

# ***THE EYESHADE REPORT***

**January 16, 2002**

<u>Company:</u> <b>THE INTERPUBLIC GROUP OF COMPANIES, INC.</b>	<u>Address and Phone:</u> 1271 Avenue of the Americas New York, New York 10020 (212) 399-8000
Ticker: IPG	Shares Out (basic): 377.6 M
Exchange: NYSE	Float: 317.2 M
Market Cap: \$ 10.2 B	Short Interest: 11,684,758
P/S: 1.5	Closing Price: (1/16/02): \$ 27.10
P/E: NE	52 Week Range: \$ 18.25 - \$ 47.43

*Description of Business: The Interpublic Group of Companies, Inc. (the "Company" or "IPG") is a worldwide provider of advertising agency and related services.*

## **Summary of Comments and Concerns**

- Decline in revenue.
- Decline in operating margin.
- Net income enhanced by reversal of severance reserve.
- Increase in total net debt.
- Decline in operating income/total net debt.
- Increase in interest expense.
- Decline in cash flow from operations.
- Cash flow from operations insufficient to pay dividend.
- Decline in working capital.
- FY 2000 reported EPS below 1998 when cost of stock options included.
- Auditor's "other" fees more than double audit fees.

The Eyeshade Report is published by Forensic Advisors, Inc., P.O. Box 10074, Rockville, MD 20849-0074 U.S.A. © 2001 by Forensic Advisors, Inc. ALL RIGHTS RESERVED. On the web at: [www.forensicadvisors.com](http://www.forensicadvisors.com). All information contained herein is solely the opinion of Forensic Advisors, Inc. and is obtained by it from sources believed by it to be accurate and reliable. However, such information is presented "as is," without warranty of any kind, express or implied. All content and opinions herein are subject to change at any time without notice. Nothing herein is or should be relied upon or construed to be a recommendation for the purchase, retention, sale or short-sale of the securities of the company mentioned. You may not reproduce, retransmit, distribute, disseminate, sell, publish, broadcast, or circulate all or any portion of this report without the express written consent of Forensic Advisors, Inc.

## Financial Statement Review

**Decline in revenue** – For the nine months ended September 30, 2001, reported revenue declined 2.5% from the same period one year ago.

(\$ - in millions)	9 months to 9/30/00	9 months to 9/30/01	% change
<b>Revenue</b>	5,140.8	5,007.3	(2.5%)

For the quarter ended September 30, 2001 (Q3 01), reported revenue declined 7% from the year ago period.

(\$ - in millions)	3 months to 9/30/00	3 months to 9/30/01	% change
<b>Revenue</b>	1,734.2	1,605.7	(7%)

The Company stated that “organic revenue” (i.e., exclusive of acquisitions and currency effects), decline by 9% for the quarter ended September 30, 2001 compared to the year ago period.<sup>1</sup>

The Company also stated that it expected its revenue to continue to decline in the fourth quarter: “Despite significant new business already won in the fourth quarter, the Company believes that clients will remain cautious. As a result, revenue is expected to decline in the fourth quarter from its year-earlier level.”<sup>2</sup>

**Decline in operating margins** – For the quarter ended September 30, 2001 (Q3 01), the Company’s operating margin (excluding nonrecurring items<sup>3</sup>) declined to 8.7% from 12.6% in the year ago period.

(\$ - in millions)	3 months to 9/30/00	3 months to 9/30/01	% change
<b>Revenue</b>	1,734.2	1,605.7	(7%)
<b>Op. Inc.*</b>	218.2 <sup>4</sup>	139.3 <sup>5</sup>	(36%)
<b>Op. Margin</b>	12.58%	8.67%	(31%)

\* The reported operating income was \$191.5 million for the quarter ended 9/30/00 and (\$570.6 million) for the quarter ended 9/30/01. The numbers in the table above exclude nonrecurring items.

<sup>1</sup> . IPG, 10-Q (9/30/01), Notes, Item 2, Results of Operations. The Company further stated that exclusive of the loss of the Chrysler account by Foote, Cone & Belding in November 2000 and the “estimated business disruptions following the events of September 11, 2001,” organic revenue was down 4.4% in the quarter ended 9/30/01 from 9/30/00.

<sup>2</sup> . IPG, 10-Q (9/30/01), Notes, Item 2, “Outlook.” IPG had Q4 00 revenue of \$1.7 billion. True North Communications, Inc. (which IPG acquired in a pooling acquisition on 6/22/01 for 59 million shares valued at approx. \$1.6 billion) had Q4 00 revenue of \$441 million.

<sup>3</sup> . IPG, 10-Q (9/30/01), Notes, Item 2, Results of Operations.

<sup>4</sup> . As defined by the Company, IPG, 10-Q (9/30/01), Notes, Item 2, Results of Operations.

<sup>5</sup> . Id.

**Net income enhanced by reversal of severance reserve** – For the quarter ended September 30, 2001 (Q3 01), reported net income was enhanced by \$50 million pre-tax (\$36 million after tax) reversal of severance reserves.

**Reported Net Income**

(in millions)	Q3 00	Q3 01	% change
<b>Net Income</b>	90.8	(477.5)	NM

**Net Income excluding reversal of severance reserve**

(in millions)	Q3 00	Q3 01	% change
<b>Net Income</b>	90.8	(513.5)	NM

The Company has embarked on some “operational initiatives” to reduce expenses through a restructuring plan that includes severance, lease terminations and other actions. The total amount of charges incurred in connection with the plan is \$645.6 million (\$446.5 million, net of tax).<sup>6</sup> We would advise investors to pay attention to future financial statements for any further “reversals” of those reserves.

The Company also stated that after removal of all non-recurring items (including the reversal of severance reserves discussed above), net income declined 49% for the quarter ended September 30, 2001 compared to the year ago period.<sup>7</sup>

**Net Income excluding non-recurring items**

(in millions)	Q3 00	Q3 01	% change
<b>Net Income</b>	107.7	54.5	(49%)

**Increase in total net debt** – For the period ended September 30, 2001, the Company’s total net debt (defined as long-term debt plus convertible subordinated notes plus short term debt<sup>8</sup> minus cash, equivalents and marketable securities) increased to \$2.4 billion from \$1.5 billion in the year ago period.

(\$ - in millions)	9/30/00	9/30/01	% change
<b>LT Debt</b>	1,128.2	1,356.3	20%
<b>Convt. Notes</b>	529.4	544.6	3%
<b>ST Debt</b>	445.7	1,225	175%
<b>Cash</b>	(626.2)	(685.6)	9%
<b>Total Net Debt</b>	1,477.1	2,440.3	65%

<sup>6</sup> . This amount exceeded the original estimate, made in July 2001, of \$500 million, due to the deterioration in revenue that caused the need for greater headcount reductions and office closings. IPG, 10-Q (9/30/01), Notes, Item 2, Non-recurring Items (i).

<sup>7</sup> . IPG, 10-Q (9/30/01), Notes, Item 2.

<sup>8</sup> . Designated “Payable to banks” on the Company’s balance sheet.

**Decline in operating income/total net debt** – For the nine months ended September 30, 2001, the Company’s operating income (excluding nonrecurring items as defined by the Company) as a percentage of total net debt (“TND”) declined to 22% from 47.5% in the year ago period.

(\$ - in millions)	9 mos. to 9/30/00	9 mos. to 9/30/01	% change
<b>Op. Inc. (“OI”)*</b>	701.3 <sup>9</sup>	540.5 <sup>10</sup>	(23%)
<b>Total Net Debt</b>	1,477.1	2,440.3	65%
<b>OI/TND</b>	47.5%	22%	(54%)

\* The reported operating income was \$585.8 million for the nine months ended 9/30/00 and (\$444.6 million) for the nine months ended 9/30/01. The numbers in the table above exclude nonrecurring items.

**Increase in interest expenses** – As would be expected from the increase in debt, the Company’s interest expense for the 9 months ended September 30, 2001 increased to \$125.8 million from \$87 million in the same period a year ago.

(\$ - in millions)	9 mos. to 9/30/00	9 mos. to 9/30/01	% change
<b>Revenue</b>	1,734.2	1,605.7	(7%)
<b>Interest Expense</b>	87	125.8	45%

**Decline in cash flow from operations** – For the nine months ended September 30, 2001, the Company reported a year-over-year decline in cash flow from operations (“CFFO”).

(\$ - in millions)	9 mos. to 9/30/00	9 mos. to 9/30/01	% change
<b>Net Income (“NI”)</b>	307.1	(616.3)	NM
<b>CFFO</b>	(80.4)	(517.5)	(544%)
<b>CFFO – NI</b>	(387.5)	98.8	NM

We note, however, that the “CFFO-NI” figure improved compared to the 9 months ended September 30, 2000.

<sup>9</sup>. As defined by the Company, IPG, 10-Q (9/30/01), Notes, Item 2, Results of Operations.

<sup>10</sup>. Id.

**Cash flow from operations insufficient to pay dividend** – As would be expected with negative cash flow from operations, the Company’s CFFO is insufficient to pay its current dividend

(\$ - in millions)	9 mos. to 9/30/00	9 mos. to 9/30/01	% change
<b>CFFO</b>	(80.4)	(517.5)	(544%)
<b>Dividends (“Div.”)</b>	(114.2)	(109.8)	4%
<b>CFFO-Div.</b>	(194.6)	(627.3)	(222%)

**Decline in working capital** – As of September 30, 2001, the Company’s working capital (current assets minus current liabilities) declined to negative \$550.5 million from negative \$326 million as of December 31, 2000.

The Company stated that part of the reason for the decline in working capital was the Company’s obligation to purchase shares of its own stock (2.4 million for the first nine months of 2001) to fulfill its obligations under various compensation plans (*i.e.*, stock option and restricted stock awards to employees).<sup>11</sup> Although the Company has ceased its share repurchase program effective July 2001 as it has sufficient shares to meet its 2001 obligations, this is an example of the fact that stock option awards to employees, though not recorded as an expense on the income statement, really are a cost to a company.

**FY 2000 reported EPS below 1998 when cost of stock options included** - The most recent data available for the effect on stock options on net income (“NI”) and earnings per share (“EPS”) is the fiscal year ended December 31, 2000. That information indicates that had the Company determined compensation cost based on the fair value at the grant date for its stock options consistent with the methodology prescribed in SFAS No. 123, net income and EPS would have been approximately 8.5% lower.

While nowhere near as large a decline as some other companies featured in our reports (*e.g.*, ResMed, Inc. (RMD) and Syncor International (SCOR)), it does show that FY 2000 EPS actually fell below FY 1998 levels when the cost of stock options are included. (Reported FY 2000 EPS was above FY 1998). It also reflects an actual “cost” to the Company as it repurchases shares in the open market to offset the dilution caused by the issuance of stock options as described in the previous section of this report.

(\$ - in 000’s)	FY 98	FY 99	FY 00
<b>Reported NI</b>	339,907	331,287	358,658
<b>NI minus stock option expense</b>	322,084	303,645	327,880
<b>% change</b>	(5%)	(8%)	(8.5%)

<sup>11</sup> . IPG, 10-Q (9/30/01), Notes, Liquidity and Capital Resources.

	<b>FY 98</b>	<b>FY 99</b>	<b>FY 00</b>
<b>Reported basic EPS</b>	\$1.15	\$1.11	\$1.18
<b>Basic EPS minus stock option expense</b>	\$1.09	\$1.02	\$1.08
<b>% change</b>	(5%)	(8%)	(8.5%)

	<b>FY 98</b>	<b>FY 99</b>	<b>FY 00</b>
<b>Reported diluted EPS</b>	\$1.12	\$1.07	\$1.15
<b>Diluted EPS minus stock option expense</b>	\$1.06	\$0.99	\$1.05
<b>% change</b>	(5%)	(7%)	(9%)

**Auditor’s “other” fees more than double audit fees** – For the year ended December 30, 2000, the Company’s auditors, PricewaterhouseCoopers (“PwC”), charged IPG \$4.6 million for audit fees and \$9.3 million for “other fees” for a total of \$13.9 million in fees. We did not locate any details regarding the nature of the “other” services provided to the Company.

**Fiscal Year 2000 Auditor Fees**

<b>Auditor</b>	<b>Audit Fees</b>	<b>“Other” Fees</b>	<b>Total Fees</b>
PwC	\$4,600,000	\$9,300,000	\$13,900,000

## Stock Chart



Chart courtesy of StockCharts.com (<http://stockcharts.com>).

### 12 Month Short Interest Data\*

Settlement Date	Short Interest	Ave. Dly. Vol.	Days to Cover
Dec. 14, 2001	11,684,758	2,740,250	4.26
Nov. 15, 2001	8,320,819	1,629,939	5.10
Oct. 15, 2001	8,074,649	2,953,082	2.73
Sep. 14, 2001	6,930,995	1,255,390	5.52
Aug. 15, 2001	6,724,375	1,932,935	3.48
Jul. 13, 2001	8,719,421	3,110,767	2.80
Jun. 15, 2001	15,835,058	1,417,182	11.17
May 15, 2001	13,029,475	2,021,991	6.44
Apr. 12, 2001	10,075,769	1,953,365	5.16
Mar. 15, 2001	5,998,083	1,535,711	3.91
Feb. 15, 2001	6,012,520	1,291,600	4.66
Jan. 12, 2001	6,099,007	1,159,856	5.26

\* Source: NASDAQ® website: [www.nasdaq.com](http://www.nasdaq.com). © Copyright 2002, The Nasdaq Stock Market, Inc. All Rights Reserved. Neither The Eyeshade Report nor Forensic Advisors, Inc. is associated with or sponsored by Nasdaq.

###