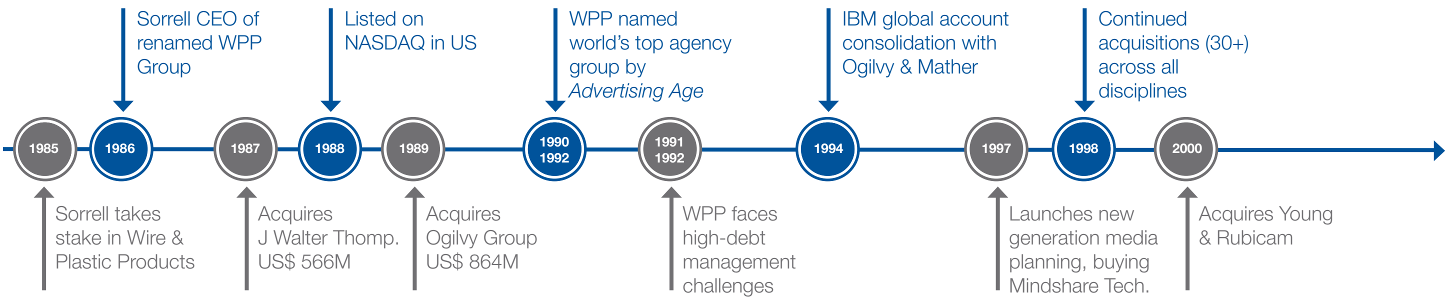
WPP | United Kingdom

OVERVIEW:

Wire & Plastic Products Plc was founded in 1971. Until 1985, it operated purely as a manufacturer and distributor of wire and plastic products and was publicly traded on the London Stock Exchange. Martin Sorrell was part of a group that acquired the company to use as a public entity to build a worldwide marketing service company. He became chief executive officer in 1986 and renamed it WPP. By 1998 WPP was the largest marketing communications company globally. This position was achieved through a strategic combination of acquisitions and organic growth.

WPP

TIME-LINE / KEY EVENTS



QUOTATIONS FROM:

Sir Martin Sorrell (born in London, United Kingdom) has led WPP as chief executive officer since its "restart" as a marketing communication company in 1986. Sorrell was Group Finance Director of Saatchi and Saatchi from 1977 to 1985 and was sometimes was referred to as the "third brother" of Charles and Maurice Saatchi. His prior business experience also included IMG, the sports marketing company led by Mark McCormack. Sorrell was knighted in the United Kingdom in 2000. Educated at Christ's College, Cambridge, and the Harvard Business School, Sorrell has been widely viewed as an early and ardent champion in the 2000 to 2010 decade (and earlier) of business activities in emerging economies.

What was the source of the initial idea, and how did that idea evolve into a viable high-growth business venture? How did it change over time?

Sorrell: "The source of the initial idea was starting my own business at the old age of 40 – what's called andropause, which is male menopause – that really was the start. We focused on multinational marketing services companies because of what I'd learnt at Saatchi & Saatchi. I was capitalizing on the experience and whatever the reputation of my nine years at Saatchis as CFO and hopefully not making the mistakes we made there – although we made plenty of mistakes afterwards.

"The concept was to build a major multinational marketing services company. This was signalled in the very first document we issued as Wire & Plastic Products in May 1985. I decided at the beginning to focus on what we thought were the unloved, fragmented areas of marketing services: areas of promotion, design services, what were crudely called 'below the line' services. These almost below-the-salt areas of activity were not fashionable. They were also fragmented and therefore had the potential to be consolidated quickly. Within 18 months we did 18 acquisitions, we had a P/E multiple of about 150 times earnings.

"The initial idea changed after a year or so. One of the criticisms made during our so-called hostile takeover for JWT in 1987 was that JWT included not only public relations (Hill & Knowlton), market research (BMRB) and other below-the-line activities, but also a big advertising agency (J Walter Thompson). People said, 'Isn't this countercultural for a company with an avowed focus on 'below the line' services?' We then made the basic change to include in our focus both above-the-line and below-the-line. Logically, that made sense because today the industry is a trillion dollar industry of which half is advertising and above the line and half (i.e. US$ 500 billion) is below the line, including market research."

What was the initial growth vision or aspiration of the founding team? Was there a sizeable change in this growth vision or aspiration over time? If a change, please describe.

Sorrell: "Originally I initiated the search for a shell company – what the French call a coquille – with a stockbroker called Preston Rabl, who co-invested with me at the beginning and then I topped up my shareholdings. We had between us about 29%. In those days, you triggered a bid – today you still do – if you're over 30%. If there was one mistake made, it's probably that we should have made a compulsory bid, gone over 30%, soaked up more shares at the beginning – there would then be dilution through acquisition. That was probably a practical mistake at the beginning. About the time of the JWT bid, Preston and I then went our different ways. Preston's view was that you shouldn't do things on scale. My view always was to start something, and run it, of scale. Running something small was not really of interest, particularly having been involved with Saatchis for nine years. I wanted to capitalize on my knowledge in the advertising and marketing services business, and whatever reputation I had at that time. I wanted to start something – in other words, be entrepreneurial – but I also wanted to manage something. Often people who can start something can't run it, and people who can run things can't start them. I think the role of entrepreneur is fundamentally different to the role of manager.

"I don't think the original vision or aspiration of WPP changed over time. However, the emphasis on building a global advertising and marketing services organization did change in the sense that we moved from where we were to a company that today focuses on new markets, new media and consumer insights. New markets account for almost 30% of our business, new media for almost 30% of our business and consumer insight for almost 30% of our business. So we changed our growth objectives. For instance, we identified China as being critically important as early as 1993. We held our first board meeting in Guangzhou in 1989, and acquired our first Chinese operations through JWT in 1987. We started to focus on new media in the mid and late-1990s, before Internet 1.0. So really I would say we have had the same growth vision and aspiration, but it changed in time in terms of emphasis."

Describe the strategy or business model that enabled your company to achieve its high rate of growth.

Sorrell: "If you start as a wire basket manufacturer 25 years ago with two people in one room and your objective in your lifetime is to build a major advertising and marketing services company, you have to do it primarily by acquisition otherwise you'd be dead before you got very far! But the strategy and business model has remained the same. In the early stages, you focus on growth through acquisition and then organic growth becomes more and more important as you pick out the growth segments like new markets, new media and consumer insight.

"There have been several distinct phases at WPP: 1985 to 1990, 1990 to 1992, 1992 to 2000, and 2000 to 2010.

"The period from 1985 to 1990 was essentially a growth phase by acquisition, the largest of which were JWT in 1987 (13 times our size) and Ogilvy in 1989 (twice our size). Both were described as 'hostile', although there is no such thing as a hostile acquisition. It's only hostile to the CEO. It's not hostile to the clients, it's not hostile to the people inside the company and it's certainly not hostile to the shareowners.

"We then ran into severe trouble because I overleveraged the company in 1989.

"The restructuring phase in 1991 and 1992 had two parts. The first was the rescheduling of debt. The second was the debt-for-equity swap, which at its time was revolutionary. That was quite a ballsy thing to do as banks really hadn't focused on service businesses and debt-for-equity swaps in service businesses. We never missed an interest payment or a debt payment despite the challenges.

"The 1992 to 2000 period was an organic growth phase. Having come out of the tunnel of that terrible two years – it was a very tough two years – the basic fabric of the business remained very much intact and growing. The problem was within TopCo, whose name was not the same as the operating companies. This separation was an advantage. So you had WPP and then companies like JWT, Ogilvy, Hill & Knowlton and Millward Brown underneath it. Having come out of that, from 1992 to 2000, we did acquisitions but on smaller scales.

"Then in 2000, we effectively increased our size by 50% with the acquisition of Y&R, and through to 2010 we continued to build the business organically and by acquisition. Every two or three years, we've made significant sized acquisitions: 2001, a somewhat controversial CIA acquisition on which, after 9/11 we tried to invoke the material adverse change clause. Despite the fact that we were unable to do so (the takeover panel ruled against us), that has proven to be an extremely successful acquisition. Then in 2005, we acquired Grey. All these acquisitions were around 5, 10 or 15% of our size, and then in 2008, TNS. From 2000 to 2010 we have continued to build the company based on the mantra of new markets, new media and consumer insight – organically and by acquisition. It's fundamentally the same model. It's understandable that organic growth has become more important since 2002. If you start in 1985 with a £ 1 million market cap wire basket manufacturer (today we're £ 9 billion), obviously the emphasis (the law of big numbers) changes the mix by which you grow."

What were the major growth accelerators for your company in its high-growth years?

Sorrell: "A major reason why we've grown, (obviously acquisitions made a difference but even if you pro forma it, we've grown significantly) is that we've tried to focus on where the growth areas are. At the moment, if your business is located in Asia and the Pacific you're going to grow faster than if it's located in Western Europe. We try to identify growth trends in our industry and our continued growth rate will be dependent on that. It will also obviously be dependent on finding the best acquisition, but primarily it will be pushing on open doors. Warren Buffett's old saying holds in my view – if you put good management together with a bad business the bad business always wins. It doesn't matter how clever you are, if you're pushing on a closed door it's much more difficult.

"There have been two principle accelerators for us – geography and technology – that drive everything. All problems, in my view – and it's a simplistic thing to say – can be reduced to those two elements. If you think about classical economics, those supply and demand models had certain criteria and a couple of the criteria are very important because they've driven our business. One has been free trade and lack of protection, and that has basically driven our business because it's taken hundreds of millions of people out of poverty (in, for example, India or China) and moved them into the middle class. Also, in Brazil or Russia. And then there's the free flow of information. Google has created information for everybody. Information is no longer power: it's your ability to use it, certainly at zero marginal cost. So those two things that you learnt about in supply and demand models are very relevant, ironically, for the growth of our business. So I would say pick the markets and they have accelerated because of things like free trade and free flow of information."

Briefly describe the financing of your company and how this financing impacted the growth of your company.

Sorrell: "We've used judicious amounts of debt and equity, taking advantage of the fact that you can deduct debt interest. We've made mistakes. I overleveraged the company in 1989 and with the Ogilvy acquisition forgot that convertible preferred stock in a recession becomes preferred stock. The coupon was extremely expensive because you couldn't deduct preferred stock interest for tax, so I think the gross cost was about 10.5%. I always remember somebody from the Prudential saying to me when we did our convertible preferred rights issue, 'Anything you can do, Martin, with a convertible you should be doing with your equity'. And in the fullness of time, having gone through that restructuring period from 1990 to 1992, he was dead right. If we had just done it through straight equity, although there would have been further dilution, we probably wouldn't have had to go through such a severe restructuring.

"Essentially we now aim to use free cash flow first and also a mix of debt and equity. I would say we probably used too much equity in the past. I now own about only about 1.5% of the company, and absent having built a bigger stake at the beginning, which I should have done, the one way of having that stake greater would have been by buying back more stock in the market or by not having sprayed around so much equity in terms of acquisition. Essentially, small acquisitions we funded out of cash flow; medium and large acquisitions we funded with a mixture of debt and equity."

What were the major challenges your company had to handle in its high-growth years, and how were they managed?

Sorrell: "You're putting this in the past tense and I'm somewhat hesitant to answer because I hope high growth has not deserted us and it's not the law of bigger numbers. I think the major challenge, particularly in our business, is that scale brings some perceived – and I underline perceived and I'll underline it again – disadvantage. Clients think the bigger an agency gets the worse it gets, the more impersonal it is. David Ogilvy always used to say once you get beyond about 350 people in one location it gets rather impersonal and I think that's true. But the nature of our business has changed in that respect, (certainly from the 'Mad Men' era, it's changed). As a creative business, we do strategic thinking, creative execution (the development of big, creative ideas), distribution, as well as the application of technology and the analysis of data. So there are five things we do now.

"The major challenge in an industry, which is basically creatively-led, is that there are diseconomies of scale. With the exception of media planning and buying – where we buy around US$ 65-US$ 70 billion of media around the world and have a market share of, say, 25-30% – the bigger our businesses get, the more difficult they are to manage. And it's exponential, so if a creative department doubles in size it's three or four times more difficult to manage.

"The other big challenge is to get everybody to play together in the sandpit. It's amazing how ingenious human beings are in finding ways not to co-operate. We had a co-ordination problem with two people in one room 25 years ago. Today you can imagine the issues dealing with 140,000 people where we don't even have control of some of the businesses (we own 20% to 49% of them) with 100,000 people that we actually control directly – it's very difficult."

Give examples of dark moments or negative periods that your company or you faced as part of your journey as an executive with this company.

Sorrell: "The period from 1990 to 1992 presented the biggest challenge when people would say we nearly went bankrupt, we were over-leveraged. The market always goes one way and another and in dark moments, it always goes too far one way or the other. But the darkest moment was then. On the other hand, intellectually, whilst it was a challenging time it was a very interesting time. The biggest test of companies, people, individuals, families and countries is in their darkest moments, in their toughest moments. It's not the easy times that are the true test, it's the difficult times. In those dark moments in 1991 and 1992 I never ever thought that we were going to go down. Not even for one second.

"Dealing with the bankers was difficult because they didn't have rules for service companies; they had rules for manufacturing companies. I remember at one meeting, a German banker said, 'Why don't we control capital expenditure?' So I said to the bank, 'If you want to control spending in our company I could blow a big hole through your capital budget constraint at the first remuneration committee meeting (we had little capital expenditure at that time – it was a small amount of around £ 350 million), and if you want to control it you should join me at the remuneration committee meeting'. If I was him I would have said, 'Yes I will', but he said no. So it was quite difficult at that time for banks to get their minds around dealing with service businesses. But I would say that was the darkest moment.

"I'm trying to think back now as to whether there were moments of challenge when we were trying to do things and we didn't. Anything we've set our minds to doing in terms of buying companies, certainly public companies, we've never been defeated and I don't think – bravely said! – we will be because I think we've always been pretty ingenious. I think we've always had the ability to turn on a sixpence, which I think is vital. The challenge to big companies is sclerotic structures that prevent them turning on a sixpence. The key for big companies is to be entrepreneurial, and for entrepreneurial companies to have the scale and resources of big companies."

What are the key lessons about entrepreneurship and successful growth strategies you've taken from your company experience?

Sorrell: "I think a fundamental lesson is that being entrepreneurial and being a big company is regarded by many people as being counter to one another, in conflict with one another. The key is to try and make sure that they are not. In other words, as companies grow and get bigger their biggest dangers are themselves. The biggest enemies are from within, not from outside. The key lesson is that as you grow you have to try and keep it small. This sounds completely illogical and nonsensical, but you know what I mean. The general view is that the bigger you get, the worse the problems that scale brings. If you said to me, 'What's the biggest enemy to Google?' I would say scale. The biggest danger is from within, not from without – not from Apple, not from Facebook, but within.

"Building and managing a multi-branded company which grows by acquisition is a very difficult growth model. If I was doing the Harvard

Business Review article on it, the simplest model would be uni-branded, which is organically grown. Of the service industries, there is no doubt that the best brands are McKinsey and Goldman Sachs. One reason is that they recruit relentlessly in the best schools and the best universities. We have to mimic the same. Both McKinsey and Goldman have very strong cultures, very strong constitutions.

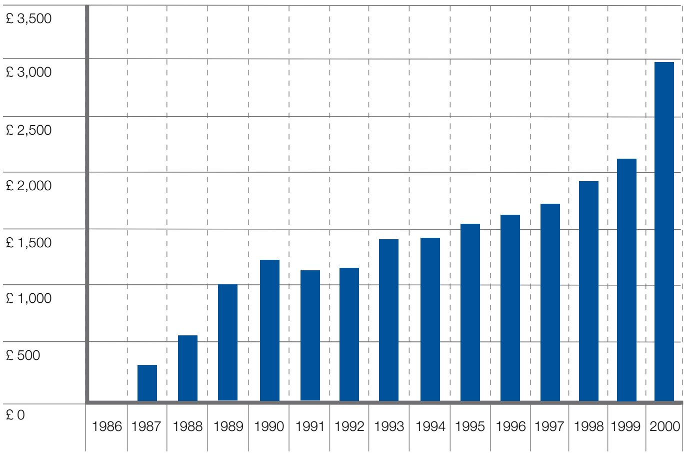
“Terms like culture and entrepreneurialism have, unfortunately, been used in ways that are clearly dysfunctional. Many now use the word culture to justify not doing what you want them to do. They say, ‘It’s not in their culture’, when it means that they really don’t want to do it. When people say they want to be entrepreneurial, they often want to be entrepreneurial with your money. Entrepreneurial means taking risks with your own money. Incentives are critically important, and getting people to put money on the table, not options. Warren Buffett is clearly right: you wouldn’t give a financial institution an option over your stock for seven or 10 years at zero cost, so why should you do it with management? Management should put money into their company, act entrepreneurially, and take risk.

“When people talk about entrepreneurialism inside big companies, often what they actually mean is autonomy, which is, ‘Leave me alone to get on with things and don’t interfere’. I disagree with this because it comes back to networking. Even the companies that we compete against – who’ve made great virtues of saying, ‘Come into our group, and we’ll leave you alone’ – know today that that doesn’t work. What clients want is the best resources on their business. They don’t care whether it comes from Ogilvy or JWT or Y&R or Grey or Millward Brown or Landor. They want the very best people working on their business. Building teams, as we are doing at WPP, such as Team Ford, Team Unilever, Team Procter, Team J&J, Team Nestlé, etc., and having Country Managers who co-ordinate our business horizontally on a country-by-country basis, is the way that we’re going to get people to work together.” ■

WPP

REVENUE

MILLIONS (£ M)



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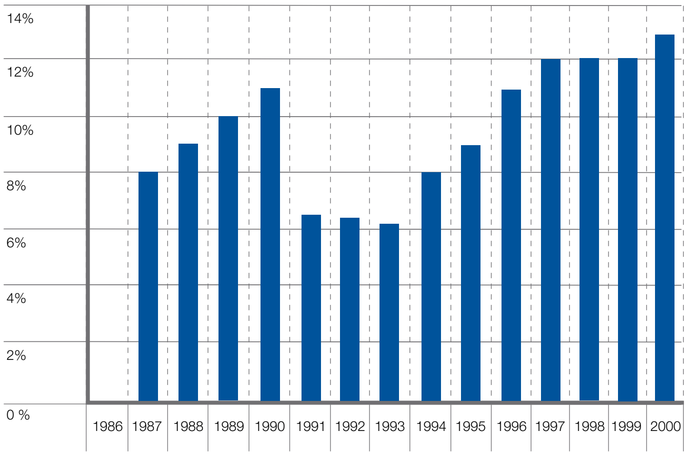
OPERATING INCOME/REVENUE



Prepared by George Foster, Max von Bismarck, and Benjamin de los Heros, 16 November 2010