WPP PLC (WPP)

Updated June 3rd, 2019 by Josh Arnold

Key Metrics

Current Price:	$59	**5 Year CAGR Estimate:**	13.1%	**Volatility Percentile:**	60.8%
Fair Value Price:	$70	**5 Year Growth Estimate:**	3.0%	**Momentum Percentile:**	15.6%
% Fair Value:	85%	**5 Year Valuation Multiple Estimate:**	3.4%	**Growth Percentile:**	13.1%
Dividend Yield:	6.7%	**5 Year Price Target**	$82	**Valuation Percentile:**	69.3%
Dividend Risk Score:	F	**Retirement Suitability Score:**	C	**Total Return Percentile:**	67.3%

Overview & Current Events

WPP traces its roots back to 1985 when its founder, Sir Martin Sorrell, purchased a small manufacturer of wire baskets and teapots. The company grew subsequent to Sorrell taking it over through acquisitions and organic growth and today, it is the largest advertising firm in the world. The company should generate in excess of $16 billion in 2019 revenue and has a market capitalization of $15.5 billion. The stock is listed in London and New York, but we'll be using US dollars for this report unless otherwise noted.

WPP reported its Q1 trading update on 4/26/19 and results were weak, as expected. The company is still reeling from huge client losses in 2018 stemming from the tumultuous exit of the company's founder, Martin Sorrell. However, WPP did manage 0.9% of revenue growth in Q1, and it appears the worst of the client exits are over.

The gain was due in part to favorable currency exchange movements as constant currency revenue was down 0.6% in Q1. Like-for-like revenue was off 1.3% compared to the year-ago period, while revenue minus pass-through costs was down 0.7% on a reported basis, down 2.3% on a constant currency basis, and down 2.8% like-for-like. Results were expected to be weak in Q1 and they were, but the important thing is that WPP's top line appears to have stabilized.

The company said its financial targets for this year are unchanged after Q1, and reiterated its 2021 goals of 15% operating margins and positive organic growth. As a result, we are reiterating our estimate of $6.40 in earnings-per-share for this year.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	$2.60	$3.53	$4.37	$4.79	$5.53	$6.27	$6.54	$6.70	$9.18	$5.47	***$6.40***	***$7.42***
DPS	$1.36	$1.26	$1.51	$2.02	$2.50	$2.91	$3.28	$3.31	$3.97	$4.07	***$3.97***	***$4.50***
Shares	251	252	252	253	270	265	266	266	254	248	***245***	***240***

WPP's earnings history has been impressive in the past decade, but we see a number of challenges moving forward. As a result, we forecast just 3% earnings-per-share growth in the coming years.

We see growth as being limited by some key factors. First, revenue growth has been and should continue to be a problem. WPP is divesting non-core assets and while this is generating significant cash proceeds, it is also crimping the top line at WPP. Core revenue growth should remain in the low single digits and combined with divestitures, may lead to more quarters of very little or no revenue growth. Margins are an issue right now as well but WPP is looking at its structure and ways to save operating costs. The effort is still in its infancy, so we'll have to wait and see if anything comes to fruition there, but for now, margins are a headwind. The company is buying back its stock and has repurchased a small amount thus far. Should the share price remain depressed, it is likely WPP will be able to buy a more substantial number of shares and thus, boost earnings-per-share via a lower share count.

The dividend is around $4 this year, but we are more cautious on dividend growth now that WPP's revenue issues are clearer. With the payout ratio already reasonably high, we see limited upside for the payout for the foreseeable future, although the yield will certainly remain robust. Note that the UK has no foreign investor dividend tax on common stock, so the net yield is the same as the headline yield.

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Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	14.3	14.8	13.1	13.6	16.5	16.7	17.2	16.6	11.1	14.1	***9.3***	***11.0***
Avg. Yld.	3.7%	2.4%	2.6%	3.1%	2.7%	2.8%	2.9%	3.0%	3.9%	5.3%	***6.7%***	***5.5%***

WPP's valuation has suffered immensely during this period of transition and today, the stock is trading for the lowest valuation in the past decade. At just 9.3 times this year's earnings, WPP looks well below fair value, which we see as 11 times earnings. WPP's average historical multiple is closer to 15, but the uncertainty of a new CEO and transition plans has us a bit more cautious. The yield is also quite high at 6.7%, which we see moving down over time to under 6%.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	49%	35%	30%	40%	42%	43%	47%	48%	41%	74%	***62%***	***61%***

WPP's payout ratio is quite high by its own historical standards, so we see limited upside to the dividend in the near term. That said, the dividend is safe and barring a shift in capital allocation strategy, it should drift higher over time.

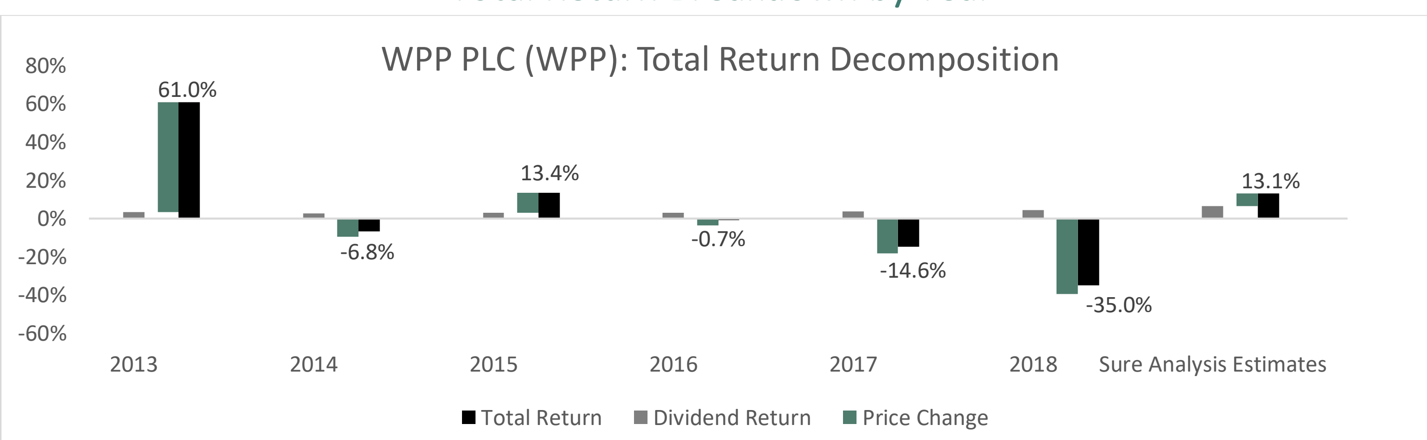
WPP actually performed quite well during the last recession, although earnings did decline by 27% in 2009. Earnings quickly rebounded, however, and crested the pre-recession peak by 2011. The dividend wasn't cut during the Great Recession in the company's home currency.

WPP's competitive advantage used to be that it was the premier advertising business in the world, attracting the largest companies the globe has to offer. However, since the scandal that caused long-time CEO Martin Sorrell to be shown the door abruptly, WPP seems to have lost that edge. For context, Sorrell left WPP amid allegations of misuse of company funds and inappropriate treatment of junior staff. The company is working hard to regain that advantage, but today, competitive advantages for WPP are hard to come by as its brand has been damaged. Repairing of the brand that was so closely tied to Sorrell personally appears to be underway, but WPP still has much work to do.

Final Thoughts & Recommendation

We still see WPP as attractive given its valuation and yield. We forecast total expected annual returns of 13.1%, consisting of the current 6.7% yield, 3% earnings-per-share growth and a 3.4% tailwind from the valuation. WPP would therefore be suitable for value and income investors and given the combination of a low valuation and high yield, we rate the stock a buy. There will be a period of transition, so this is for long-term investors, but WPP looks attractive.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	13603	14385	16070	16437	17241	19004	18698	19496	20406	20817
Gross Profit	12501	13197	14814	15077	15765	16591	16084	4120	4100	3921
Gross Margin	91.9%	91.7%	92.2%	91.7%	91.4%	87.3%	86.0%	21.1%	20.1%	18.8%
SG&A Exp.	1083	N/A	N/A	N/A	N/A	N/A	N/A	1325	1636	2011
D&A Exp.	624	587	615	628	649	620	563	580	597	726
Operating Profit	1193	2631	3079	3141	3387	3719	3641	2795	2464	1910
OP. Margin	8.8%	18.3%	19.2%	19.1%	19.6%	19.6%	19.5%	14.3%	12.1%	9.2%
Net Profit	686	903	1347	1304	1465	1776	1773	1897	2346	1418
Net Margin	5.0%	6.3%	8.4%	7.9%	8.5%	9.3%	9.5%	9.7%	11.5%	6.8%
Free Cash Flow	886	1763	661	916	1705	2455	1702	2017	1397	1759
Income Tax	244	293	147	312	444	495	378	527	254	432

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	36145	37574	38050	40202	41185	41437	42592	42468	45500	42975
Cash & Equivalents	2695	3033	2999	3144	3663	3911	3530	2994	3232	3354
Acc. Receivable	12207	13649	9715	10026	14986	9864	10073	9895	10662	10230
Inventories	496	565	514	563	502	509	487	492	573	465
Goodwill & Int.	17300	16994	17397	18236	18371	18130	18350	18958	20232	19090
Total Liabilities	26320	27314	27427	28792	28246	29255	30717	30468	32037	30531
Accounts Payable	15806	18063	11237	11680	17662	12212	12649	12664	13369	13354
Long-Term Debt	6965	5948	6797	7703	7358	7452	8286	8068	9290	8451
Total Equity	9531	9950	10267	11007	12511	11674	11315	11455	12829	11905
D/E Ratio	0.73	0.60	0.66	0.70	0.59	0.64	0.73	0.70	0.72	0.71

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	1.9%	2.5%	3.6%	3.3%	3.6%	4.3%	4.2%	4.5%	5.3%	3.2%
Return on Equity	7.6%	9.3%	13.3%	12.3%	12.5%	14.7%	15.4%	16.7%	19.3%	11.5%
ROIC	4.1%	5.5%	8.0%	7.1%	7.4%	8.9%	8.9%	9.4%	11.0%	6.5%
Shares Out.	251	252	252	253	270	265	266	266	254	248
Revenue/Share	54.93	53.71	59.87	60.76	63.37	71.04	71.20	75.21	79.97	82.53
FCF/Share	3.58	6.58	2.46	3.39	6.27	9.18	6.48	7.78	5.47	6.97

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.