EDISON

Dentsu Group

New medium-term plan actioned

Q1 results and plan appraisal

Media

23 May 2025

Dentsu Group's Q125 figures show 0.2% organic net revenue growth and an improvement in operating margin. Japan performed well, with international operations more challenged. Dentsu's new management plan aims to drive profitability and competitiveness, particularly ex-Japan. It targets up to ¥50bn of operating cost reductions, returning the group to consistent profit growth from FY27. The ¥50bn cost of reshaping the group weighs on FY25 profits but should result in a simpler organisation. A further ¥45bn will be invested over three years with the aim of no markets being loss-making by FY26. The group will focus on the key Japanese and US markets, with the international business centred on adding value to Dentsu's existing strengths in media. The goal is to achieve a mid-teens return on equity by the plan's completion.

Year end	Net revenue (¥m)	PBT (¥m)	EPS (¥)	DPS (¥)	P/E (x)	Yield (%)
12/23	1,144,819.0	151,631.0	339.79	139.50	9.3	4.4
12/24	1,201,647.0	162,167.0	355.24	139.50	8.9	4.4
12/25e	1,215,000.0	124,439.9	275.25	139.50	11.5	4.4
12/26e	1,281,770.6	166,520.9	370.74	139.50	8.5	4.4

Note: PBT and EPS are normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments. FY23 and FY24 net revenue includes ¥15,249m and ¥7,578m from disposed Russia business.

Reshaping against difficult markets

Q1 figures showed Japan (c 45% group net revenue) posting organic net revenue growth of 5.5% and a step up in operating margin to 29.0% from 27.6%, while the international business posted organic declines in all three regions, with the Americas (c. 27% group net revenue) down 5.1%. The degree of global macroeconomic uncertainty is an unhelpful backdrop to the strategic decision-making required in the new management plan, but there is little to be gained by delaying. There is a general internal acknowledgement that Dentsu needs to play more to its strengths, rather than try to match up against the larger global peers. This involves focusing on its core markets, consolidating its position as the dominant major player in Japan and leveraging its strong media-based offering in the US.

Targets look credible, subject to global macro

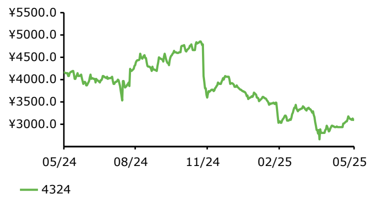
The key FY27 financial targets are for organic growth of 4.0%, with an operating margin of 16–17% and operating cash flow of ¥140bn. The guided return on equity is in the mid-teens. While our formal forecast horizon does not currently extend to FY27, we model FY26 operating margin recovering back to the FY24 level of 14.7%, having dipped with the planned investment spend in the current year. On a reduced cost base and with the operational leverage of increased scale in a narrower range of markets, the guided margin expansion looks to us to be achievable.

Valuation: Discount narrowing

Global macroeconomic uncertainty has affected the share prices of all the major global peers. On EV/EBITDA averaged across FY24–26, Dentsu now trades 16% below peers, from 26% in February. Our view is that the market is not yet giving any attribution to the likely beneficial impact of the restructuring and new plan.

Price	**¥3,160.00**
Market cap	**¥840bn**
Net debt as at end December 2024	¥175,265.0m
Shares in issue	265.8m
Code	4324
Primary exchange	TSE
Secondary exchange	N/A

Share price performance



%	1m	3m	12m
Abs	9.8	1.7	(21.9)
52-week high/low		¥4,821.8	¥2,652.0

Business description

Dentsu Group is a holding company, operating in more than 120 countries. It provides a wide range of client-centric integrated communications, media and digital services.

Next events

Q225 figures	Mid-August 2025

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Investment summary

Dentsu describes itself as a 'Business-to-Business-to-Society (B2B2S)' company. It aims to provide its clients with integrated growth solutions (a phrase that we discuss below). It consists of a global network of marketing and communication agencies that provide integrated services to help brands plan for the future and achieve growth. The offering includes services across media, customer experience management and creative, focusing on both experience and business transformation. Headquartered in Tokyo, Japan, the group has grown organically and through acquisition, with net revenue outside of Japan accounting for 61% of the FY24 group total. (Net revenue is widely used across the sector as the key top-line measure to avoid the distortions of media costs passed through to clients.)

The previous management plan aimed to tackle the proliferation of agencies and legal entities and to bring the commercial offerings under a limited number of agency brands. The newly launched plan, which runs from FY25 to FY27, is more strategic and looks to focus the group's core effort on the Japanese and US markets, the former being the home market where the group has a leading position, the latter being the largest market globally. With the competitive landscape changing, Dentsu intends to maintain good relationships with its large global clients, as well as placing a focus on the large and medium-sized clients in each market where it has a strong presence and capability set, servicing their requirements both locally and internationally, where relevant.

Financials

Dentsu's good financial performance in its home market has been overshadowed by mixed results from its international businesses, where past acquisitions have not necessarily either delivered on their expected projections or worked coherently alongside and to the advantage of other group companies. The new plan aims to eliminate the loss-making geographies and increase internal co-ordination to deliver better results both for clients and for the group. If well implemented, this should deliver stronger group operating margins and position Dentsu to present more convincing client propositions, growing the top line. One-off costs of ¥50bn are guided for the current year, with a further ¥45m over the three years of the plan. Write-downs on the balance sheet taken at the end of FY23 and the FY24 figures give a clean basis from which to rebuild. The new mid-term management plan incorporates a target for return on equity for the first time, aligning the group more closely with the objectives of investors.

Sensitivities

The biggest factor affecting top-line progress is the underlying economic backdrop where the group does business, as advertising revenues are highly correlated to GDP. Low levels of corporate confidence continue to affect demand for the larger, business-transformational projects that had been a core area of focus for the group. Operating across many countries, Dentsu is exposed to both transactional and translational currency impacts, reporting financial results in Japanese yen. Competition is a perennial sensitivity, with new business levels highly scrutinised. The group has been undergoing an extended period of major structural and cultural change, which can have destabilising effects. It can also reinject energy and focus. The advertising industry comes with high levels of reputational risk.

Valuation

Dentsu Group is the fifth largest quoted agency holding company globally, after Publicis, Omnicom, Interpublic and WPP. We also include a smaller Japanese competitor peer, Hakuhodo, the recently-listed smaller peer in Europe, Havas, and one smaller but ambitious US-based group, Stagwell, in our peer comparison. All of these share prices have retrenched so far this year, with poor levels of underlying business confidence globally compounded by increasing fears of a US recession. WPP has seen the weakest performance, down 33%, while Hakuhodo has been the most resilient, down 12%. Dentsu's performance lies halfway between at -24%. The resultant valuation metrics fall into a current year EV/EBITDA range of 5.1–7.4x. If Dentsu were to be trading at the peer average over FY25–26 and across both EV/EBITDA and P/E, the share price would be ¥3,663, 16% ahead of the current level. A discounted cash flow (DCF) at a WACC of 10% and terminal growth of 2% returns a value of ¥4,701, well above the level indicated by the peer comparison. Dentsu is currently offering the highest yield in the sector.

Providing integrated growth solutions to brand owners

Dentsu Group is a global leader in media and digital communications, founded and headquartered in Japan and now operating in around 120 countries globally. Dentsu was founded on 1 January 1901 and has therefore a vast heritage on which to draw. It listed on the Tokyo Stock Exchange in 2001, as an international advertising and PR business, growing since that date through a combination of organic progress and considerable M&A activity.

The business emphasis shifted markedly in 2012, when the group announced the acquisition of London-listed Aegis, a deal which completed in 2013 at a cost of £3.2bn and was the first major foray outside of its home market of Japan. In 2016, Dentsu expanded its global reach through the purchase of Merkle in the US. Merkle's objective is to 'use data, technology and analysis to help the world's best brands make their advertising more addressable, their experiences more personal, and manage relationships over time'. The changes to the underlying marketing communications ecosystem, with the growth in importance of Google and Meta, have necessitated a pivot to data centricity, making it a crucial element of Dentsu's client service proposition.

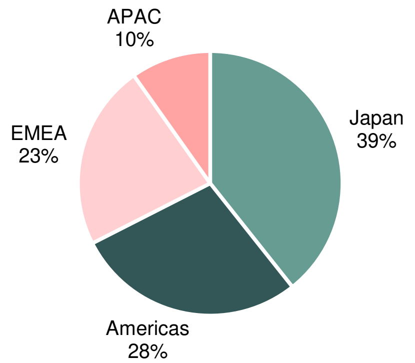
Having grown through an extensive acquisition programme to diversify beyond its Japanese home market, the organisation had become unwieldy and inefficient. An integration programme was initiated in early 2020 and was progressed that summer as an 'accelerated transformation plan'. The objective was to simplify the business and make it fit for purpose, reducing structural overheads and allocating capital to growth and innovation.

With the FY21 results published in February 2022, management set out its strategy for the FY22–24 period, focused around four themes: transformation and growth; operations and margin; capital allocation priorities and shareholder returns; social impact and ESG. Each element had set targets for leadership to reach. For organic growth, a target of 4–5% proved to be beyond reach, given the underlying market conditions, and similarly an operating margin target of 18.0% was overly optimistic. Net debt targets of 1.0–1.5x underlying EBITDA were, however, achieved.

In September 2022, Dentsu announced a further fundamental restructuring, which did away with the differentiation between the Japanese and international operations. The resultant organisation was described as One dentsu, with a unified board, headed by President and Global CEO Hiroshi Igarashi. While in the short term, the prospects for advertising revenue growth in the US have been disrupted, it remains the world's largest market and a key element of Dentsu's offering beyond its own domestic market. Elsewhere, Dentsu is set to concentrate on delivering what it describes as 'integrated growth solutions' to larger and mid-sized clients in each of its geographic markets.

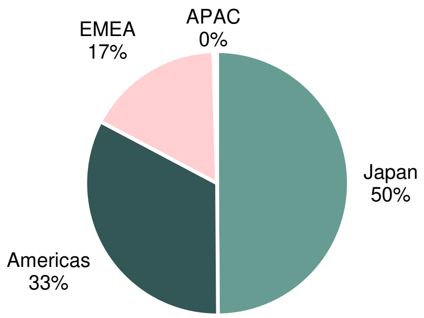
With the FY24 results in March 2025, Dentsu has initiated a new mid-term management plan, which builds on the earlier initiatives to drive efficiency across the group and which is described in greater detail below.

Exhibit 1: FY24 net revenue by geography



Source: Company accounts

Exhibit 2: FY24 operating profit by geography



Source: Company accounts

Japan accounts for half of group operating profits

Dentsu reports its figures for Japan and international operations separately, with the international numbers split out for the Americas, Europe, Middle East and Africa (EMEA) and Asia-Pacific (excluding Japan), as shown below. We discuss the relative performances in greater detail in the financial section below, but it is clear from these exhibits that for FY24, the Japanese business leads the way in revenue and in operating margin, as would be expected in a territory where the group is the clear market leader. The Americas represents the largest region on an industry basis, as shown in Exhibit 8 and discussed below.

What are ‘integrated growth solutions’?

Dentsu describes itself as providing integrated growth solutions, but this may not be a clear indication of its activities to all observers. We understand it to mean a more comprehensive approach to business growth, beyond traditional marketing and sales efforts. It involves integrating various business functions and capabilities in order to drive a client’s top-line revenue growth and increase its market share, often embedded into that client’s workflow. It may include areas like content, media activation, creative work, marketing technology, customer experience management, systems integration and strategic growth planning.

Examples could include the creation of content and media activation to reach target audiences, or using technology to optimise marketing operations and enhance customer experience, or integrating different systems within a business and implementing strategies to support growth.

What does the new mid-term management plan entail?

Why is a new plan needed?

The competitive landscape for marketing services has shifted, with the biggest peers benefiting from their scale. Major tech companies and consultants have also been expanding their reach into areas that would traditionally have been serviced by the main group of holding companies in the sector: Publicis, Omnicom, WPP, Interpublic, Havas and Dentsu itself. With the acceleration of the development and implementation of AI-based solutions, very deep pockets are needed to stay at the forefront.

Dentsu’s earlier growth was heavily predicated on M&A to expand the group’s capabilities and geographic reach. While some of these deals have proved effective, particularly the purchase of Merkle, integration has not been a strength, meaning that the full potential benefits have not flowed through and inefficiencies abound. As described above, there has already been an extensive period of reshaping the business. The messaging now is that this has not been sufficiently swift or rigorous. A great deal of effort has been expended on reducing the number of brands and legal entities. Across FY20–24, a total of ¥152.5bn has been spent on restructuring and a further ¥489.5bn as impairment losses. Despite this, the group still consists of a complex matrix of practices and regions, encouraging siloed mindsets, which management and this plan are addressing.

The objective is to restore profitability and competitiveness in the international business, which in turn will improve the health of the group balance sheet. The initial phase involves ‘re-evaluating underperforming businesses’ and ‘rebuilding the foundations of the business’.

Re-evaluating underperforming businesses realistically relates only to the international businesses. They could be underperforming because of their markets or because they simply have not delivered in the way that was expected when they were bought. So, what constitutes an underperforming market? This is clearly defined as one where investments of at least ¥10bn have been made (although the timescale is not defined) and where losses have been generated in two or more consecutive years. The group’s financial reporting is not sufficiently granular for us to identify these markets with any degree of certainty and there are obvious sensitivities to public disclosure ahead of the internal communications. It also may be misleading to draw conclusions from those markets that have shown organic revenue retrenchment over recent reporting periods. The Chinese business, for example, services many Japanese clients.

What might fall under the ‘underperforming entities’ category? The wording used refers to recent M&A targets that have not met the acquisition plan’s targets. Across FY22–23, a total of c ¥200bn was spent on 11 completed acquisitions (excluding minority investments). This was across all four regions, with 29% spent in Japan, 31% in the Americas, 28% in EMEA and 12% in APAC.

The goal of this exercise is that at the end of the period, no geographic markets should be operating at a loss and that the international business as a whole should be contributing to increasing shareholder value by the end of FY26, as well as that, by the end of the following year, all four regions of the group should be achieving that objective.

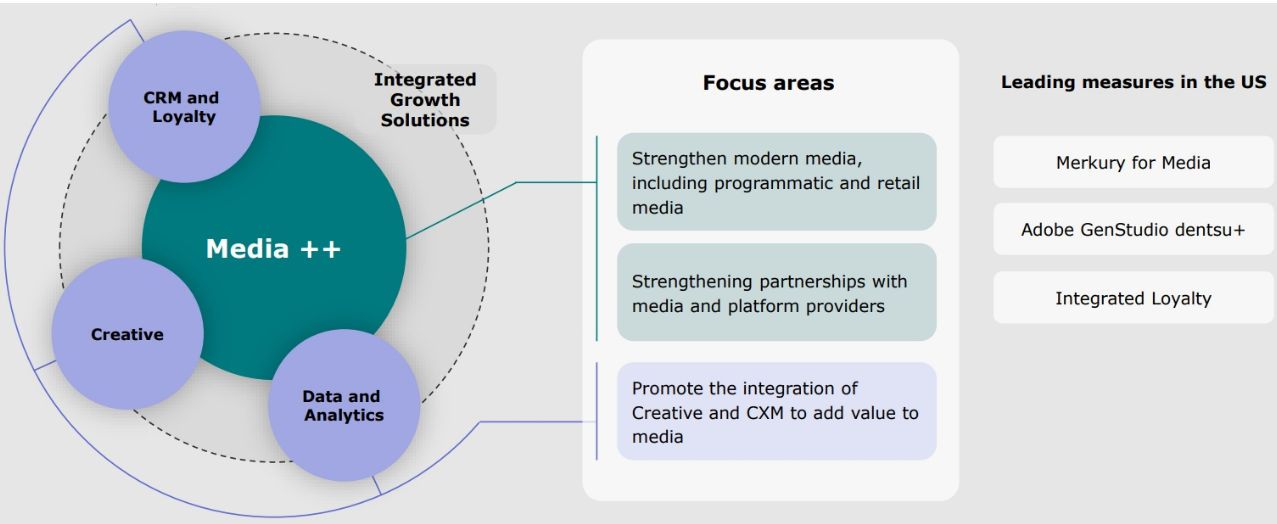
The second element of the plan is described as ‘rebuilding the foundations’, which targets cost savings of up to ¥50bn in FY27 over FY24, equivalent to a reduction of 4.7% in group selling, general and administrative expenses. The first element of this is in terms of the global headquarters. Historically, head office functions have been carried out in Tokyo and in London, reflecting the earlier division of the group between the domestic and the international operations, with London having been the home of Aegis, which was bought for £3.2bn in 2012 (completed 2013). With the One dentsu operating model, there is a degree of duplication of function, particularly regarding teams handling elements such as finance, human resources, legal and IT. Alongside this reorganisation, the role of the regional headquarters will also be re-evaluated to see what functions are best devolved and what is more efficiently handled from the centre.

Beyond the simplification of front, middle and back office structures, Denstu's management is also indicating that greater efficiency can be achieved for the group through standardisation and automation (including the use of AI).

How does this affect the broader strategy?

- The first major shift in emphasis is the move away from the aim to be seen as a group that aspired to meet its clients' needs across all capabilities and geographies, as has been the traditional approach of the holding companies in the sector. The focus is now firmly on the Japanese and the US markets, with other markets catered to where the group already has a strong positioning, such as Taiwan and Spain.
- From a client angle, the new approach acknowledges that Dentsu may not be best placed to pitch for the largest global multifaceted accounts. The focus is to be on the large and medium-sized clients in each market, but not restricted to servicing their needs in that geography. The concept of global accelerator clients continues, with those clients accorded greater attention and tailored programmes, with dedicated account management (which will be strengthened further).
- In the international business, the focus is on the media business as the core element of the integrated growth solutions, with value added through supplementary service offerings as outlined in the graphic below. This approach makes sense for a group that has a strong reputation in the media arena, but may have been falling behind some of its larger peers, consultants and tech firms in data, technology and investment in AI.
- Sports and entertainment has been identified as a key element of the growth strategy, and this is widely recognised across the sector as an important channel for brands to use to build relationships with consumers that align with their interests and passions.
- The quest for engagement and authenticity by brands looking to increase their reach and promote loyalty is another key theme. Here, the influencer economy is rapidly growing in importance. Dentsu has identified the need to participate, with content at the core and partnering with various stakeholders to contribute to the growth of intellectual property globally.

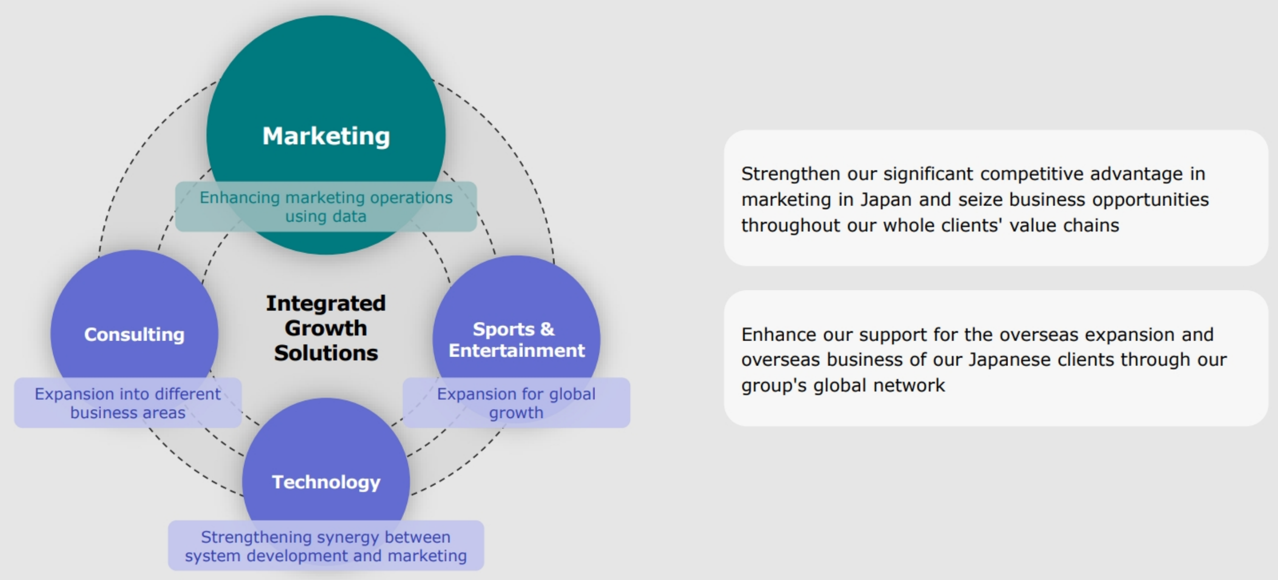
Exhibit 3: Objective for international business in new plan



Source: Dentsu

- In Japan, the core integrated growth solutions will be supplemented with enhanced capabilities in business transformation and in technology, including consulting, technology, sports and entertainment, as illustrated below.

Exhibit 4: Objective for the Japanese business in the new plan



Source: Dentsu

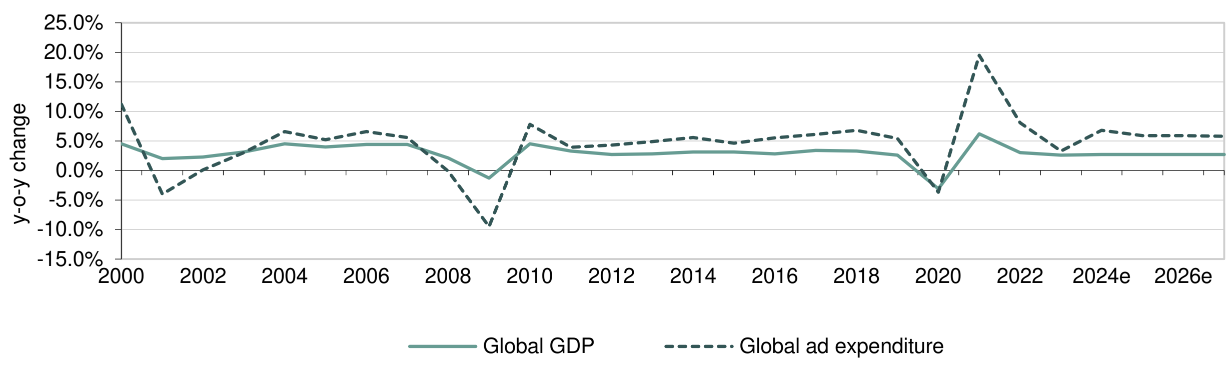
What are the targeted financial outcomes?

Management's key FY27 financial targets, based on successful implementation of the new mid-term plan, are for organic growth of 4.0%, with an operating margin of 16–17% and operating cash flow of ¥140bn. The guided return on equity is in the mid-teens.

Shifting contextual landscape

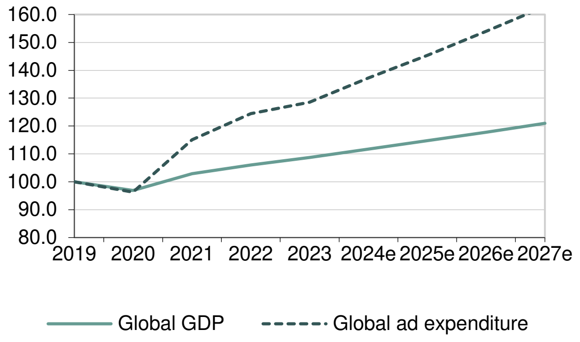
Global advertising spend has a correlation with GDP, as shown below, with advertising spend generally exaggerating the changes in underlying GDP (ie underperforming in times of downturn and outperforming in stronger periods). The US market is the largest by value (see Exhibit 7, below) and Dentsu's latest edition of Global Ad Spend Forecasts shows 6.7% growth in 2024, broadly in line with global growth of 6.8%. The anticipated progress for the current year is for growth of 5.0%, against global growth of 5.9%, but it should be noted that these forecasts predate the market turmoil of recent weeks. Dentsu tends to update its market trend assumptions in May, and it will be interesting to see how these have moderated. For FY25, the fastest-growing markets are expected to be India (6.5%), the UK (5.7%) and Brazil (5.2%). The Chinese market is obviously affected by the local economic backdrop, with more moderate growth of 4.2% pencilled in.

Exhibit 5: Long-term global GDP growth versus ad spend



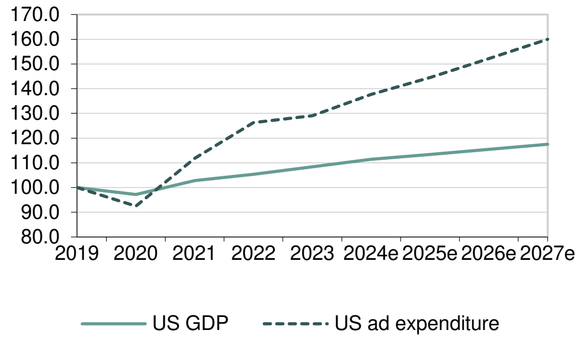
Source: World Bank, Dentsu

Exhibit 6: Global GDP versus global ad spend



Source: World Bank, Dentsu

Exhibit 7: US GDP growth versus US ad spend

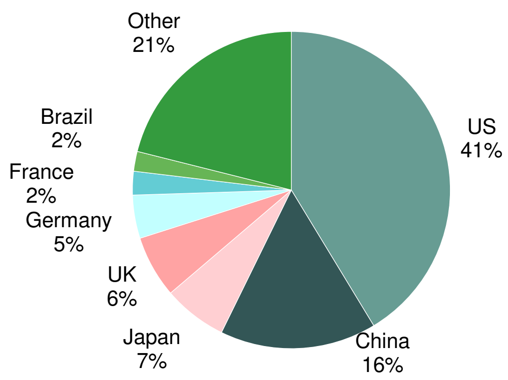


Source: World Bank, Dentsu

It is worth pointing out that the forecasts presented here predate the turmoil in the US markets and questions over the outlook for economic prospects for the country over this year and the following periods. With so much uncertainty, we would anticipate expectations for both GDP growth and ad spend to be revised downwards. Global ad spend will tend to underperform a downturn and outperform an upturn, and will more likely be a leading rather than a lagging indicator, with brands dialling down their marketing activities as they sense consumer confidence flagging.

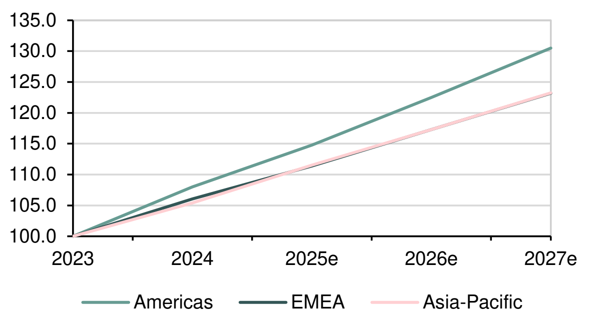
It can look like an obvious easy win for brands to cut their advertising spend during periods of economic downturn. However, numerous studies over the last century, some of which are mentioned here, demonstrate that those brands that continue to invest will pick up the most strongly and gain market share as conditions improve.

Exhibit 8: Largest ad markets, 2024



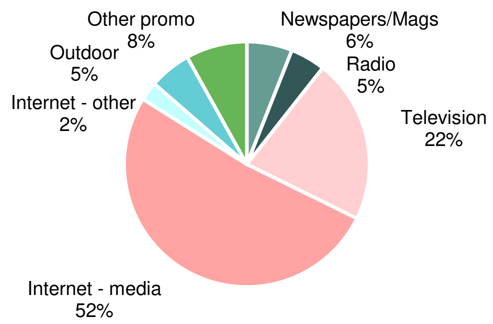
Source: Dentsu

Exhibit 9: Regional ad spend growth forecast



Source: Dentsu

Exhibit 10: Global ad spend by medium FY24

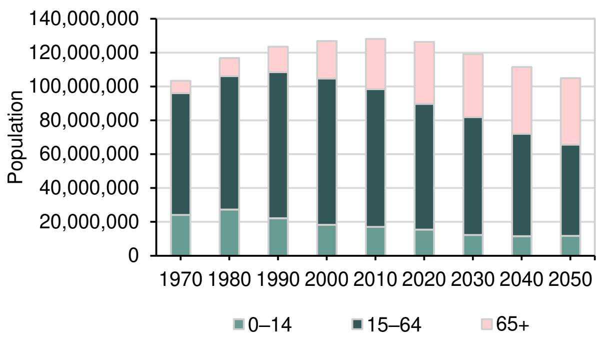


Source: Dentsu

The sheer scale of the US market in global terms means that being a global supplier necessitates having a major presence here. It is obviously also a highly sophisticated and competitive market, with strong incumbent players. The scale of opportunity has also attracted all the larger sector participants to address the Chinese market, usually on the back of non-Chinese brand owners looking to establish and/or expand their presence.

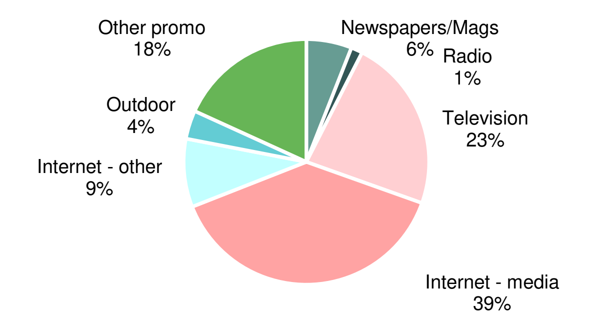
Japan remains the world's third-largest advertising market, with Dentsu reporting ad spend growth of 4.9% in FY24. It has relatively modest growth assumptions pencilled in for 3.8% in FY25, followed by 2.6% and 3.3% for the following two years. The Japanese ad market remains well behind the curve on digitisation and remains overweight to television, which is forecast to grow by 3.8% in FY25 before slowing to 2.6% in FY26 and staging a slight resurgence to 3.3% in FY27. The different dynamics are at least in part attributable to the country's demographics, with an older population favouring more traditional media, although the 'digital natives' will obviously be moving up the age range bands over time.

Exhibit 11: Japan: population by age cohort



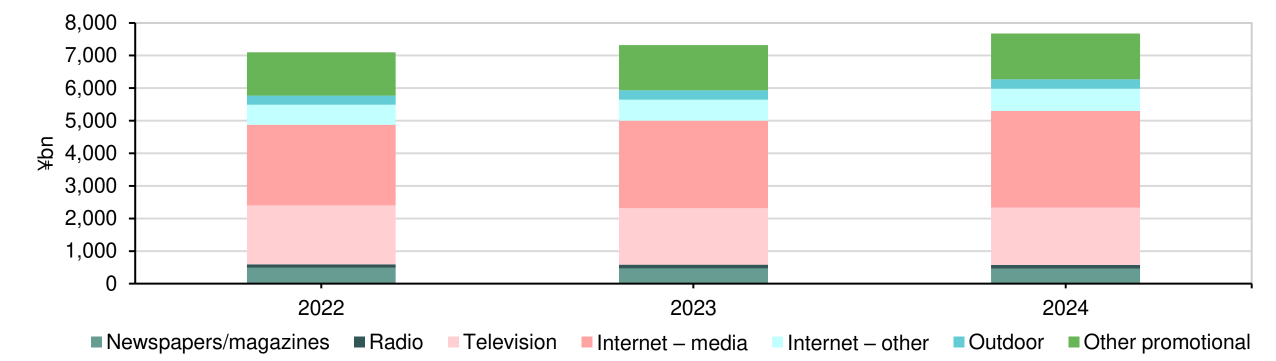
Source: World Bank

Exhibit 12: Japan ad spend by medium FY24



Source: Dentsu

Exhibit 13: Japanese advertising market by channel



Source: Dentsu

Large agency groups still dominate

The marketing services industry remains heavily influenced by the large global agency holding companies, listed below in Exhibit 16. Over recent years and as digital transformation has become a central theme, the traditional industry heavyweights have been joined by the large global consulting companies. In the more data-led, tech-driven space, key competitors would commonly include Accenture Song, Deloitte Digital and PWC. Of these, only Accenture makes partial disclosure of its marketing-based activities. WPP, Omnicom and the others (as listed below) are all keen to push their digital credentials and their progress on the implementation of data-driven AI models and services, both within their own business and increasingly as part of the client offering.

Sensitivities

- The key underlying sensitivity to the financial results is the health of the underlying economy, as demonstrated in Exhibit 5 above, which shows that global advertising spend tends to outperform the economy in upturns and underperform in downturns. Within this broad pattern there are other factors, such as major sporting events or political elections, that can have a substantive impact on advertising demand. Larger project work is more susceptible to delays and cancellations, and reductions in scope, when the backdrop is uncertain.
- Competition will always be a factor and clients review their relationships with their agencies as a matter of course. The shift in the nature of the work being carried out is leading to a wider peer set, with the major global

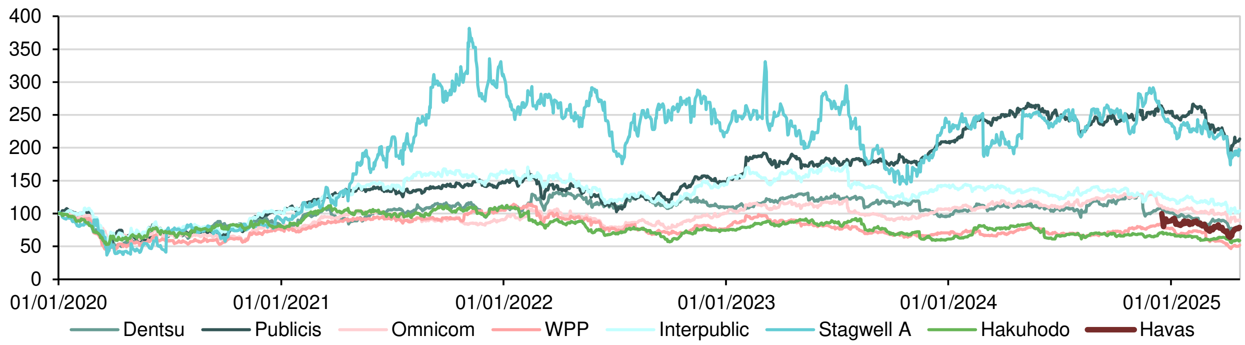
consultancies vying for the digital transformation business. In-housing by clients has been a feature of the market over recent years and may remain so. Close partnership relationships can mitigate this risk.

- Major brands reviewing and changing their media account partners can disrupt the flow of business, with multiple reviews often happening in the same reporting periods, followed by periods of relative calm. Client loss is another perennial issue, closely tied to the competitive landscape.
- The degree of exposure to different sectors of the economy can also have a substantive impact, and this has been the case over the last year with the major negative attitude shift by and towards the technology sector. Dentsu is more heavily weighted to this area than some of its peers, particularly within its US operations, which has been a constraint on financial performance in recent reporting periods but may ameliorate as the year progresses.
- AI is becoming an increasingly important element in optimising advertiser spend to reach the most appropriate audiences at the most appropriate time. With very large sums being spent by the major marketing service holding companies, technology companies and platforms and consultancy firms, changes to business practices are happening fast and there is no sure way of knowing how developments will play out at this stage.
- Currency: Dentsu's key exchange rate is the US dollar to Japanese yen although, with subsidiaries globally, other currencies are also relevant.
- The mid-term management plan involves possible major reconfigurations of the business. To deliver on management's top-line growth ambitions and margin improvement, the plan must be executed as envisaged.
- Reputational risks can occur because of internal issues, client problems or controversy. Historical issues have led to a cultural shift towards realising client goals in a broader context, alongside additional transparency, stricter compliance guidelines and enhanced training.
- Particular risks arise over the handling of data and its security. Regulatory risks are also relevant in this context.

Valuation

Over the last decade, there has been increasing differentiation between the largest global companies in the marketing services sector and their share prices no longer react in concert with the macroeconomic backdrop, despite the correlation shown above between GDP and spending on advertising.

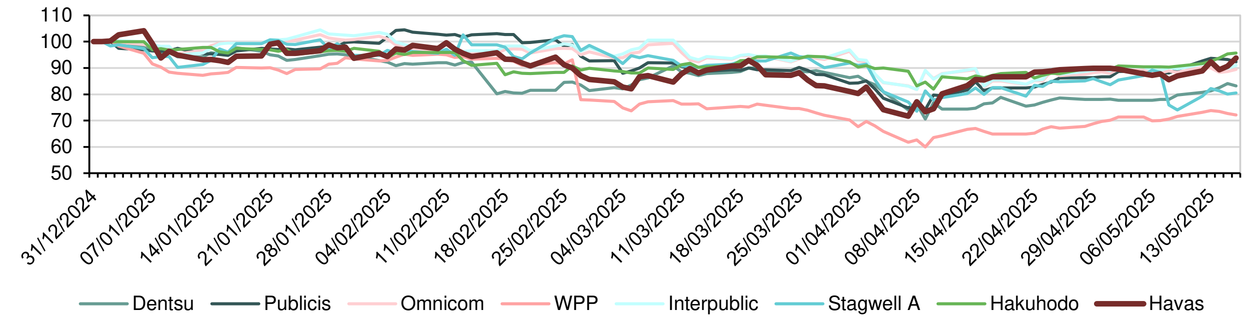
Exhibit 14: Share prices of leading peers, FY20 to date



Source: LSEG Data & Analytics. Note: Prices as at 19 May 2025

The best performers over this period have been Publicis and Stagwell. For the former, the technology strategy has been a major factor, built on the 2019 acquisition of Epsilon and the subsequent bringing together of client data, which has given a strong business proposition that has helped it outperform in the new business tables. Stagwell has espoused an aggressive acquisition-led growth strategy. There is then a fairly large performance gap between these and the other large marketing service companies. In the year to date, all these companies have seen pressure on their share prices, with WPP struggling the most.

Exhibit 15: Share prices of leading peers, year-to-date



Source: LSEG Data & Analytics. Note: Prices as at 19 May 2025

The resultant valuation metrics fall into a current year EV/EBITDA range of 3.9–8.1x, and for FY26 of 3.7–7.7x. If Dentsu were to be trading at the average over FY25–26 and across both EV/EBITDA and P/E, the share price would be ¥3,663, 16% ahead of the current level.

Dentsu is currently offering the highest yield available in the sector.

Our conclusion is that the market is currently pricing in the impact of the restructuring on the current year numbers, but not yet giving any recognition of the positive impact that the new plan should have on future years' earnings.

Exhibit 16: Peer valuations

	Price	Market cap	YTD	EV/revenue (x)	EV/EBITDA (x)			P/E (x)			Dividend yield
Company	(local CCY)	(US$m)	(%)	CY24	CY24	CY25	CY26	CY24	CY25	CY26	(%)
Publicis	95	27,275	(8)	1.8	8.4	8.1	7.7	15.7	12.5	11.9	3.5
Omnicom	77	15,020	(11)	1.2	7.3	7.2	6.9	11.5	9.2	8.7	3.3
WPP	593	8,621	(28)	0.7	4.9	5.5	5.4	16.8	7.4	7.3	4.8
Interpublic	25	9,420	(9)	1.0	N/A	6.9	6.4	15.4	9.7	9.1	4.7
Hakuhodo	1,125	3,034	(6)	0.4	5.6	5.3	5.1	36.9	18.6	16.7	3.0
Havas	2	1,700	(11)	0.7	4.0	3.9	3.7	9.5	7.1	6.6	0.0
Stagwell	5	1,430	(19)	1.1	7.8	7.4	6.4	N/A	6.4	5.6	0.0
Peer average			**(13)**	**1.0**	**6.3**	**6.3**	**5.9**	**17.6**	**10.1**	**9.4**	**2.7**
Dentsu	3,140	5,165	(18)	0.9	5.3	6.0	4.9	5.9	10.1	7.5	5.0
Premium/(discount)				***-9.5%***	***-17.2%***	***-4.4%***	***-16.9%***	***-66.5%***	***-0.8%***	***-20.6%***	***83.8%***

Source: LSEG Data & Analytics, Edison Investment Research. Note: Prices as at 19 May 2025.

It is also worth considering the valuation implied by a DCF. Here, we have used a base assumption of a 10% WACC and a terminal growth rate of 2.0%, and use the new mid-term management plan as guidance to the assumptions across FY25–27. This returns a considerably higher figure of ¥4,701, 48% above the current price.

Exhibit 17: DCF (¥/share) at varying WACC and terminal growth assumptions

		------------------Terminal growth rate------------------				
		0.0%	1.0%	2.0%	3.0%	4.0%
------------WACC------------	12.0%	3,155	3,327	3,534	3,786	4,101
	11.5%	3,350	3,545	3,780	4,071	4,439
	11.0%	3,563	3,784	4,054	4,392	4,826
	10.5%	3,796	4,049	4,360	4,755	5,271
	10.0%	4,053	4,343	**4,705**	5,170	5,791
	9.5%	4,338	4,672	5,095	5,649	6,404
	9.0%	4,654	5,042	5,542	6,207	7,139
	8.5%	5,008	5,462	6,056	6,866	8,036
	8.0%	5,406	5,942	6,656	7,657	9,157
	7.5%	5,858	6,496	7,366	8,622	10,596

Source: Edison Investment Research

Financials

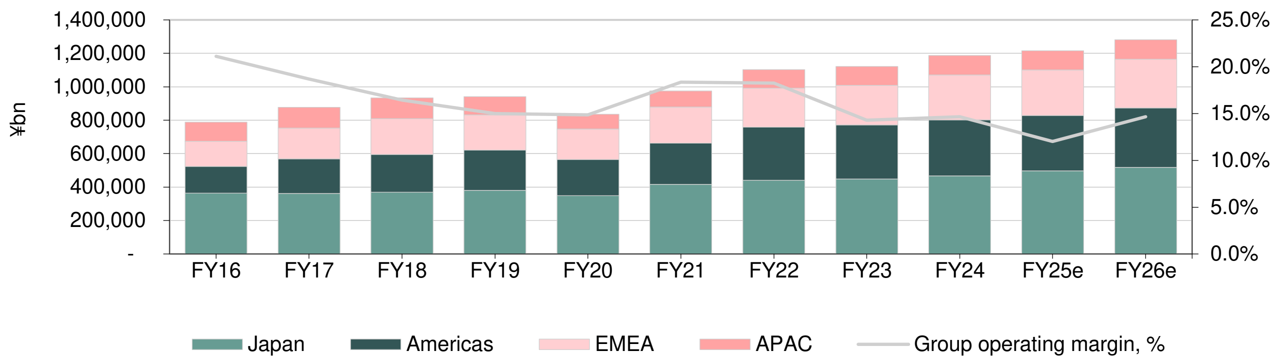
Dentsu has been built through a combination of organic and acquisition-led expansion, the most significant of these purchases being Aegis (2013), Merkle (2016, moving up to full ownership in 2020) and Tag (2023). As shown in the exhibit below, this has also been the impetus behind the diversification by geography, with a particular emphasis on growing in the important US market. The strategy has had a dilutive impact on margin, as is broadly inevitable when expanding the base of a business.

This long-term record also clearly shows the impact of COVID-19 on net revenue, as well as the relative speed of recovery as conditions normalised.

In the following Exhibit 19, we show the quarterly progression by geography over the past two years, which clearly shows the heavy skew (common to the sector) to the fourth quarter, with the accompanying bounce up in operating margin. This pattern can make it difficult to make confident predictions of the outturn for any particular financial year.

In common with other market participants, Dentsu has seen the impact of weaker market confidence on its larger transformation project work, with the scale of projects downgraded and continued delays to timescales — unsurprising given that the lack of confidence is persistent, discouraging companies from making the fundamental, structural changes to their ways of working while the payback is uncertain. This activity previously was encapsulated in the Customer Transformation & Technology or CT&T terminology, which also included services related to marketing technology, customer experience management, commerce, system integration, and transformation and growth strategy. This represented 28.3% of group FY24 net revenue and was targeted to grow to 50% of group net revenue under the previous management plan. The internal grouping has now been de-emphasised and the revenue split on this basis will no longer be disclosed. Under the new mid-term management plan, the emphasis has shifted to be more media-centric, connecting into other capabilities, such as marketing technology, data and analytics, and relevant consultancy.

Exhibit 18: Long-term net revenue and operating margin



Source: Company accounts, Edison Investment Research

We looked at the FY24 results in our February note, when we aligned our FY25 estimates with management's guidance and set out our expectations for FY26. We have only made small adjustments to our modelling at this juncture (primarily correcting an error on the FY25 dividend payment).

Q1 figures show good performance in Japan, weakness elsewhere

The overall tenor of the first quarter figures was in line with management's expectations for the full year. Japan performed better than had been anticipated, while the Americas and EMEA came in below. Organic net revenue growth was 0.2%, while the reported figure was a decline of 0.6%, reflecting the Russian business sold in July 2024. Underlying operating profit increased by 13.7% as tighter control of sales, general and administrative expenses tightened, reflected in an increase of 140bps in the underlying operating profit margin.

Net revenue in Japan was up 5.5% and the operating margin expanded from 27.6% to 29.0%. The top-line progress was driven by increased levels of business from existing clients, boosted with the first contributions from new business won in FY24. March tends to be the most important trading month of the year in Japan (as opposed to December across much of the rest of the world), which, in turn, will have boosted operating margin. With the increased investment in talent and technology, we would not expect this level of operating margin to be maintained across the year.

The Americas continue to represent a challenge and organic growth came in below internal expectations, with the CXM element continuing to be a particularly difficult market. Here, budgets from existing clients declined (again) and new projects continue to be delayed due to the uncertain macroeconomic circumstances. Management of the decline is a priority, with forensic analysis of the situation identifying the particular challenges to tackle. There is also new leadership in place, with a new technology officer, a new global head of CRM, a few senior sellers, and a new head of commerce and experience. We would anticipate starting to see an improvement in the later months of the year.

The Q125 results from EMEA also came in slightly behind management expectations, with CXM again cited as the main cause, with the overall impact affected by the higher weighting of CXM in the mix in the UK, the Netherlands and Denmark. For APAC, the results were slightly better than internal expectations, with an organic revenue decline of 4.6% and CXM the key element.

Exhibit 19: Quarterly progression of net revenue and underlying operating margin

¥bn	Q123	Q223	Q323	Q423	FY23	Q124	Q224	Q324	Q424	FY24	Q125
Net revenue											
Japan	120	101	107	122	449	123	102	110	132	467	130
Americas	73	77	83	89	322	81	87	81	86	335	76
EMEA	52	54	58	74	238	57	68	65	79	269	57
APAC ex-Japan	22	26	29	36	113	24	29	27	36	116	23
Eliminations	2	1	2	18	23	2	2	2	9	14	1
Group	**269**	**259**	**279**	**338**	**1,145**	**286**	**287**	**285**	**343**	**1,201**	**287**
Underlying operating profit											
Japan	34	15	24	31	103	34	15	23	42	114	38
Americas	13	15	21	24	73	13	21	17	24	75	14
EMEA	4	2	2	16	24	(1)	10	8	22	38	(2)
APAC ex-Japan	(2)	0	2	8	8	(3)	1	(2)	5	1	(3)
Eliminations	(11)	(10)	(12)	(12)	(43)	(13)	(13)	(12)	(15)	(53)	(12)
Group	**38**	**23**	**37**	**66**	**164**	**30**	**33**	**34**	**79**	**176**	**34**
Underlying operating margin											
Japan	28.2%	14.7%	22.5%	25.3%	23.0%	27.6%	14.9%	20.8%	32.0%	24.5%	29.0%
Americas	18.2%	19.7%	24.8%	27.0%	22.7%	16.3%	23.9%	21.2%	28.0%	22.5%	17.7%
EMEA	7.1%	3.7%	4.0%	21.9%	10.2%	-1.2%	14.2%	11.6%	27.8%	14.3%	-2.7%
APAC ex-Japan	-10.0%	1.5%	7.1%	21.4%	7.0%	-12.8%	2.0%	-6.8%	14.7%	0.9%	-14.0%
Group	**14.0%**	**8.9%**	**13.4%**	**19.6%**	**14.4%**	**10.4%**	**11.5%**	**12.0%**	**23.1%**	**14.7%**	**11.8%**

Source: Company accounts

FY25 prospects within mid-term management plan

It is worth a reminder at this point of the objectives of the new mid-term management plan. These are that by FY27, organic growth should be running at 4.0%, with an operating margin of 16–17% and operating cash flow of ¥140bn. The guided return on equity is in the mid-teens.

Our modelling for the current year is based on the management guidance issued with the FY24 results, which were reiterated with the Q125 figures (Dentsu generally publishes fairly detailed current year forecasts with revenue, net revenue, underlying operating and net profit, underlying basic EPS and dividend, operating profit and net profit, as well as the key exchange rates at which that guidance has been drawn up). It is worth noting that the US$ to ¥ exchange rate is 7.7% below the level at the start of the year. The mechanistic impact if this shift was applied to the FY24 figures would be a reduction to net revenue of ¥26bn. The impact on underlying group operating margin would be less marked, due to the natural hedging effect of a cost base in the same currency.

For FY26, we have assumed a stronger rebound in net revenue growth against the suppressed comparative periods: 4.2% for the Japanese business and 6.4% for international as the growth strategy achieves greater traction, giving a blended growth rate of 5.5%.

In this context, an organic growth target of 4.0% for FY27 looks achievable against normalised market trading conditions. On the operating margin aspect, the current year figures reflect the ¥50bn one-off investment being made to 'rebuild the foundations', bringing the margin back in to 12.0% from the 14.8% logged in FY24.

The internal investment planned over the three years to build up operations in key markets and activities is for a total of ¥45bn, with the spread over the timescale as yet unclear (we have simply spread equally over FY25–27).

Transactions support cash flow, with returns to shareholders

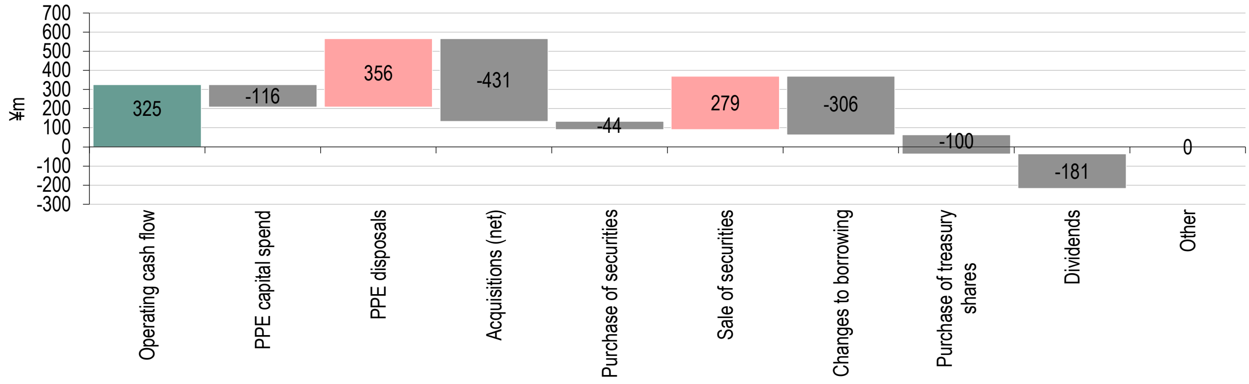
While the short-term cash flow is subject to various vacillations, it is more meaningful to show how the balance sheet has been transformed over recent years through the generation and use of cash. To illustrate this more clearly, we have combined the cash flow statements from the years FY19–24 inclusive, as shown below.

By doing this, the scale of the transformation and the key elements become more obvious. The main factors to note are:

- Property disposals: the largest element by far was the sale and leaseback of the Shiodome building in Tokyo in September 2021. The building, which is a major landmark, had a book value of ¥177bn and a gain of approximately ¥89bn (¥56bn net) was realised (the actual sale price was not disclosed).

- Sale of securities: historically, it has been common practice in Japan for companies to hold equity positions in other companies with which they have a commercial relationship. This has not sat comfortably with Western notions of corporate governance. The largest contributor to this cash inflow was the sale of shares in Recruit Holdings in the period up to December 2020, with total receipts of ¥194bn. The remaining stake in Recruit Holdings was sold in Q125 for ¥15bn (not included in Exhibit 20 below, as it falls into the current financial year). This unwinding process is now effectively completed.

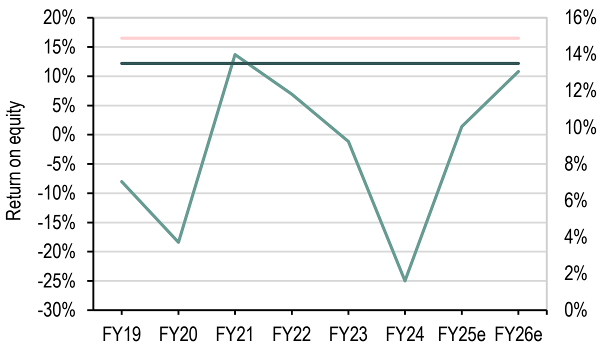
Exhibit 20: Five-year cumulative cash utilisation (FY20–24)



Source: Company accounts, Edison Investment Research

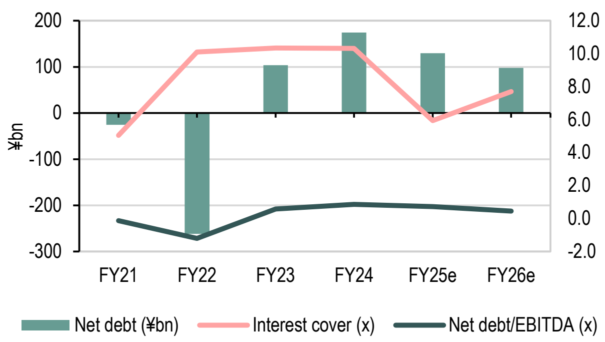
- The largest use of funds over the period has been acquisitions (the figure shown in the exhibit above includes sums raised and spent on subsidiary company holdings). Full ownership of Merkle was brought forward from the original plan to April 2020, although payment was not made until the previously agreed date in Q321. In FY23, Dentsu bought Tag Group, a global company based out of London, for £533m (¥89.0bn), to bolster the group's content production and personalisation capabilities. Future M&A is not ruled out, but will be more selective, stricter on pricing and geared towards the group's stated goals.
- Share buybacks: there have been a number of share buyback programmes over the years, with ¥30bn bought in FY19, ¥30bn in FY21, ¥40bn in FY22 and ¥20bn in FY24, with this being the preferred route for return of capital for some group shareholders. There is no mention of further share buybacks in management's capital allocation policy in the new mid-term plan.
- Dividends: other shareholders prefer to receive dividends. As part of the previous plan, management outlined a progressive increase in the payout ratio, with a medium-term target of 35%, reaching this level in FY23. For FY24, the payout ratio dipped back to 30% on a maintained dividend and is set to rebound to 51% on the reduced expected earnings in the current year, with management again guiding to a payout for the year of ¥139.5. The basic rule is for a 35% payout ratio with at least a stable dividend for the duration of the new plan.

Exhibit 21: RoE over time, including forecasts and target



Source: Company accounts, Edison Investment Research

Exhibit 22: Net debt, interest cover, net debt/EBITDA



Source: Company accounts, Edison Investment Research

New goal of return on equity

Return on equity was not previously an external KPI, although was monitored internally. This new management plan acknowledges the need for better alignment of goals with shareholders and has set a target of mid-teens return on equity in FY27, which is represented by the horizontal bands in Exhibit 21, above. As can be seen, we would envisage good progress towards this aim from the low point in FY24.

Improving financial position, asset write-down

On the basis of our modelling, net debt will have peaked in FY24. Interest cover is set to be lower in the current year due to the suppressed level of EBITDA as the restructuring goes through. As described in our earlier note, with the FY24 results, Dentsu recognised a goodwill impairment of ¥210.1bn, split ¥153.0bn against EMEA assets and ¥57.1bn in the Americas. A ¥67.8bn write-down on Asia-Pacific assets was taken at the end of FY23. The reasoning cited is a higher discount rate being used in the calculations in light of the continuing environment of high interest rates, alongside a re-evaluation of operational risks in the respective markets. This pushed the group into a reported loss for the 2024 financial year.

It does, though, refresh the balance sheet ahead of the implementation of the new mid-term management plan.

Exhibit 23: Financial summary

¥'m	2022	2023	2024	2025e	2026e
Year end 31 December	IFRS	IFRS	IFRS	IFRS	IFRS
INCOME STATEMENT					
Revenue	1,246,401	1,304,552	1,410,961	1,501,727	1,542,951
Cost of Sales	(126,882)	(159,733)	(209,314)	(286,727)	(261,181)
Net revenue	**1,119,519**	**1,144,819**	**1,201,647**	**1,215,000**	**1,281,771**
EBITDA	217,519	178,127	204,006	177,643	217,624
Operating profit (before amortisation and exceptionals)	204,319	163,515	176,233	146,000	187,783
Amortisation of acquired intangibles	(28,721)	(30,691)	(29,335)	(29,335)	(29,335)
Exceptionals	(56,849)	(87,840)	(529,592)	(2)	(1)
Share-based payments	0	(500)	0	0	0
Reported operating profit	118,747	45,312	(124,992)	116,667	158,449
Net Interest	(20,246)	(15,810)	(17,073)	(24,613)	(24,360)
Joint ventures & associates (post tax)	(1,932)	3,400	3,009	3,053	3,098
Exceptionals	5,467	526	(2)	0	0
Profit Before Tax (normalised)	187,608	151,631	162,167	124,440	166,521
Profit Before Tax (reported)	102,038	33,103	(139,058)	95,107	137,187
Reported tax	(34,982)	(38,572)	(43,605)	(34,238)	(49,387)
Profit After Tax (normalised)	139,949	95,309	93,622	79,642	106,573
Profit After Tax (reported)	67,055	(5,469)	(182,663)	60,868	87,800
Minority interests	(6,077)	(5,245)	(8,808)	(8,192)	(8,192)
Net income (normalised)	130,854	89,840	92,936	71,450	96,993
Net income (reported)	60,977	(10,714)	(191,486)	52,676	79,608
Average Number of Shares Outstanding (m)	268.0	264.4	261.6	261.6	261.6
EPS - normalised (¥)	488.3	339.8	355.2	275.2	370.7
EPS - normalised FD (¥)	485.3	337.7	355.2	275.2	370.7
EPS - basic reported (¥)	227.5	(40.5)	(734.6)	40.3	335.6
Dividend (¥)	155.3	139.5	139.5	139.5	139.5
Net revenue growth (%)	16.9	2.3	5.0	1.1	5.5
EBITDA margin to revenue less pass-through costs (%)	19.4	15.6	17.0	14.6	17.0
Normalised op. margin to revenue less pass-through costs (%)	18.3	14.3	14.7	12.0	14.7
BALANCE SHEET					
Fixed Assets	1,281,646	1,494,840	1,329,901	1,279,860	1,121,546
Intangible Assets	962,100	1,069,854	900,744	865,703	832,465
Tangible Assets	26,577	29,430	26,159	26,159	29,431
Investments & other	292,969	395,556	402,998	387,998	259,650
Current Assets	2,270,531	2,139,556	2,177,355	2,345,579	2,577,061
Stocks	3,670	6,396	6,095	8,349	7,605
Debtors	1,531,957	1,524,289	1,678,146	1,786,099	2,029,087
Cash & cash equivalents	603,740	390,678	371,989	430,009	455,876
Other	131,164	218,193	121,126	121,122	84,493
Current Liabilities	(2,017,695)	(1,939,910)	(2,067,395)	(2,168,197)	(2,389,827)
Creditors	(1,532,591)	(1,527,612)	(1,566,979)	(1,667,781)	(1,859,996)
Tax and social security	(30,894)	(28,088)	(27,172)	(27,172)	(27,172)
Short-term borrowings	(95,790)	(39,213)	(173,646)	(173,646)	(173,646)
Other	(358,420)	(344,997)	(299,598)	(299,598)	(329,013)
Long-term liabilities	(768,403)	(781,735)	(670,828)	(665,211)	(659,594)
Long-term borrowings	(245,961)	(455,232)	(373,627)	(368,010)	(362,393)
Other long-term liabilities	(522,442)	(326,503)	(297,201)	(297,201)	(297,201)
Net Assets	766,079	912,751	769,033	792,030	649,186
Minority interests	(75,060)	(71,104)	(72,197)	(80,389)	(88,581)
Shareholders' equity	691,019	841,647	696,836	711,641	560,605
CASH FLOW					
Operating Cash Flow	176,208	111,822	(57,609)	185,422	225,699
Working capital	(3,519)	(60,338)	(114,899)	(9,405)	(50,029)
Exceptional & other	40,156	85,937	513,473	3,167	2,870
Tax	(115,764)	(47,301)	(25,651)	(34,238)	(49,387)
Net operating cash flow	97,081	90,120	315,314	144,945	129,153
Capex	(4,585)	(27,623)	(25,564)	(25,684)	(25,683)
Acquisitions/disposals	(40,873)	(136,544)	(22,343)	4,238	(10,762)
Net interest	(18,301)	(20,583)	(22,088)	(24,613)	(24,360)
Equity financing	(40,006)	(4)	(20,006)	0	0
Net dividends	(37,895)	(42,009)	(35,847)	(34,880)	(36,494)
Other	(24,920)	(27,786)	(16,500)	(349)	15,802
Net cash flow	(69,499)	(164,429)	172,966	63,657	47,655
Opening net debt/(cash)	(144,352)	(262,008)	103,748	174,579	110,942
FX	13,932	11,117	17,114	0	0
Other non-cash movements	173,223	(212,444)	(260,911)	(20)	(16,189)
Closing net debt/(cash)	(262,008)	103,748	174,579	110,942	79,476

Source: Company accounts, Edison Investment Research. Note: historic figures include contribution from Russia, disposed July 24

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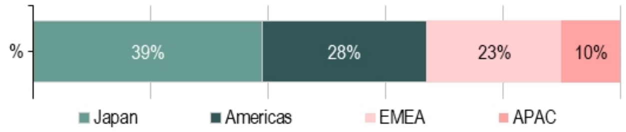
Revenue by geography



Note: Revenue split is for FY24 net revenue.

Management team

Representative executive officer, president and global CEO: Hiroshi Igarashi

Mr Igarashi joined Dentsu in 1984 in account management, handling clients across a wide range of sectors, with a particular focus on business development and on the creation of solutions with roots in social issues and sports. He became an executive officer of Dentsu in 2017, adding the role of head of Japanese business in 2018. On the transition to a holding company structure in January 2020, he assumed the roles of group co-COO, Dentsu Japan network president & CEO and Dentsu Inc representative director, president & CEO. This latter role includes shaping the group's long-term vision and corporate strategy. He is also president of the Japan Advertising Agencies Association.

Representative executive officer, executive vice president, global chief governance officer: Arinobu Soga

Mr Soga joined Dentsu in 1988, later becoming CFO and then CEO of Geneon Entertainment USA, a Dentsu business. He continued to build his career in Japan and abroad, and was appointed as CFO and director of Dentsu Group Inc in 2020. In his role as chief governance officer since 2023, he works closely with the wider management team to ensure the highest levels of corporate governance across the policies, structures and processes of the organisation.

Executive officer, executive vice president, global COO, dentsu and chairman and acting CEO, dentsu Americas: Giulio Malegori

Mr Malegori joined Dentsu in 2010 as president and CEO of Italy, later extending responsibility to Southern Europe. He was appointed EMEA CEO in 2017 and global COO in 2023. He started his career at McCann Erickson before moving to ACNielsen. In 1989, he founded an independent media agency, later part of CIA Medianetwork, and in 1999 he was founding-CEO of Mindshare in Italy (part of WPP), becoming CEO of Mindshare EMEA and joining the global executive team in 2003.

Executive officer, global CFO, dentsu: Shigeki Endo

Mr Endo joined Dentsu in July 2024 as global CFO designate. He has over 30 years of experience and is an established global finance leader. He began his career at ITOCHU Corporation. After working for the company in New York, he joined General Electric in 2000, where he worked in internal audit, M&A integration and process improvement in the US, Europe and Asia. In 2011, he joined BAT, where he worked in the London then as head of finance in Japan and South-East Asia, working in Cambodia and Sri Lanka. He joined Accenture in 2018, and was appointed MD and Japan CFO.

Principal shareholders	%
The Master Trust Bank of Japan (Trust accounts)	12.78
Kyodo News	7.29
Northern Trust Co (AVFC) re Silchester International Investors International	4.20
Value Equity Trust	3.47
Jiji Press	3.01
Custody Bank of Japan (Trust accounts)	

Note: Principal shareholders as at 31 March 2025

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