportunity for WPP? Were you dismayed or pleased to see that announcement?

Martin S. Sorrell
Founder

It could be both.

Patrick Thomas Wellington
Morgan Stanley, Research Division

And do feel free to say more.

Martin S. Sorrell
Founder

I wish I could be free to say more, but I can't be free to say more for obvious reasons, okay? Yes, go ahead.

Christopher Anton Giles Collett
Deutsche Bank AG, Research Division

Chris Collett from Deutsche. A couple of questions. One was just to go back to billings. So obviously, it's a big focus within WPP. And looking at your account wins, I'm just wondering, are you perhaps focusing in the wrong place or putting too much emphasis on new account wins since we can see they're not really driving growth? Perhaps you're focusing too much on winning new clients rather than extracting -- sorry, extracting may not be the right word -- working more closely with your existing customers to get more growth out of the customers that you have. And then related to that, a lot of talk about the upcoming

Mediapalooza 2. Do you think you're in a position to win more? Or are you going to be an incumbent in more of the business there? And then lastly, would you like to just give us an indication of what the media business did underline? Perhaps maybe stripping out account losses in the year, how did that business perform?

Martin S. Sorrell
Founder

We could -- we wouldn't give you a separation between the advertising and media. I think we gave you enough detail for that. But I don't think we could strip it out in the way you're suggesting anyway. I mean, I don't think you could strip out -- quite difficult to do that. On the existing billings or billings point, focusing on the existing business is a critical part of it as well, and I wouldn't disagree with the comment. In the net new business figure -- and it's a net figure, not a gross figure. In the net new business figure, you would find a significant number of existing client wins as well. So if you went through each of the new business wins or losses, you would come up with the existing clients to a very significant degree. So they would reflect the existing business activity. But the drift of your question, if you look at what's happened in terms of revenues as a proportion of billings, or revenues less pass-through costs as a proportion of the business, that's increased. So using the word extraction is probably inappropriate. But that rate, if you like, has improved actually in the course of 2017 despite the, say, the least mediocre performance. Mediapalooza, I mean, there is increased media activity, and Paul's mentioned that most of the new business activity is media-driven. But on Mediapalooza, I don't think it's enormously stronger than we've seen on a fairly consistent basis. And you had a figure, Paul

Paul W. G. Richardson
CFO & Executive Director

Yes. So the 3-year-ago Mediapalooza, when everything was said and done, was media or billings changed the volume of around $21 billion. Actually, in a normal year, media changes hand at around a volume of $18 billion. So it wasn't a double what a normal year was at the end of the day. It was a significant because there are a number of major accounts, household names in the U.K., U.S.A. in particular.

Martin S. Sorrell
Founder

I mean, of the major public reviews, we're involved in Mars, where we do planning; in Shell; and in HSBC. Those, I think, are the major, major ones out there. Then there are other opportunities. I think Microsoft is one, and I'm trying to remember there was another one as well. But the level of activity in new -- I would say the more important point is not -- isn't in comparison to Mediapalooza. But the significant amount of new business activity or retention activity is around the media area. Creative has taken a backseat I think. I mean, Mark, do you want to comment on new business activities from a digital perspective?

Mark Read
CEO & Executive Director

I mean, I think there's a tremendous amount of digitally driven new business activity, a lot driven by companies looking at how they reorganize their tech stack, how they work with Adobe, Salesforce, other partners. And I think increasingly, you see, I think particularly in the media review, desire for integration of media with -- I mean, the creative work but maybe less the creative work than with the client's data and its technology stack. So you really get a single view of the customer across all of your marketing activities.

Martin S. Sorrell
Founder

Okay. Irwin, you're on the line from I think Los Angeles. Do you want to comment? As we got you up in the middle of the night, we must use you.

Irwin Gotlieb
Former Chairman

So to the early part of the question, there's no doubt that we apply more focus to plugging any leaks in our bucket than we do on filling it from the top. That's just good common sense. On extraction rates, the good news for us is that the media landscape continues to increase in complexity. And complexity is -- contributes to our extraction rate because compared to 10, 15 years ago when digital was a smaller component, our extraction rates today are significantly higher. That's the good news. The other point I would make is that when we win a piece of business, we go in with a defined scope. And history has shown that, that scope gets added to over time. And both of those things I think address the heart of the question that you asked.

Martin S. Sorrell
Founder

Okay. Yes?

Simon Baker
Societe Generale Cross Asset Research

Simon Baker, Soc Gen. Three questions, please. You've taken a haircut to your operational budgets. Could you give us a sense as to whether that's normal? How often, perhaps, over the last 20 years or so that you've done that? Secondly, on the accelerated strategic focus, how should we think about that? Is it just about sort of better effectiveness internally? Or are there financial implications, restructuring charge, for example? And thirdly, this might be a question for Mark, if I may. But we've got Facebook deemphasizing its ad load. The implication there is you got more cost per thousand inflation as a component. I know it's an auction process, but the majority of its 30% revenue growth perhaps this year comes from that. If we acknowledge Facebook's got an 8.5% market share globally in the ad market now, is it more a price maker? Does it affect relative pricing for cost per thousand elsewhere? Are you seeing any of that come through?

Martin S. Sorrell
Founder

Mark, do you want -- yes, Adam.

Mark Read
CEO & Executive Director

I think it's more Adam question than a Mark question.

Adam Smith

The changes in news feed are certainly identified as a potential source of inflation. But equally, they will encourage us to seek out alternatives, and so I'm not sure that it makes sense to talk of sort of price leadership in markets which are so automated. The U.K. market is essentially dark now. It's sort of 80% automated. So one will look for alternatives. And when you're doing that, it's better not to do it with the pure objective of trying to optimize cost. I can see problems going down that route. It's about optimizing quality, which we generally mean viewability now, which we regard as an opportunity. When we can improve the value of viewability, we like to do it at a lower cost than that value is.

Mark Read
CEO & Executive Director

I mean, I'd add that Facebook is Facebook and Instagram and WhatsApp today. And as I understand it, the ad load on Facebook is declining in response to something -- you said a decline in usage. I think you'll see ad load on Instagram increasing. And then looking very aggressively at how WhatsApp can be used as a business tool, like WeChat will be used in the U.S. So I think you see a shift in overall pattern of spend.

Martin S. Sorrell
Founder

On the operating budget, I think if you went back and looked at the last 33 years, you go back to '91 to -- then 2001 to -- and '09 will be the 3 big pressure points -- cyclical pressure points that we had. I can't recall that we were as aggressive on the top line. David can -- both shaking their heads, meaning that we've -- this is probably the most aggressive we've been. And I think it is probably for the past few years. And it's because I think of the experience in 9 months. Your second question on financial?

Simon Baker
Societe Generale Cross Asset Research

[indiscernible]

Martin S. Sorrell
Founder

Implications?

Simon Baker
Societe Generale Cross Asset Research

It was whether there are financial implications, restructuring charges, cost savings we should think about.

Martin S. Sorrell
Founder

They're organizational chiefly. There'll be some restructuring expenses but within the context of what we normally do. No biggie abnormal restructuring expense. Yes, we've got out of order here. Yes?

Matthew John Walker
Crédit Suisse AG, Research Division

It's Matthew Walker from Crédit Suisse. 2 questions please. The first is, I guess, going sort of structural versus cyclical, you could call it as sort of Michael to Auteur scale, Michael being it's all cyclical, there's no structural problems, Auteur being like more like well, there are structural problems, quite a lot, but we've got a plan to deal with it. Where would you put yourselves in that scale? Because I'm not sure based on the explanation you've given today, how much of the stuff you think is structural versus cyclical?

Martin S. Sorrell
Founder

It's an impossible question to answer. You go to either end of the spectrum probably with the spend depending on what your vested interest is. The answer, I think is it's both, all right? If you look at the CPG stuff, that clearly to some extent is cyclical. If you look at the technological disruption stuff, it's clearly structural in the sense that it's affecting everything. I mean, is there a client that you can take a look? Carla, it's a little bit saner for you, it's only 6:23 in the morning. But maybe, you can talk a little bit about the structural stuff that you see from a consulting point of view? Because Ogilvy Consulting is doing a lot of digital transformation consulting. I mean, is there a company that you have come across or that Ogilvy is aware of where you've seen in the context of WPP that isn't going through some form of transformational production, marketing, distribution challenge?

Carla C. Hendra
Vice Chairman, Chairwoman of Ogilvy Global Strategy & Innovative Practice & Chairman of Ogilvyred

No. I mean, there's no company unless they are on another planet. We sort of look at them as being in 3 buckets. They are either quite invested in moving up the digital maturity curve and they've been creating business value for some time, by competing with disrupters and doing well. There's some who are kind of in the middle, they might spend a lot and might try a lot of things but they're not necessarily getting the digital ROI that they want, or they need to get to compete better. And then there's quite a few who are still stuck at the starting line, who are legacy companies that have a lot of baggage, they have a lot of expense in their data systems and the things that are hard to change. And all of them need advice. So this is one of the reasons why we've seen the big consultancies trying to move in to what might have been considered our terms, but they are certainly in the advisory business too. I think the difference is in the way we approach things is that today, in low growth, not too many boards want to take on tens of millions, hundreds of millions of transformation expense to do big IT implementation projects. They're quite careful about that. So there is a big space around being agile and using all of the WPP capabilities to come up with more pragmatic, more practical proof of concept in digital trends that lets companies get somewhere and demonstrate that there is a return, and that there is an innovation that's worth a brand investing in. And one of the reasons and the ways that we do it a little differently is by understanding brands and understanding customers and customer experience on a much more definitive level, because we have been dealing with that through all of our lives because we have the data around how customers behave and even how they think. We can do it with a more insightful touch. And so there is a tremendous opportunity for us for growth to help the C-suite from the very top of the company right through to CMO, chief digital officers, CTO, CIO and certainly, the innovation groups to manage digital transformation and then follow on from that the execution services that many of the WPP companies are delivering.

Martin S. Sorrell
Founder

I think the answer is we would respond to both and our vested interest is we believe we have assets that can do both. So you pay your money and take your choice. But I think we -- and there's got to be some cyclical stuff here and there's got to be some structural stuff.

Matthew John Walker
Crédit Suisse AG, Research Division

Got us to talk about Sapient's 15%, 16% to revenues, they're expanding, they define this business transformation. If you were to dot the same definition in terms of business transformation or digital transformation or whatever, however you describe that, what proportion of your revenues come from that now and where do you want -- where do you think it should go to?

Martin S. Sorrell
Founder

Well, we -- impossible to log. You look at our digital capabilities, it's about 42%. It's gone up about what, 200 basis points in the last year or 300? So digital, but just to your point, and if you've got 15% in transformation, you got 85% that isn't. What do you do about that? And it's the tail wagging the dog. So the issue, and it's exactly the same issue as anybody who has a "legacy" business, you have to manage the legacy business at the same time or change the engines on the airplane at the same time as you're flying. So -- I hear what you say, but if you've got growth coming from business transformation and Mark, you comment on what you see in -- Wunderman is in the forefront of our digital transformation as one of the agencies.

Mark Read
CEO & Executive Director

To some extent, I prefer not to think about cyclical versus structural but how you position the business for growth. Because it's kind of very hard to split down what's [waging]. When you get times of cyclical pressure, the structural things tend to happen more quickly, right? You got an activist investor breathing down your neck. You examine where you're spending your money more forensically than you used to and you may shift more or less quickly. So I think that we're really in a business of positioning the business for growth. We -- Wunderman, we don't send clients many invoices called digital transformation, yet we worked with Microsoft for 12 years and they used to spend 20% of the budget on digital. Today they spend 80% of their budget on digital. I'd argue, that's what we've achieved with them or GSK. We've been working for the last 3 years on a similar shift. Now there are clients where we are directly engaged in much more digitally transformation-led project. So we have business in Spain called The Cocktail; they rebuilt BBVA's mobile banking application. It's now the #1 mobile banking application. To be honest, I think it's a bit grand to call that a digital transformation project, but effectively, that's what it is. So we work with Sainsbury's through one in e-commerce. We're building Sainsbury's e-commerce platform, and not just the website but literally going how they pick the product in-store, how they schedule the vans, how they integrate the order management system into the line of availability to store level, how when you arrive at the website, it determines which of the delivery stocks you find available. So I think we can work on those complex transformation projects in a lead program management role, so we're currently replatforming an online retailer from this in-house systems to IBM WebSphere Commerce. I think it's 45 different websites they own around the world, and this is, I think, the #1 luxury online retailer. And that involves a digital transformation. It's a project of that nature. So I think there is substantial amounts of that going on but it's very hard to say in Wunderman's more than GBP 1 billion of revenue, what will you call transformation, what will you call just what we do for clients, I think.

Martin S. Sorrell
Founder

Yes, and owing to that point as you put up 57 again, I mean, there is clearly a difficulty that the consultants have in estimating what their digital transformation revenues are. It's very difficult to isolate it. You can talk about what your digital activities are as a whole, but the nature of them is a very, very different dynamic.

Julien Roch
Barclays Bank PLC, Research Division

Julien Roch from Barclays. You guiding to 0 topline, 0 margin improvement, which shouldn't come as a surprise because you've been saying that for a couple of months in public forum. However, today you've been pretty much Doctor Gloom while in previous forum, you said that, that was the budget but you were hoping for 1% to 2% growth there. So can we see a bit Mr. Bright Side or has it been snowed under? That's my first question.

Martin S. Sorrell
Founder

I think with flat top line and with flat margins.

Julien Roch
Barclays Bank PLC, Research Division

Okay. The second question...

Martin S. Sorrell
Founder

I think we said that the budgets were coming in about 1% to 2% growth, to be fair. The bottom up was coming at that level but we prefer to focus on flat.

Julien Roch
Barclays Bank PLC, Research Division

The second question is on Mediapalooza again. So you said that you didn't think it would be different this year, but your competitors disagree. They think it will be big. So specifically, have Amex, Vodafone or Nestle called a media review? That is my second question.

Martin S. Sorrell
Founder

I'm not aware of those at all. Nestle has reviews in countries on a fairly consistent basis.

Julien Roch
Barclays Bank PLC, Research Division

And the third question is on your...

Martin S. Sorrell
Founder

[indiscernible] Nestle, if I remember rightly, in France at the moment, where we are not the incumbent.

Julien Roch
Barclays Bank PLC, Research Division

And then the last question is on your structural response. One of them is simplifying your verticals, and you give a couple of examples like Ogilvy with next chapter. All those merger of agencies, what kind of percentage of revenue that represents? Is it something kind of marginal where you're merging 5% of your revenue? Or is it something really structural where you're merging 25% of your revenue?

Martin S. Sorrell
Founder

Well, I'm just trying to get that list up there. Actually, it's very significant because you take Kantar, you take Ogilvy and you know yourself we don't break out Ogilvy separately. But you take -- just take Kantar for a minute. You are talking about 20%, 25% of the revenue base on its own without going any further. So we are talking about significant realignment of our office.

Julien Roch
Barclays Bank PLC, Research Division

But you're just not merging the whole of Kantar, you're just merging part of Kantar, it's not the whole division.

Martin S. Sorrell
Founder

No. In every country, Kantar has come together, right? So instead of having TNS, Millward Brown as global verticals, if I can put it that way, they are brought together with one leader for Kantar in each country. I mean, these are prototypes effectively and the same thing is true of Ogilvy. These are prototypes for where WPP as a whole would go. So the it's the same type of approach. But on a micro -- less of a macro basis on a micro basis. So if you take -- you take WPP health and wellness, that was 3 separate brands. I think we give a published figure that being $500 million of revenue, okay? Or actually it was 4, because we had medical, [far] professional Barton Media buying, planning and buying also included. So you are talking about significant parts of the group. These are not sort of ephemeral parts. I mean, Wunderman itself is over $1 billion in revenue, and that's brought in -- do you want to comment on?

Mark Read
CEO & Executive Director

If you look at where we are today, we're I think 65% bigger than we were 3 years ago, not by organic growth alone but by consolidation of the business. So we kind of -- and we operate a model which I'd say is 2 brands, 1 company. And that can evolve over time as well. And the benefit is that we give each of those companies access to the data, to the technology, to the delivery centers that we have inside the group, so you get both some reduction in overhead that's not going to be driven by reduction overhead. It's really about access to expertise.

Martin S. Sorrell
Founder

Carla, do you want to comment on Ogilvy and the next chapter?

Carla C. Hendra
Vice Chairman, Chairwoman of Ogilvy Global Strategy & Innovative Practice & Chairman of Ogilvyred

Yes. I think the strategy that we've been developing, which is really moving quickly into execution is to become one Ogilvy as a brand and as a face to our client to still have the deep, deep capability expertise in areas like digital, certainly some of the things like PR and influence that have been important growth areas for us. So we will still have those capabilities, but we will go to market as Ogilvy, losing the Mather. And it will allow us to simplify what we do for clients, which they've been asking for, in no uncertain terms. They would like to be able to come in through a single door, get whatever the best talent is for the job at hand, have a sort of plug-and-play approach to resourcing and allocation. And by doing that, it should also be more efficient and allow us to take some of the duplicate overhead costs out, which we're doing right now. So it has both a quality of service, quality of output, improvement to the client and it also has an efficiency goal. We want to be able to create brands at every -- and make them better at every level, in any channel across any time for us and we basically talk to clients about the long term and being able to build their brands, and Martin showed the staff fund that people invest in brands financially do better in the long -- even in the mid- and the long term. We want to be able to build the kind of programs that every single business has to build to do to be on the intimacy level with their customers today, that means heavy data, heavy digital and delivering quarterly results, whether it's in users or sales or however the metrics work. And then very importantly, we want to be able to deliver pulse and the content and brand information and knowledge that has to come out every single minute of the day and the way the world works now. So we have developed a new operating system that we have recognized around that platform, brand platform brands, program and brand pulse time horizon, and we've now articulated and aligned all the capabilities underneath that. We're building out a toolset and we're taking all of our top 20 markets through the ability to deliver that to clients. And it's driven by demand, by the largest clients as well as midsized and small. We have to be able to pick the pieces that a client needs first and most and apply the talent. So we think that's going to make quite a big difference in 2018 and beyond.

Martin S. Sorrell
Founder

Yes, so just to answer your question head on, it's affecting and taking Wavemaker on its own; that's not GroupM. It's affecting at least, I would say, 40% to 50% of our revenue base, just that list simplifying our verticals. Irwin, do you want to add a little bit from a GroupM perspective?

Irwin Gotlieb
Former Chairman

Sure. So I mean, we've done quite a bit of centralization within GroupM for quite a number of years. It's quite an obvious thing to do in the media sector. But just to give you examples of the more recent activity, we now operate local market with -- all the major markets have a local market head who has P&L control, single financial structure at the market level for all of the agencies. That housekeeping and overhead related, but another example would be mPLATFORMs, which is very, very practice related. Obviously, we can't develop and pay for 4 or 5 individual agency technology and data stacks, so that has to be centralized. As we scale, the value of that data increases. We used to talk about trading leverage in terms of dollars spent. Today, it's just as important to have data volume and touch point volume. The more cookies you plant, the more data you get back. We have thousands of data APIs that only need to be done once instead of 4 or 5 times across our agency. And there was an earlier question about trading leverage. And yes, of course, Gail gives us some level of trading leverage. But it's important to understand that as the world moves to biddable media, data provides a level of knowledge asymmetry that gives you an advantage in the trading environment because it is our job to know something about the avail, the impressions that becomes available that the seller doesn't know about. And we have to connect the dots between our client needs and our knowledge of the individual profile in a way that gives us a bidding advantage. So all of those things point to the value of centralization, both from -- both from the standpoint of just economies of scale as well as the benefits that those central capabilities provide [deck 1].

Martin S. Sorrell
Founder

Okay. All right, Julien?

Lisa Yang
Goldman Sachs Group Inc., Research Division

Lisa Yang from Goldman Sachs. My first question is on your outlook. You said that you're planning extremely conservatively. So when your peers are talking about 2% to 3% growth, and I think someone is even talking about mid-single-digit growth, do you think you are being too optimistic? And do you see any headwinds specific to WPP that means you might underperform your peers in 2018? Second question is on your -- the FX impact on margin. Do you expect any impact at all this year given the headwind on the top line? And the last one is on your working capital. There was enough for GBP 500 million in '17. Just wondering what the drivers is reflecting greater pressure on payment terms and how we should think about 2018?

Martin S. Sorrell
Founder

Do you want to cover the last 2 and I'll try and cover the first? I mean, it's very difficult for me to comment on that because I don't know the basis on which they've done it. Theoretically, as we said in the release, there are sort of 3 reasons, the mini-quadrennial reasons why this year should be a better year and I think, Adam, you are indicating that this year will be a better year than last year from -- even if there is a disconnect in mature markets to GDP growth for ad spending for whatever reason. So the Olympics, which were successful, the World Cup and the midterm congressional should harden the markets a little bit. You can try and estimate it. I think people talk about 50 basis points. Historically, people have talked about 50 basis points for a mini-quadrennial and 100 basis points for a maxi in a Summer Olympics, et cetera. Do you want to add anything more on that, Adam?

Adam Smith

No, I don't think so really, Martin.

Paul W. G. Richardson
CFO & Executive Director

On margin, we are not anticipating any impact of the current exchange rates on the reported versus constant currency margin, which should be good. The first year that won't happen. On working capital, it is complicated. So in the back of the accounts, you've got the split out between what I called trade working capital, which last year was an improvement of GBP 180 million and this year was a deterioration of GBP 261 million, to be precise. And so yes, we did give back some of that improvement we had last year. The other element in your GBP 500-plus million is what I call nontrade, and that things unfortunately like the bonus revision that we have to make each year is obviously GBP 40 million less than it was a year ago. It is -- we have some various pension obligations, it happens to be the obligations on the pension are lower than they were a year ago. So between pensions, NIC, bonuses, that is all the nontrade impact on the provision change, but they actually want to call true underlying working capital as measured by trade receivables, trade payables, has deteriorated but really given back that improvement we made a year ago of GBP 180 million to an outflow GBP 261 million. Again, it's a point-to-point 31st of December to 31st of December position. We were very pleased actually with the cash generation the final quarter we made this year. And if you remember in September, there was a significant difference to the average debt and the point-to-point in September of about GBP 1 billion and that has come down to the tune of around GBP 500 million. So I don't deny, there is some pressure on trade working capital, but we've actually done a pretty good job overall.

Martin S. Sorrell
Founder

Yes, over there?

Richard Eary
UBS Investment Bank, Research Division

It's Richard Eary from UBS. Three questions. The first one just comes in terms of sort of harbor on about the budget process. But there's a sort of slide on the deck on Page 76 that looks at revenues by industry. I don't know whether you can just give us a feel in terms of which industries you think you're going to perform better and which for industry you think is going to perform worse within that sort of flat budget process so we get a sense of which clients, where you think the weakness may stem from? That's the first question.

Martin S. Sorrell

Founder

6, but we'll try and find it, go on.

Richard Eary
UBS Investment Bank, Research Division

The second question just comes to the new sort of earnings number. You said 5% at the lower end, assuming sort of flat margins, flat revenues with 2% to 3% coming from M&A and 2% to 3% coming from buybacks. How much comfort have you got on that M&A? Because that's obviously only 50% of the growth assuming flat-on-flat, so maybe some color on that. And then the just the last question, going back in terms of the timing of, let's say, revenue growth through '18, you talked about 8 first half being down, second half being up. Can you just expand on that a little bit? I mean, obviously first half revenues were minus 0.5, second quarter down minus 0.7 -- 1.7. That was the weakest quarter of the year last year. So maybe just to elaborate why you think you're guiding down on the first half?

Martin S. Sorrell
Founder

Well, I think the answer to the last question is that's what we see. I mean, whatever the absolutes were, and the absolutes were higher on the bottom of basis and we took them down, we maintained a similar, similar pattern and that's what the pattern was. Paul referred to earlier that Q3 growth, we've seen it over the last, I think, 3 or 4 years. The Q3 growth always seems to be stronger, seems to come down, and then we seem to get more in Q4 than we were projecting in the original budgets. So the pattern is a little bit odd. So the answer to that question about first half versus second half is it reflects the pattern that we got in the bottom-up budgets, but with a blanket reduction pushed down on the top part.

On M&A, there is a considerable amount of activity still on the M&A front is what I would call in the small to medium-size activity levels. Valuations, I think we highlighted in the statement particularly in the U.S. in digital, continue to be on the high side. Capital is a little bit more expensive than it was before and therefore, maybe valuations are correcting a little bit, but there's still in, particularly in the digital area, on the strong side. Do you want to comment at all on the first one?

Paul W. G. Richardson
CFO & Executive Director

The quote actually we used on the outlook page on page 76 was the prime focus is to grow our revenues and profits, sorry, revenues less pass-through cost faster than the industry average. We were referring to the advertising industry average per se. That is actually the goal, the outlook, the ambition. Obviously, one can look the slide at the back on Page 87 and look at our industry mix in terms of the client categories, which actually has not changed that dramatically over the years. And obviously, we will have a strong chance of growing with those industries themselves are growing strongly. It's kind of as simple as that. The better waiting we have to the faster growing industries, the better opportunity we have to grow faster than our competitors and our peers. And it's really that logical or that simple.

Martin S. Sorrell
Founder

I think this is the slide that you're referring to, is it? I would say packaged goods is going to continue to be under sort of continuous review. I would say healthcare, also more opportunities, so it will be better than the average, maybe financial services as well, technology. And telecommunications actually, I think there's a little bit more opportunity there. So that's where I pick out, just looking at this distribution, telecommunications, technology, on the plus side, government also on the plus side, a little bit on oil actually as well, maybe a little bit of financial services. I think packaged goods continues to be, because of what you see and hear, tends to be under continuous review. Now having said that, you look at Q4, there's a little bit more volume there. There is a little bit more price. If we get some inflation, it might be very different. Auto, obviously, a number of the auto manufacturers are going through continuous review of their smart mobility strategies. And so I think that's going to be under continuous review in 2018. So that's where I would place the emphasis.

Adam Smith

There's quite an overlap areas in digital that are working the data hardest. Principally, there's sectors we should own there, consumer relationships which are the telcos, the banks, and the automobile companies, too, are emerging there.

Martin S. Sorrell
Founder

Just one thing on the top 30, they have -- I just checked it, when Paul was answering the question, the top 30 were lower than the average. So I think, I can't remember who it was who asked the question, just to make that quite clear.
Okay. Any others? Okay, thank you very much, indeed. We're all here if you want to ask any further questions.