

Ad Agency Publicis Outlook Revised To Stable On Expected Steady 2009 Credit Measures; 'BBB+/A-2' Ratings Affirmed

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Publication Date

November 23, 2009

Overview

- We expect French advertising agency Publicis to post satisfactory and relatively stable year-on-year credit measures at year-end 2009, despite the deep, ongoing advertising recession and the company's acquisition of digital agency Razorfish for about €369 million in August 2009.
- We think General Motors Corp.'s U.S. Chapter 11 bankruptcy filing in June 2009 will likely have a very modest financial impact on Publicis' capital structure.
- We are revising our outlook to stable on Publicis and affirming the 'BBB+/A-2' long- and short-term ratings.
- The stable outlook primarily reflects our expectations for satisfactory credit measures over the medium term.

Rating Action

On Nov. 23, 2009, Standard & Poor's Ratings Services revised its outlook on France-based advertising agency Publicis Groupe S.A. to stable from negative.

At the same time, Standard & Poor's affirmed its 'BBB+' long-term and 'A-2' short-term corporate credit ratings on Publicis. We also removed all ratings from CreditWatch with negative implications, where they had been placed on June 4, 2009.

Rationale

The outlook revision is based mainly on our expectation that Publicis' 2009 credit measures should be close to stable versus 2008 figures and at satisfactory levels for the ratings, despite the deep, ongoing advertising downturn and the company's acquisition of digital communications agency Razorfish for about €369 million in August 2009. The company's adjusted debt-to-EBITDA ratio at year-end 2008 was 2.5x, stable against the year-end 2007 figure.

In addition, we believe that the financial impact on the company's capital structure of General Motors Corp.'s (GM) U.S. Chapter 11 bankruptcy filing will likely be very modest and that it is consequently no longer a concern for the current ratings. GM's filing on June 1, 2009, was the main driver behind our decision to place the ratings on Publicis on CreditWatch with negative implications on June 4, 2009. Publicis had evaluated its financial exposure to GM at a maximum of €9 million when it released its first-half 2009 results.

The ratings on Publicis reflect its position as the one of the world's top four largest advertising agency holding companies, its above average geographic diversity and profitability, and good discretionary cash flow generation. Partially offsetting these factors are exposure to cyclical customer advertising spending, particularly in the automotive sector; the competitive nature of the advertising and marketing services industry; and Publicis' more limited diversification in marketing services than its main peers.

The severe advertising spending downturn since the last quarter of 2008 has resulted in a 6.9% like-for-like revenue contraction at Publicis in the first nine months of 2009. Publicis' organic growth continued, however, to compare favorably to rates at peers in third-quarter 2009, and we expect this to persist in the remainder of the year. In addition, our expectations of modest top-line improvement and cost-cutting effects in the second half of the year should enable the company to reduce its expected full-year 2009 EBITA margin slide, against the 200 basis-point fall recorded in first-half 2009.

We anticipate that favorable currency effects and good working capital management may offset the combined impact of margin reduction and the Razorfish acquisition on credit measures at year-end 2009, leaving them broadly unchanged from 2008 levels. The group funded nearly half of the transaction price through existing treasury shares. Furthermore, the full effect of cost reduction initiatives taken throughout 2009, combined with our anticipation of a slow but gradual improvement in worldwide advertising markets over the next few quarters, could result in strengthened profitability and credit measures in 2010.

Liquidity

Publicis' liquidity is adequate in our view to fund its business needs and upcoming debt maturities. The company had cash balances of about €1.2 billion at Sept. 30, 2009, covering short-term maturities of €234 million (including fair value of associated derivatives). These were mostly made up of €146 million of outstanding convertible bonds due 2018 that the company expects to be called in January 2010. Other short-term financial liabilities mainly consist of about €111 million of minority buy-out commitments and earn-outs.

The company issued a €719 million convertible bond in June 2009, which will mature in 2014, and will help refinance the outstanding 2018 bonds, as well as anticipate Publicis' closest next debt maturity, which is its €775 million Eurobonds due 2012 (including fair value of associated derivatives).

In addition to cash balances, Publicis benefited from committed and available funding as follows:

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- A €1.5 billion revolving facility maturing in 2012;
- €450 million in bilateral credit lines maturing in 2014; and
- €205 million in revolving credit lines maturing within a year.

The company has no financial covenants on its debt instruments.

Publicis enjoys good discretionary cash flow generation owing to the business' low capital requirements—less than 2% of sales—and moderate dividend payments. The company froze the dividend per share distribution for 2009 in light of the tough trading conditions. The revenue and profitability contraction expected for the full-year 2009, however, should result in sizable reductions in nominal free and discretionary cash flows from their 2008 levels.

We estimate that Publicis generated free and discretionary cash flows of about €20 million and €190 million, respectively, in 2008. The company's free and discretionary cash flow generation is still set to remain solid over the coming years, and to account for about 65% and 50%, respectively, of EBITDA.

The company's healthy cash flow generation should enable it to continue covering bolt-on acquisitions while maintaining a sound capital structure. Publicis bought back and subsequently cancelled 8 million shares, worth about €195 million, in 2008. We do not expect significant share buy-back activity in the short term, however, and we anticipate that the company will likely continue to prudently use its cash and make moderate use of share repurchases while the advertising sector remains depressed.

Outlook

The stable outlook reflects our expectation that Publicis will deliver relatively steady and satisfactory credit measures over the medium term. In particular, it integrates our view that worldwide advertising markets may show a slow but gradual improvement in 2010, which together with cost cutting undertaken in the past few quarters should result in improved profitability and credit measures for the company in 2010. In addition, we expect Publicis to maintain a moderate financial policy with continuing moderate shareholder distributions and add-on acquisitions. A sustained ratio of adjusted average debt to EBITDA of about 2.5x would be in line with the current ratings on Publicis.

Any marked deterioration in the company's operating performance or a change in financial policy—for instance through noticeably higher shareholder returns and/or sizable debt-financed acquisitions—may produce downside ratings pressure.

We do not see any rating upside at this point, given the expected medium-term profitability and credit measures improvements already incorporated into our ratings on Publicis.

Related Research

Business Risk/Financial Risk Matrix Expanded, May 27, 2009

Ratings List

Ratings Affirmed; CreditWatch/Outlook Action

	To	From
Publicis Groupe S.A.		
Corporate Credit Rating	BBB+/Stable/A-2	BBB+/Watch Neg/A-2
Senior Unsecured	BBB+	BBB+/Watch Neg

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