

Case example

Game-changing forces and the global advertising industry

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This case is centred on the global advertising industry which faces significant strategic game-changing forces driven by technological innovation, the rise of consumer spending in developing economies, changes in consumer media consumption and pressures from major advertisers for results-based compensation.

In the second decade of the new millennium, advertising agencies faced a number of unanticipated challenges. Traditional markets and industry operating methods, developed largely in North America and Western Europe following the rise of consumer spending power in the twentieth century, were being radically reappraised.



Source: PixieMe/Shutterstock

The industry was subject to game-changing forces from the so-called 'digital revolution' with the entry of search companies like Google, Facebook and Amazon as rivals for advertising budgets on mobile devices. Changing patterns in global consumer markets impacted on both industry dynamics and structure. Budgets being spent through traditional advertising agencies were being squeezed as industry rivalry intensified with the entry of specialist consultancies.

Overview

Traditionally, the business objective of advertising agencies is to target a specific audience on behalf of clients with a message that encourages them to try a product or service and ultimately purchase it. This is done largely

through the concept of a brand being communicated via media channels. Brands allow consumers to differentiate between products and services and it is the job of the advertising agency to position the brand so that it is associated with functions and attributes which are valued by target consumers. These brands may be consumer brands (e.g. Procter & Gamble, Samsung, Nestle) or business-to-business (B2B) brands (e.g. IBM, Airbus Industrie and UPS). Some brands target both consumers and businesses (e.g. Microsoft and Apple).

As well as private-sector brand companies, governments spend heavily to advertise public-sector services such as healthcare and education or to influence individual behaviour (such as 'Don't drink and drive'). For example, the UK government had an advertising budget of £300m (€335m) in the late-2010s. Charities, political groups, religious groups and other not-for-profit organisations also use the advertising industry to attract funds into their organisation or to raise awareness of issues. Together these account for approximately 3 per cent of advertising spend.

Advertisements are usually placed in selected media (TV, press, radio, mobile and desktop internet, etc.) by an advertising agency acting on behalf of the client brand company; thus they are acting as 'agents'. The client company employs the advertising agency to use its knowledge, skills, creativity and experience to create advertising and marketing to drive consumption of the client's brands. Clients traditionally have been charged according to the time spent on creating the advertisements plus a commission based on the media and services bought on behalf of clients. However, in recent years, larger advertisers such as Coca-Cola, Procter & Gamble and Unilever have been moving away from this compensation model to a 'value' or results-based model based on a number of metrics, including growth in sales and market share.

Ad industry growth

Money spent on advertising has increased dramatically over the past two decades and in 2018 was over \$205 billion (€176bn, £158bn) in the USA and \$583 billion worldwide. While there might be a decline in recessionary years, it is predicted that spending on advertising will exceed \$787 billion globally by 2022.

The industry is shifting its focus as emerging markets drive revenues from geographic sectors that would not

Table 1 Global advertising expenditure by region (US\$ million, at 2017 average rates)

	2014	2015	2016	2017	2018 (estimate)
N America	169,277	175,024	183,075	191,130	196,099
W Europe	111,300	114,712	119,531	124,790	128,035
Asia Pacific	122,000	130,711	137,639	145,695	149,483
C & E Europe	32,284	35,514	36,691	37,305	38,275
Latin America	34,082	36,836	38,530	39,226	42,315
Africa/ME/ROW	25,941	28,044	29,334	28,608	29,352
World	494,884	520,841	544,800	566,754	583,599

Source: ZenithMedia, Statista, December 2018.

have been significant 5 to 10 years ago, such as the BRICS countries and the Middle East and North Africa. This shift has seen the emergence of agencies specialising in Islamic marketing, characterised by a strong ethical responsibility to consumers. Future trends indicate the strong emergence of consumer brands in areas of the world where sophisticated consumers with brand awareness are currently in the minority (see Table 1).

In terms of industry sectors, three of the top 10 global advertisers are car manufacturers. However, the two major fmcg (fast-moving consumer goods) producers Procter & Gamble and Nestlé are in the three top spots for global advertising spend. Healthcare and beauty (L'Oréal), consumer electronics (Samsung), fast food, beverage and confectionery manufacturers are all featured in the top 20 global advertisers. The top 100 advertisers account

for nearly 50 per cent of the measured global advertising economy.

Despite the increase in worldwide advertising revenues, the holding companies that own the world's largest advertising groups: WPP, Publicis, Omnicom and Interpublic Group (see Table 2) are under intense pressure in a changing business environment to deliver shareholder value.

Intensifying competition

Advertising agencies come in all sizes and include everything from one- or two-person 'boutique' operations (which rely mostly on freelance outsourced talent to perform most functions), small- to medium-sized agencies, large independents to multinational, multi-agency conglomerates employing over 200,000 people. The

Table 2 Top five multi-agency conglomerates: 2017, by revenue, profit before interest and tax, number of employees and agency brands

Group name	Revenue	PBIT	Employees	Advertising agency brands
1. WPP (UK)	£15.2bn	£2.16bn	200,000	GroupM, JWT, Grey, Ogilvy, Y&R
2. Omnicom (US)	\$15.4bn	\$2.059bn	76,000	BBDO, DDB, TBWA
3. Publicis Groupe (France)	€10.8bn	€1.51bn	79,000	Leo Burnett, Saatchi & Saatchi, Publicis, BBH
4. IPG (US)	\$7.88bn	\$973m	49,700	McCann Erickson, FCB, MullenLowe Group
5. Dentsu (Japan)	\$7.2bn	\$938m	47,324	Aegis, Carat, Dentsu Media, iProspect, Isobar

Sources: WPP, Omnicom, Publicis Groupe, IPG, Dentsu.

industry has gone through a period of increasing concentration through acquisitions, thereby creating multi-agency conglomerates such as those listed in Table 2. While these conglomerates are headquartered in London, New York, Paris and Tokyo, they operate globally.

Large multi-agency conglomerates compete on the basis of the quality of their creative output (as indicated by industry awards), the ability to buy media more cost-effectively, market knowledge, global reach and increasingly range of digital services. Some agency groups have integrated vertically into higher-margin marketing services. Omnicom, through its Diversified Agency Services, has acquired printing services and telemarketing/customer care companies. Other agency groups have vertically integrated to lesser or greater degrees.

Mid-sized and smaller boutique advertising agencies compete by delivering value-added services through in-depth knowledge of specific market sectors, specialised services such as digital and by building a reputation for innovative and ground-breaking creative advertising/marketing campaigns. However, they might be more reliant on outsourced creative suppliers than larger agencies.

Many small specialist agencies are founded by former employees of large agencies. In turn, smaller specialist agencies are often acquired by the large multi-agency conglomerates in order to acquire specific capabilities to target new sectors or markets or provide additional services to existing clients.

With the development of the Internet and online search advertising, a new breed of interactive digital media agencies established themselves. These agencies

differentiate themselves by offering a mix of web design/development, search engine marketing, internet advertising/marketing, or e-business/e-commerce consulting. They are classified as 'agencies' because they create digital media campaigns and implement media purchases of ads on behalf of clients on social networking and community sites such as YouTube, Facebook, Instagram, Flickr and other digital media.

The rise of mobile and the digital duopoly

Search companies, such as Google, Bing and Yahoo and social network Facebook, exploit their ability to interact with and gain information about millions of potential consumers of branded products. Facebook and Google have effectively become a 'digital duopoly' to the extent that they represent almost 60 per cent of the global digital mobile ad market, according to eMarketer, the research group.

Digital search and mobile advertising budgets are increasing faster than other traditional advertising media as search companies like Google and Facebook generate revenues from paid search as advertisers discover that targeted ads on mobile and desktop are highly effective (see Table 3). By 2017, Google had a 66 per cent market share of the \$81.6bn spent on online search advertising globally, with Facebook also increasing its share.

Sir Martin Sorrell, the former CEO of WPP the world's largest multi-service agency group, pointed out that Google is a rival for the service relationships with WPP's clients. WPP group spent more than \$6bn of its clients'

Table 3 Global advertising expenditure by medium (US\$ million, at 2016 average rates)

	2013	2014	2015	2016	2017
Newspapers	93,019	92,300	91,908	90,070	88,268
Magazines	42,644	42,372	42,300	40,185	39,391
Television	191,198	202,380	213,878	210,670	210,459
Radio	32,580	33,815	35,054	34,457	34,130
Cinema	2,393	2,538	2,681	2,767	2,850
Outdoor	30,945	32,821	34,554	36,143	36,324
Internet – Mobile and Desktop	70,518	80,672	91,516	130,019	156,543
Total	463,387	486,908	511,891	544,401	567,965

Note: The totals in Table 3 are lower than in Table 1, since that table includes advertising expenditure for a few countries where it is not itemised by advertising medium.

Sources: ZenithMedia, e-Marketer, Statista, February 2018.

Table 4 US mobile ad spending 2015–2019

	2015	2016	2017	2018 (estimate)	2019 (estimate)
Mobile ad spending (US\$bn)	28.72	40.50	49.81	57.78	65.87
% change	50.00%	41.00%	23.00%	16.00%	14.00%
% of digital ad spending	49.00%	60.40%	66.60%	67.70%	72.20%
% of total media ad spending	15.30%	20.40%	23.90%	26.30%	28.60%

Source: eMarketer.com

ad budgets with Google in 2017 and \$2.1bn with Facebook. Sorrell called Google a 'frenemy' – the combination of 'friend' and 'enemy'. Google is a 'friend' where it allows WPP to place targeted advertising based on Google analytics and an 'enemy' where it does not share these analytics with the agency and becomes a potential competitor for the customer insight and advertising traditionally created by WPP.

Mobile ad spending on sites such as YouTube, Pinterest and Twitter continues to increase at the expense of desktop, taking a bigger share of marketers' budgets. The shift to mobile ad spending is being driven mainly by consumer demand and is predicted to be over 28 per cent of total media ad spending in the US which is why Google has made acquisitions in this sector (see Table 4).

Entry of 'big data' technology consultancies

The analysis of 'big data' is playing an increasingly important role in helping to create targeted and personalised advertising campaigns for the world's major marketers. Consultancies, such as Accenture Interactive and IBMiX, as well as the large accountancy firms PwC Digital Services and Deloitte Digital, all with global reach, are now competing for a share of the advertising market by acquiring creative agencies to add to their 'big data' digital services and have now entered the top 10 agencies ranked on the basis of turnover.

Their services include programmatic advertising and the use of artificial intelligence algorithms that analyse consumer behaviour allowing for real-time campaign optimisations towards an audience more likely to convert to the advertiser's product or service, which is a major innovation, the impact of which is still being assessed.

This has led some industry experts to observe that 'Madmen' now need to become 'Mathsmen', as data

analytics and artificial intelligence are seen to be becoming more important than creativity which traditional advertising agencies have relied upon as a differentiator. This is enabling them to offer a range of services to the major marketing companies that compete directly with traditional advertising agencies.

The disruptive change in the advertising industry at the beginning of the twenty-first century started with the Internet. The convergence of Internet, TV, smartphones, tablets and laptop computers has had a major impact on the advertising industry.

Factors that have driven competitive advantage to date may not be relevant in the future. Traditionally the advertising industry has embodied the idea of creativity as the vital differentiator between the best and the mediocre – and individuals have often been at the heart of this creativity. The emergence of data analytics, programmatic advertising and the use of artificial intelligence algorithms are disruptive to 'business as usual' in the industry. A key question is whether creativity will be important in the future, in relation to breadth of services, global reach and data analysis.

Sources: ZenithMedia, Advertising Age, Statista, eMarketer, February 2018.

Questions

- 1 Carry out a five forces analysis of the advertising industry. What are the strengths of the five forces and what underlying factors drive them? What is the industry attractiveness?
- 2 What strategic group dimensions and strategic groups can you identify? What are the differences between them?
- 3 Which PESTEL factors are driving changes in the industry? Which factors are becoming more negative or positive for the major advertising agencies?