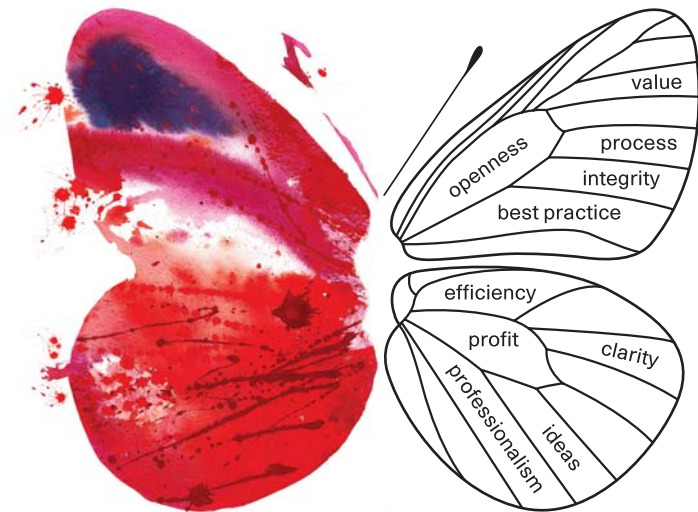


Magic and Logic

**Re-defining sustainable business practices
for agencies, marketing and procurement**



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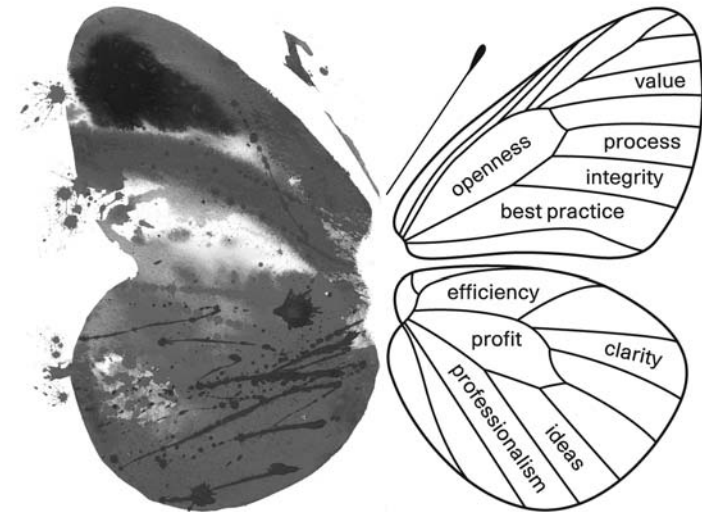


IPA

ISBA

Magic and Logic

**Re-defining sustainable business practices
for agencies, marketing and procurement**



Prepared by Marilyn Baxter
for the Value Framework Steering Group

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Foreword

We read often of the conflicts between Marketing and Procurement, between Procurement and Agencies, and between agencies and their marketing clients. In our view this is counter-productive to our business now, and will become increasingly so as we face the challenges and opportunities of the new digital age.

CIPS, the IPA and ISBA believe we have a responsibility to our memberships to take steps to unify these three key groups of practitioners around a common understanding and mutual respect, and to find shared objectives, shared beliefs, and shared methods. That's why we have created the Value Framework Initiative.

Marketing clients, and the procurement professionals acting with them, need to ensure that they achieve maximum value from their agency relationships, and agencies need to ensure they are run as profitable, sustainable businesses.

Working together we can come to a better appreciation of the complex iterative creative processes involved in developing advertising and marketing communications, so that the inputs involved are valued fairly and realistically.

We can achieve a similar understanding of the nature and value of the outputs and outcomes achieved, especially in a context where on average a third of all shareholder value resides in intangible assets, most of which are brands.

Further, we believe that Marketing, Procurement and Agencies should unite against a common enemy. That enemy is ignorance in the 'City' and the Boardroom about the linkage between marketing (and marcoms as a subset) and the creation of these brand assets. In this way, the joint aspirations of the tripartite Value Framework Steering Group can be set

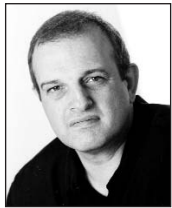
in the context of a wider vision to raise the perceived value and status of Marketing, and its key role in building intangible brand assets.

This 'white paper' contains a valuable analysis of how the relationship between Marketing, Procurement and Agencies can work better to produce a win/win for all parties. It proposes some radical and some not-so-radical changes to current practice that will make our industry better equipped to meet the changes of the future. As such, it represents a call to action for the industry, and sets a clear direction for the way forward. It is in all of our interests to 'make it happen'.



A stylized, handwritten signature of Jane Gibbs.

Jane Gibbs
*Supply Chain Director
Rok Property Solutions
President, CIPS*



A stylized, handwritten signature of David Pattison.

David Pattison
*Chief Executive
PHD Media
President, IPA*



A stylized, handwritten signature of John Clare.

John Clare
*Chief Executive
DSG International
President, ISBA*

1.1 Overview

This paper seeks to identify how Agencies, Marketing and Procurement can best work, individually and together, to produce 'profitable ideas that make profit'.

The findings from interviews with successful leading practitioners in agencies, marketing and procurement, indicate that the required behaviours and processes are not rocket science, or indeed at all surprising or novel; they are in fact simple common sense business practice. Although much of the responsibility falls to agencies to change their approach and practices, agencies cannot create more profitable ideas **for** clients without best practice **from** clients: the parties have a joint responsibility to act in ways that are more likely to produce a win/win.

The simple, common sense nature of the findings, belies the amount of change that will be demanded of all three parties in order to adopt the best practices of the leading companies. The findings might be easy to understand but they still represent a challenge to many of the traditional practices and attitudes in the industry. For example, identifying 'what best agencies do' as a subtle blend of *logic* and *magic* throws into sharp relief that *logic* (anything to do with project management, financial management, traffic, purchasing of third-party services, etc.) has been woefully neglected by many agency managements and by many marketing clients, and needs significant improvement. On the other hand, though there was little or no criticism from clients of the quality and value of the *magic* part of what agencies deliver (anything the agency does to produce brilliant ideas that can grow brands and businesses), it was still recognised that better *management* of the *magic* would help improve its effectiveness.

Agencies that are successful are run much like other successful businesses; they share a number of characteristics to do with management philosophy and attitude, and business processes and ways of working. The rewards for operating best practice are potentially huge for agencies, not least in terms of profitability. Because they have a better all round 'product' they get their top-line income right and their superior management processes enable them to achieve better bottom-line profits.

Marketing clients have an essential contribution to make towards helping their agencies produce ideas that make profit for their brands and businesses. The impact of the marketing client on an agency's ability to run a successful business is significant, especially in relation to clear briefing and avoiding wasted work. It is no coincidence that the best clients tend to work with the best agencies: broadly speaking, each gets the partner they deserve.

The recent addition of **Procurement** into the agency/marketing relationship has sometimes been a difficult one. The more enlightened procurement people realise that what their company wants are executable ideas which make a real difference to the business bought in an open and transparent way, and they look for a win/win when dealing with their agencies. Key to their effectiveness is an understanding of how agencies create value for the client company and therefore an understanding that the main focus of their attention should be on the *logic* element of the agency's activities, leaving the management of the *magic* to their marketing colleagues.

The paper concludes that there is still much that can be done by Agencies, Marketing and Procurement, and by the industry trade bodies, to improve ways of working and create more productive relationships, that result in ideas that make profit for all. The paper puts forward proposals for what each of the parties needs to do to achieve best practice. The proposals differ for each of the parties, but there are many common themes to do with clarity of agendas, openness, integrity, professionalism, process, and efficiency. More controversially, the paper calls for radical changes to accepted practice in agency and marketing management, financial transparency, pitching, the measurement of effectiveness, approaches to decoupling, and remuneration.

I wish the industry well, in getting to grips with the issues, and taking the recommendations of this report forward.



Marilyn Baxter
Research Consultant

1.2 Introduction

This report has been commissioned by the Value Framework Steering Group, a tripartite group representing CIPS, the IPA and ISBA. It forms part of the Value Framework Initiative, which aims to find common ground between the three parties: Agencies, Marketing, and Procurement. The brief for this particular project was to find ways of working that would produce 'profitable ideas (for marketing services agencies) that make profit (for client companies/brands)' – and so deliver a win/win for both clients and agencies. The thinking behind the project was that agencies need to make adequate profits in order to invest in producing the kinds of ideas that will help grow their clients' businesses and profits, so it is in the interests of all three parties to work together in the most productive way.

A first stage of research was conducted by Professor Robert Shaw using 'think tanks' of senior representatives of each of the parties; these elicited the issues and problems as seen by practitioners. This stage found many negative attitudes and practices, and a general lack of alignment between Agencies, Marketing and Procurement that resulted in business models and processes that often worked against, rather than for, the interests of each of them. The purpose of Stage 2 of the research was to find the common ground between the parties, and to develop practical guidance on business models and processes that work. The research approach was not to dwell on what is currently wrong with the relationships, or on some theoretical model of how they could work better together, but to concentrate on what is right and what is currently being practised, and to distil the essence of business success. The research method was to use depth interviews with the senior representatives of successful agencies and marketing and procurement clients (as selected by CIPS, the IPA and ISBA), and from these to derive a 'model' of best practice that the industry could adopt.

In total, 24 depth interviews were completed between November 2005 and March 2006: 11 with agencies (covering creative, media, integrated and digital) including two heads of agency procurement; nine with clients (both marketing and procurement); and four with

consultants/intermediaries. A full list of the organisations interviewed is contained in Appendix III. During these interviews, respondents were asked for their views, experience and practice across their whole careers, not just in their current role. Since all respondents were in very senior positions, their careers spanned several decades and many changes of employer. Thus, this report represents a much wider range of experience than simply that of the 24 organisations that participated in the research.

I am grateful to all respondents for giving so freely of their time and thoughts. Every interview was a stimulating encounter, rich in insight and experience, and respondents were very willing to share their practices. After 30 years in the industry, I started this project with a general feeling that there must be a better way of working that would benefit all parties, but without any preconceptions about where that thought might lead. Over the course of the research the 'better way' began to emerge, and I was struck by the way ideas from the different disciplines came together into a coherent industry view.

The views expressed in this report are those of the respondents, but the key conclusions are those of the author. Where appropriate, quotations from respondents (identified only by their category) have been used to illustrate the general points made.

1.3 Magic vs Logic: a useful framework for considering the issues

There has always been a tension in agencies between the creative part of the business and the implementation/delivery. Traditionally, it has been the view that agencies cannot manage each of these equally well, but that one is bound to dominate – either creatively led and rather chaotically managed, or very well organised but creatively unexciting. In the face of a new breed of agencies, some of which are managing to do both, this view looks increasingly outdated. However, it would be wrong to conclude that there is no difference between these two activities or that they can be managed in the same way.

In a recent article in *Market Leader* (Autumn 2005), Charles Kirschner of MSC proposed a useful way of thinking about what agencies do which could lead to a different way of thinking about how to manage them. He has applied it to marketing activity in general, but it seems to work equally well for agencies. This notion is that the work of an agency can be divided into '*magic*' and '*logic*.' The *magic* is anything the agency does to produce brilliant ideas that can grow brands and business (customer insight, strategic thinking, brand strategy, creative and media strategy and creative expression); it requires high value, creatively minded people working in a stimulating environment and in small teams, who are highly motivated, and who have a lot of freedom and not much in the way of process to constrain them. The *logic* is the part of the agency business concerned with project management, traffic, creative services, production, financial management, time management, job control, purchasing of third-party services (e.g. print buying), production, arguably media buying etc., where more analytical and administrative skills are required, and the work is more amenable to establishing processes. In most agencies, 90% of the management focus is on the *magic*, but 90% of the client's money is spent on the *logic*.

Interestingly, this research has thrown up little or no criticism from clients of the quality and value of the *magic* part of what agencies deliver. Most of the problems between clients and agencies appear to be in the *logic* department.

The *logic* part of the agency's activities has traditionally been somewhat neglected by agency managements. By comparison with the *magic*, it has been considered dull, done by people who are a long way down the hierarchy, by back-room people (below stairs almost) who rarely get to meet clients, and lacking the glamour and excitement of the *magic*.

Agency managements are not alone in having neglected the *logic* of what agencies deliver: client marketers have also tended to concentrate only on the *magic*. Enter Procurement, who are very interested in the *logic*, and by focussing on it in their dealings with agencies they have changed the dynamic of the client/agency relationship and, in some cases, the management focus of agencies.

A major contribution to the objective of producing ‘profitable ideas that make profit’ could be made if all three parties recognise the *magic/logic* distinction, deal with each other accordingly, and pursue both with equal vigour.

1.4 Layout of the report

Using the results of the interviews, this report examines how the best practitioners in our business deliver ‘profitable ideas that make profit’, dealing with each group in turn – Agencies, Marketing and Procurement. In the first two sections I deal with agencies at greater length than the other parties as it is agencies that are the ‘common ground’ between the parties, and also there is much to say about agencies’ general business practices as well as how they interact with Marketing and Procurement. Sections 4 and 5 then go on to examine best practice in the way that Marketing and Procurement can help Agencies produce profitable ideas. Section 6 proposes changes that each of the parties need to make to deliver best practice. The Appendices contain further detail of some signature practices, and also include an examination of the actual profitability of agencies from the Willott Kingston Smith annual survey of financial performance of marketing services companies.



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2

What differentiates profitable and successful agencies from the rest?

This section examines the business practices and processes of some of the best performing agencies. As referred to above, it is mainly in the *logic* department that the best agencies stand out. However, though there were few criticisms by clients of the *quality* of the *magic* that agencies deliver, nonetheless there were questions about how efficiently and effectively the *magic* was delivered. The successful agencies are the ones who are good business managers and who are able to manage both the *magic* and the *logic* elements equally well.

The objective of this research was to distil the essence of business success, and from the interviews it is possible to identify six characteristics of successful agencies that are key to their success; five of them are to do with management philosophy and attitude, and one is to do with business processes and ways of working.

Agency management philosophy and attitude

- They run their agency as a business.
- They have a differentiated product.
- They are in business to create value for clients and are results oriented.
- They are confident of their ability and their value.
- They run their business with a high degree of professionalism and integrity.

Agency business processes

- They have disciplined business processes.

2.1 Run their agency as a business

IT'S A BUSINESS, NOT A LIFESTYLE.

Marketing

I'M SCEPTICAL WHEN I HEAR AGENCIES
COMPLAINING ABOUT NOT MAKING PROFITS
BECAUSE I CAN SEE HOW INCOMPETENT SOME
OF THEM ARE IN RUNNING THEIR BUSINESSES.

Marketing

In the 70s and 80s it was relatively easy to make money in the agency business. Commissions generated large revenues and so there was no imperative to manage the agency's resources (time) rationally; it allowed inefficient working practices to develop – it didn't matter how many meetings were held, or how many iterations of creative work; it didn't matter if the contract hadn't been signed, or there was no contract; there was no necessity to be good at negotiating fees. It also offered no incentive to look after the client's money, indeed conspicuous waste was almost a badge of honour in some agencies, particularly in the 80s.

Further, the original agency business model was set up on the basis of a commission system that paid for a client service ethic that placed close personal relationships with individual clients at the centre of the business.

Clients got used to being 'over-serviced', expecting the agency to write the chairman's speeches, to be lavishly entertained and so on, and the agency willingly colluded in this, believing, often rightly, that the strength of the personal relationship with the client would protect the business relationship.

The move to fees based on time was a logical one, but many attitudes and working practices stayed the same (in both agency and client organisations). There are still some 'dinosaurs' left roaming the agency and client world, where the 'high package/high lifestyle' of top management sets the tone for everyone else.

CHARACTERISTICS OF SUCCESSFUL AGENCIES AGENCY MANAGEMENT PHILOSOPHY AND ATTITUDE

- RUN THEIR AGENCY AS A BUSINESS
- HAVE A DIFFERENTIATED PRODUCT
- IN BUSINESS TO CREATE VALUE FOR CLIENTS AND ARE RESULTS ORIENTED
- CONFIDENT OF THEIR ABILITY AND THEIR VALUE
- RUN THEIR BUSINESS WITH A HIGH DEGREE OF PROFESSIONALISM AND INTEGRITY

AGENCY BUSINESS PROCESSES

- HAVE DISCIPLINED BUSINESS PROCESSES

THE ECONOMICS OF THE AGENCY
WORLD DOESN'T MATCH THE
GLAMOUR OF THEIR WORLD.

Marketing

But the whole commercial/financial environment is different now than then: there is pressure to reduce costs in all businesses, and the agency market is more crowded and competitive than ever. In response, some agencies at least have changed their approach to meet the challenge and succeed in this new environment. Here, the creative agencies may have something to learn from media and integrated agencies, who have generally been more business-like in their approach to managing both the *magic* and the *logic*, more focussed on effectiveness, and less assumptive about their right to be heard.

Successful agencies are run much like other successful companies. Success starts from the top and these agencies have people in top

management who feel a sense of ownership of their agency; they have clear business goals, coherent values, and a defined culture, and they give a strong lead.

THE TOP MANAGEMENT AREN'T SWANNING ABOUT HERE, THEY'RE REALLY COMMITTED. THE NAMES ON THE DOOR ARE GENERALLY THE FIRST IN IN THE MORNING.

Agency

Because they regard the agency as a business, they develop grown-up business relationships with client companies, rather than personal relationships with individuals, and their business focus is shared throughout the agency – everyone understands it's a business.

These best practice agencies are supported by good financial and commercial management and systems; money – clients' and the agency's – is respected. Those in agency management are financially educated, make sure they have good management information, have a clear understanding of their cost base and of the profitability of each client. Financial and commercial people are integrated in the business and understand the nature of client service and the importance of quality: their commercial goals are aligned with their client service goals. They don't believe that being in a creative business means you have to be chaotic.

SUCCESSFUL AGENCIES CAN BE BOTH CREATIVE AND BUSINESS FOCUSSED - IT DOESN'T HAVE TO BE A CHOICE. THE PEOPLE AT THE TOP DON'T HAVE TO BE FINANCIAL EXPERTS BUT HAVE TO BE AT LEAST INTERESTED AND GIVE THE FINANCIAL PEOPLE THE AUTHORITY TO MANAGE IT.

Consultant

Management care about and focus on efficiency/cost. They pay attention to the use of their resources, they aim to have efficient processes that cut out waste, they control costs, and do not 'over-engineer' their account teams. They earn a client's trust as they are seen to be mindful of the client's money. They do not see Procurement's pressure to reduce costs as a threat or as undesirable, but rather as a legitimate desire to ensure the best product is delivered at the best price.

IF YOU SEEK PERFECTION IN WHAT YOU DO, WHY WOULDN'T YOU WANT TO RUN THE BUSINESS PROPERLY?

Agency

Many of them put the quality of their people at the heart of the business, believing in a service/value/profit chain, which works as per Figure 1.

Figure 1: The service/value/profit chain



They focus more attention and resources on maintaining and growing existing customers rather than chasing new ones, and make a realistic assessment of the probability of winning before agreeing to pitch.

To help improve efficiency, they are willing to use consultants/expert help to manage the business better and work smarter.

2.2 Have a differentiated product

AGENCIES THAT SUCCEED ARE THOSE THAT CONCENTRATE ON DELIVERING A QUALITY PRODUCT AND HAVE AN OFFER DISTINGUISHABLE FROM THEIR COMPETITOR.

Consultant

THE BETTER PERFORMERS HAVE A BETTER WAY.

Consultant

If you have a better mousetrap, people will beat a path to your door, says the old marketing maxim, and that is certainly true for agencies. But it is hard to develop a better product in this business and even harder to sustain it.

ALL NEW AGENCIES START OUT BY TRYING TO BE DIFFERENT, BUT END UP NOT BEING.

Marketing

Those agencies that have enjoyed consistent success appear to have a better way. Most significantly, they have intellectual content – beliefs, proprietary models, tools and processes that articulate how they believe

communications work, how they produce great ideas, how they measure results or how to build in effectiveness. By making definitive statements of these ideas, they not only position and differentiate themselves in the market, they also create a culture that attracts like-minded employees and clients.

Some also differentiate through developing a different structure than the conventional agencies, one that is designed to fit their business strategy rather than just following the conventional agency model.

2.3 In business to create value for clients and are results oriented

AGENCIES HAVE MOVED FROM BEING SPENDERS TO BEING INVESTORS AND VALUE CREATORS.

Marketing

Best practice agencies are run by people who understand how to create value for clients and who are personally motivated by creating great ideas; it's what they care about above all else. The quality of the ideas is the driving force of the agency.

WE MANAGE QUALITY, NOT MONEY.

Agency

AGENCIES THAT SUCCEED ARE THOSE THAT ARE WATCHING THE BALL, NOT THE SCOREBOARD.

Consultant

They focus the agency's resources on creating value, and in particular believe that the quality of people is key to producing the best product (see Figure 1, page 14). They hire the best people they can and pay them accordingly, and invest in their development.

MOST AGENCIES DON'T LOOK AFTER THEIR PEOPLE VERY WELL. IT'S NOT SURPRISING THERE IS SO LITTLE LOYALTY AND STAFF MOVE AROUND SO MUCH. THAT'S NOT IN OUR INTEREST AT ALL.

Marketing

Also central to the agency's philosophy is a focus on results and effectiveness of outcomes as well as outputs – doing great work that works. It is part of the culture, not bolted on. They don't believe there's a conflict between effectiveness and creativity: the emphasis is on converting creativity *into* effectiveness. They take the initiative in proposing evaluation rather than wait for it to be 'done to them', and invest in the people, systems, and methods that will enable them to prove effectiveness. They take the view that their investment in proving effectiveness (e.g. through research or econometrics) bolsters the agency's perceived value to the client.

OUR AIM IS TO PRODUCE A CLEAR LINE OF SIGHT AND A CLOSER CONNECTION BETWEEN THE ADVERTISING AND THE BUSINESS RESULT.

Agency

An approach that focuses on the return on investment that advertising delivers is seen as a bulwark against further margin erosion:

AGENCY MARGINS ARE UNDER PRESSURE BECAUSE ADVERTISING AND AGENCY FEES ARE SEEN AS A COST. AGENCIES ARE NOT GOOD AT SQUEEZING OUT COSTS. THE WAY FORWARD IS TO TIE OUR WORK TO BUSINESS RESULTS AND SO WE HAVE TO FIND METRICS THAT WILL HELP US DO THAT.

Agency

They are conscious that it is not enough simply to care about creating value – they also have to communicate the fact. These agencies explain and merchandise the value of what the agency does to clients (both Marketing and Procurement) and help Marketing explain the value to their colleagues and superiors in the client company.

2.4 Confident about their ability and their value

GET THE PRODUCT RIGHT, THEN HAVE THE BALLS TO CHARGE ENOUGH FOR IT.

Consultant

Self-confidence is not in short supply in the agency world. But what differentiates the successful agency is a depth of confidence that runs through the entire organisation, a cultural confidence rather than a personal self-belief, and it is founded on knowing that the agency can and does produce truly great work that delivers value for clients.

Many respondents emphasised that agency managements needed to be firmer about standing their ground, and some of the profitability issues in agencies are unquestionably caused by unconfident management, or being in a weak negotiating (business) position. Often, attempts by the

more confident agencies to stand firm can be undermined (and undercut) by weaker brethren. In this connection, several respondents mentioned how their confidence in negotiating with clients had been transformed by taking a negotiating skills course, especially where the whole management team had been trained together, thus ensuring they were all aligned in their approach. Acquiring these skills had made them far more robust in their negotiations with clients.

True confidence in best practice agencies is manifested in a number of ways:

- They are on the **front foot** with Marketing and Procurement, and take the initiative.
- They are **not reticent** in asking for money, because they know they are adding value and have the skills to negotiate.
- They **have boundaries**. They are prepared to walk away if clients don't share their goals (either financial or quality). They resign business, decline to pitch, or pull out of a pitch, if they discover a poor fit with the prospective client's culture. Sadly, although this is good commercial practice, it is sometimes regarded as supreme arrogance by clients and very much resented.
- Because they can, to some extent they **pick their clients**. They choose to work with clients who fit their culture and for whom they believe they can deliver value.

WE DON'T WORK WITH PEOPLE WHO DON'T
VALUE US - IF THEY WANT TO TRADE ON
PRICE, WE'LL JUST WALK AWAY.

Agency

- They demand a **partnership relationship** with clients, not a supplier one. The relationship is collaborative, not arms length, and there is shared responsibility and more commitment on both sides. They set boundaries of behaviour they will and won't tolerate, and make these clear at the beginning of a new client relationship.

However, none of the agencies interviewed had found a way of pitching for new business without giving away some element of their unique contribution – their ability to create ideas, much to the amazement of some of the industry commentators:

AGENCIES, UNIQUELY, GIVE AWAY THEIR
BEST IDEAS TO OTHER PEOPLE'S CLIENTS.

Consultant

The most confident operators avoided presenting whole finished campaigns at pitches, but nonetheless admitted to giving away potential valuable ideas. One solution adopted by best practice agencies was to aim to get more work from existing clients, on the basis that a client who already knew and had confidence in the agency would be more likely to award new business without a pitch. Although agencies found it difficult to see how they could pitch without giving away their best ideas, experienced procurement people have some thoughts on this that are developed in section 6.

2.5 Run their business with a high degree of professionalism and integrity

The classic 60's Hollywood caricature of an 'adman' was of a charming, but less than trustworthy, wheeler/dealer; as with all caricatures, there was then some truth in this portrayal. Although business practices in

agencies have been cleaned up significantly in recent years, nonetheless, something of this perception still remains. Recent scandals (and investigations into specific agencies' 'Spanish practices') have harmed the reputation of the whole sector.

This is an external factor driving more transparency and accountability, but many agencies haven't yet worked out how to respond. The better agencies have, and run their businesses professionally. They are transparent and honest in their financial dealings: they have open books, no hidden revenue streams, and clarity in their contracts. The rise of Procurement is not a threat to agencies who are transparent and who have worked out their business model, fee structure and charges to allow for giving up previously hidden revenue streams. These agencies welcome the contribution of Procurement: they respect their skills, are willing to learn and apply their methods and are open to conversations. In some cases, Procurement are seen as longer-term players than Marketing, and so building relationships with them is doubly important.

OUR MANTRA IS TO BE AS ACCOUNTABLE
AND TRANSPARENT AS POSSIBLE.

Agency

WE MUST EMBRACE THEM (PROCUREMENT)
- THEY CAN ADD REAL VALUE, AND WE
IGNORE THEM AT OUR PERIL.

Agency

Again, the tone is set from the agency leaders who make it clear that high standards of behaviour are expected from all staff. The client's objectives and business imperatives are taken seriously, rather than hoping to persuade her/him to accept inappropriate recommendations, and they are honest about the achievability of client objectives where these are believed to be unrealistic, even at a cost to the agency.

2.6 Have disciplined business processes

The philosophies and attitudes listed above tend to be associated with, and manifested in, specific business processes. Culturally, agencies are creative organisations, generally run by people who are unsympathetic to the notion of controls and processes, but the better ones appreciate that they must pay some attention to process if they are going to be financially successful.

From our interviews, it does not appear that agencies have generally adopted specific 'schools' of business process, e.g. business process re-engineering, Kaizen, Six Sigma, etc., but rather have developed approaches that pragmatically reflect their business philosophy (though the arrival of more MBAs in agencies in recent years has had a positive effect on professionalising management processes). There is one published example, RKCR/Y&R, which has successfully applied the Lean Six Sigma approach to some of their *logic* processes, like back-office financial functions (e.g. billing) and some studio functions (e.g. retail black and white press ads).

Some agencies have embraced the need to be more process oriented by hiring senior and experienced procurement people of their own. They have introduced more process into the *logic* parts of the agency, in what was previously seen as a 'process-free zone'. These agencies report substantial benefits, in terms of: understanding client profitability; understanding and refining work flows and use of resources; more projects done 'right first time'; more cost efficient purchasing from suppliers; saving cost by using technology to hold assets digitally; more robust dealings with client procurement people, and more transparency based on a clearer exposition of what the agency does. And there are more efficiencies to be had from using procurement expertise:

WE LIKE TO THINK WE'RE SPECIAL IN THE
AGENCY WORLD, BUT THE BACK-OFFICE STUFF IS
SIMILAR IN MANY ORGANISATIONS, SO WHY
NOT USE THE LEARNING THAT'S OUT THERE?

Agency procurement

As well as achieving real efficiencies and savings, agencies report another benefit of being better at process, which is to change the dynamic of the agency's relationship with Procurement: procurement people are impressed with agencies that are seeking efficiencies for themselves, and see that they can work *with* the agency to reduce costs, instead of *against* them.

Far from thinking that 'process' has no role in a creative business, best practice agencies believe in the positive role of business processes *as a support* to people doing the business.

THE BETTER THE MACHINERY RUNS, THE MORE IT TAKES CARE OF ALL THE ADMIN AND ALLOWS PEOPLE TO BE CREATIVE.

Agency

For those who really cannot get on with the idea of 'processes' in an agency, the phrase 'ways of working' seems to meet with more acceptance.

More examples of the signature practices of best practice agencies can be found in Appendix 1.

3

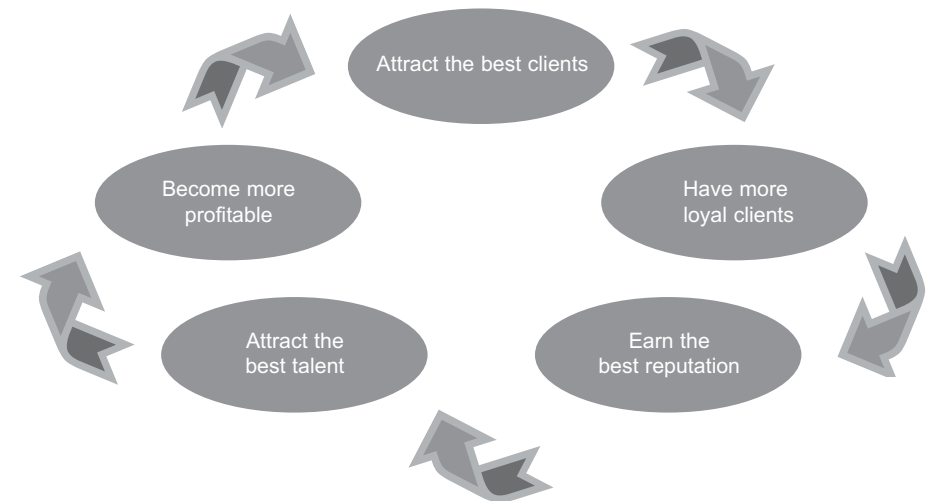
What are the rewards for agencies that operate best practice?

The rewards for operating best practice are potentially huge for agencies, and come from a virtuous circle of effects. Best practice agencies are able to:

- Earn the best reputation
- Attract the best talent: both employees and third-party suppliers
- Attract the best clients
- Have more loyal clients

... and through these, become more profitable. See Figure 2.

Figure 2: Virtuous circle of effects



3.1 Earn the best reputation

Agencies, as businesses, are naturally motivated by the pursuit of profit, but it would appear from these interviews that other softer factors are often more important rewards for best practice agencies than money. These are, for example, the more personal, self-actualising rewards of fame, recognition and reputation, the esteem of the industry, self esteem, agency morale, and so on.

In a world where image and appearance matter a great deal, and where agency reputations are endlessly discussed, the importance of a good reputation cannot be underestimated, and it is this fact that may explain the industry's preoccupation with awards of all kinds.

3.2 Attract the best talent: both employees and third-party suppliers

Real benefits flow from these reputational rewards that serve to make it easier for best practice agencies to be successful, financially and otherwise. A good reputation in the industry is a magnet that attracts and retains the best people, and attracts the best outside suppliers, from which the agency gets the stimulation of working with excellent people and the freedom to do more exciting and original work.

3.3 Attract the best clients

From this research, there certainly seems to be something in the notion that the better agencies attract the better clients (though it is not universally true). This probably occurs because:

- The best clients care about (and can benefit from) the reputation of those they work with, and will seek out agencies with good reputations.

- Good clients help the agency be better – agencies learn a lot from very professional clients, and there is an exchange of good processes and a mutual reinforcement of best practice.
- Arguably, the best clients will buy the best work, which will be produced by the best talent – a virtuous circle for a creatively excellent agency.
- Best practice agencies can avoid or afford to resign unprofitable or difficult clients, whereas less good agencies are more likely to be struggling financially and so must tolerate the less good clients.

3.4 Have more loyal clients

Greater client loyalty is another potential reward for best practice agencies. From our interviews, it would appear that adhering to best practice can bring rewards in the length of client relationships, though it is by no means guaranteed; we found several examples amongst best practice agencies of longer-term relationships being sustained over many years, and also of longer-term contracts being negotiated. Nonetheless, the best operators in the business did not necessarily feel more secure about their client base than other agencies: 'You're only three phone calls from disaster' is a widespread feeling even in the best agencies. Where longer contracts had been negotiated, or long-term relationships sustained, these tended to be between best practice clients and best practice agencies.

WE HAVE CONFIDENCE THAT THE AGENCIES WE HAVE APPOINTED ARE THE RIGHT ONES; WE MAY HAVE TO KEEP UP THE PRESSURE TO MAKE SURE WE GET THEIR BEST PEOPLE ON OUR BUSINESS, BUT WE DON'T EXPECT TO RE-PITCH DURING THIS 5-YEAR PROGRAMME.

Marketing

Getting the *logic* part of the business right can contribute to client loyalty. As is well known, it is often the lack of hygiene factors (invoicing, budget control, timing, etc.) in the agency's performance that produce dissatisfaction from clients, and these problems can have a big impact on client retention. Getting the hygiene factors right can reduce client frustration, takes out the pain, and allows clients to get better value because resources are used better, the job is done quicker, and ultimately they get better work. There is also a potential creative benefit to being more efficiently managed, in that the agency is more likely to get things right first time; this increases the chances of getting great work accepted, thus bringing a win/win for both clients and agency.

A focus on effectiveness appears to build stronger and longer client relationships. Agencies that clearly care about the effectiveness of their work are more likely to be treated seriously as a partner by clients. Discussing effectiveness up front forces clients to be clearer about their objectives, and about how to define and judge success (a discipline on both sides). It can improve their financial relationship, because they have a more constructive dialogue on PBR. Marketing clients are more likely to stay with an agency that can prove the value of what they do, and that can give them the ammunition to engage and convince finance directors and Procurement.

Client loyalty itself produces a virtuous circle: long-term relationships bring client and agency closer together; they trust each other more; the client will share more about his business with the agency; so the agency has more depth of understanding, can have better insights and do more effective work; which earns more loyalty from the client; and so on.

3.5 Improved profitability

A GREAT PRODUCT GETS THE TOP
LINE RIGHT. PROFIT COMES FROM
GOOD MANAGEMENT.

Consultant

There are two ways an agency can improve its profitability: by increasing its income ('top-line effects'), or by managing its costs ('bottom-line effects'). Agencies in the Top Ten tables tend to be those that manage to do both. Best practice (as described in section 2) can produce both top- and bottom-line effects.

3.5.1 Top-line effects

As the consultant quoted above suggests, the quality of the agency's product is the most important element in getting the top line right, for the simple reason that they are able to charge more for what they do: as quoted earlier: "Get the product right, then have the balls to charge enough for it". Some agencies have succeeded in increasing their fees by moving away from simply charging for time, and instead charging a flat fee for a 'process', much like management consultants do. This works particularly well in planning (both media and through the line), where agencies have historically found themselves under pressure to 'give away' the planning with the execution. However, it would appear that the best agencies, though adopting what they believe to be a premium business model, are not necessarily charging premium rates for their 'better' contribution. Two agencies recognised as delivering exceptionally good work and who are run on this best practice model both remarked that they suspected there was little difference between their charges and those of other agencies.

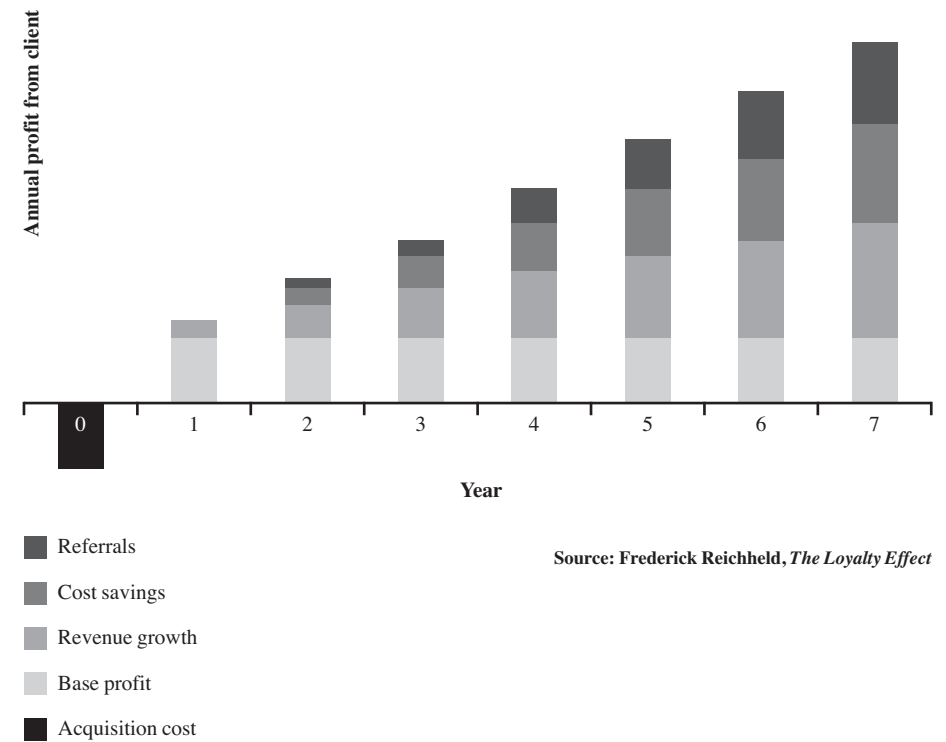
A good product is the start of a virtuous circle of potential top-line effects: doing great work builds fame and reputation; this increases your attractiveness to clients; you can then pick and choose the best clients, which enables you to do even better work; this attracts the best talent, and the best suppliers, which reinforces the circle yet more. Adding an emphasis on proving effectiveness to the mix improves the top line even more, as clients spend more money behind campaigns that are demonstrated to bring results.

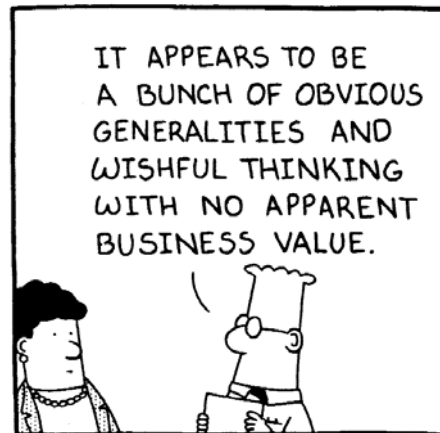
3.5.2 Bottom-line effects

Ensuring that a good level of income produces a good bottom line is all about good management, principally, though not entirely, to do with managing costs. Applying the best practices detailed in section 2 produces several bottom-line effects. Agencies that have a clear understanding of their cost structures, and of individual client profitability, are in a stronger position to negotiate with clients (with Procurement especially). Better business processes enable the agency to work more efficiently, cutting out waste, and applying expensive resources in the most productive way.

The reputation of best practice agencies for great work also produces some positive bottom-line effects through increased client loyalty. Keeping and growing existing clients cuts down on pitching costs, as business from existing clients is commonly awarded without a pitch. High client turnover is very expensive; it costs a lot to pitch, and often profitability is not established on an account for two or three years. And clients who are very satisfied with their agency are more likely to recommend them to other clients. An academic study by Harvard professor Frederick Reichheld, an expert in loyalty, has demonstrated that loyal clients drive up profitability, and has found that this effect is greater in advertising than in other industry sectors. The mechanism of this effect is illustrated in Figure 3.

Figure 3: How loyal clients drive up profitability





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4 How do the best marketing people contribute to their agencies producing profitable ideas?

Marketing clients have an essential contribution to make towards helping their agencies produce profitable ideas for them. The rewards for clients who operate best practice can be enormous: on the one hand, they get ideas that transform their brands and businesses, or that can produce revenue in their own right; and on the other, those ideas can be produced in less time, with less waste, hassle and pain, and at a lower cost. The impact of the marketing client on an agency's ability to run a successful business is equally significant, especially in relation to clear briefing and avoiding wasted work. It is no coincidence that the best clients tend to work with the best agencies: broadly speaking, each gets the partner they deserve.

In the same way that the research has identified characteristics of successful agencies, we have also identified the characteristics of best practice marketing clients, and they are these:

- They are professional, disciplined, and well organised.
- They understand and respect the agency's contribution and champion it internally.
- They know what they want and are demanding.
- They are committed to quality and expect to pay for it.
- They are honest and fair dealing.
- They regard agencies as partners, not just suppliers.
- They have a constructive relationship with Procurement.

4.1 Professional, disciplined and well organised

Marketing is often criticised as being rather a ‘flaky’ occupation. By contrast, best practice marketing department teams are well organised and disciplined, and are strongly led from the top by people who are serious, true professionals. They develop adult business relationships with their agencies. They have clear, quantified objectives, and realistic and sensibly set budgets that are aligned with their objectives; they establish metrics, monitor and measure performance in order to learn and continuously improve. They recognise their responsibility for avoiding waste, through disciplined briefing and approvals processes, and control their team and colleagues.

Some larger companies use a standardised process to ensure that the marketing people throughout the company work to the same approach and the same standards in developing communications activity and in working with agencies; it works because everyone knows the rules. Typically such a process will document how to brief an agency, how to judge work, how to feedback responses, how to use research, how to measure results, how to appraise the agency, and so on. The effectiveness of this type of process is underpinned by training courses and workshops. In one case, their process was designed by asking agencies what they did and did not like about working with the company. While this formal approach is not for everyone, it does make for a more disciplined and better organised relationship with the agency.

Pitching is an area that can really benefit from a more disciplined approach on the part of Marketing. A huge amount of creativity, time and money is wasted by both clients and agencies on pitching, and there is a belief among our respondents that this is not the best way to get ‘profitable ideas that make profit’. Best practice marketing teams either choose to award new assignments to agencies already on the roster that they know and believe in, or they invite only a few agencies to pitch, having established beforehand (through interviews, credentials, etc.) which agencies are likely to fit their needs; they have a clear pitch process, with timetables and milestones, and stick to it. This degree of formality is apparently quite rare.

ALL TOO FREQUENTLY, PITCHING
IS A PROCESS-FREE ZONE.

Procurement

CHARACTERISTICS OF SUCCESSFUL MARKETING CLIENTS

- PROFESSIONAL, DISCIPLINED AND WELL ORGANISED
- UNDERSTAND AND RESPECT THE AGENCY'S CONTRIBUTION AND
- KNOW WHAT THEY WANT AND ARE DEMANDING
- COMMITTED TO QUALITY AND EXPECT TO PAY FOR IT
- HONEST AND FAIR DEALING
- REGARD AGENCIES AS PARTNERS, NOT JUST SUPPLIERS
- HAVE A CONSTRUCTIVE RELATIONSHIP WITH PROCUREMENT

4.2 Understand and respect the agency's contribution and champion it internally

Best practice marketers have a strong belief in the ability of agencies to deliver the *magic* that can transform their brands and businesses. This means they trust and respect the agency's ability to create value, their expertise, and their creative judgement about what will work.

WE ENCOURAGE THE AGENCY TO TAKE OWNERSHIP AND TO TAKE RISKS. WE KEEP LETTING THE LINE OUT, BUT STILL MAKE SURE WE HAVE THE OTHER END SO WE CAN PULL IT IN IF NECESSARY!

Marketing

They are very clear that their own role and that of the agency are different, and know where to draw the line; they don't play at being creative director.

They feel a sense of ownership, co-authorship and responsibility for the ideas created by the agency. They stand up for the agency and their work. They are committed to proving the effectiveness of the agency's work and merchandising it through the company. This means they are willing to work at developing appropriate metrics, and to invest in evaluation. They appreciate and champion the potential value created by agencies to the business, the bottom line, culturally, and to the company's reputation.

4.3 Know what they want and are demanding

No one would suggest that best practice marketers are necessarily easy to work with; indeed they are generally very demanding. They give direction, and are clear with agencies as to what is expected of them in terms of both outputs and results. They are good decision makers, with good judgement about ideas, balancing rational and emotional reactions. They demand the best.

WE ENSURE EVERYONE IS UP FOR IT. WE'VE NO TIME FOR SLACKERS OR PEOPLE WHO AREN'T THE BEST.

Marketing

THIS IS A VERY CHALLENGING ENVIRONMENT. WE DEMAND HIGH STANDARDS, WE'RE NEVER SATISFIED. THE PEOPLE WE LIKE TO DO BUSINESS WITH MATCH OUR CULTURE.

Marketing

4.4 Committed to quality and expect to pay for it

Best practice marketers are looking for the best ideas they can get for their business. They appreciate that quality comes from the best people and the best processes, that it comes at a price and that it's worth paying more for.

THE BEST PEOPLE ARE GIVEN THE FREEDOM TO PRODUCE THE BEST IDEAS.

Marketing

They see agency fees as only a small part of the budget compared to what those fees can deliver. They understand the difference between price and value for money and are prepared to make the trade-off where it matters.

4.5 Honest and fair dealing

During the course of this research, some horror stories of bad client behaviour were described, particularly in relation to pitches, entertaining, bonus payments and notice periods. Integrity and transparency in dealing with agencies is a key ingredient in best practice behaviour. These marketers deal honestly, both commercially and personally, with their agencies: they have clear, published terms of business; they honour

agreements and contract terms with their agencies, especially in paying out performance related bonuses; they review agency performance regularly, honestly and openly. In pitches they ensure a level playing field, use formal and transparent pitch assessment criteria, give debriefs to unsuccessful agencies, and don't use ideas without paying for them.

Where they have many agencies, they deal transparently and even-handedly with all those on the roster. One client has joint meetings with all his roster agencies, and shares with them his budget allocation for each communications discipline. Roster agencies are invited to have a point of view on every other agency's work, and all are bonused on a collective target. Everything is in the open.

4.6 Regard agencies as partners, not just suppliers

Clearly, agencies are suppliers to client companies, and the commercial relationship between the two is important to get right. However, best practice marketing believes that 'profitable ideas' are more likely to be created by agencies if they treat them as true business partners rather than simply as suppliers. Partnership is exhibited in:

- **Long-term relationships:** there is a general belief that the best ideas will only be produced if the agency really knows and understands the client's business, and that this can only happen over a period of time from the accumulation of learning, not only in the account team but in senior agency management. It is also more likely that the agency will develop long-running campaigns.

WE PLACE A HUGE VALUE ON PERSONAL RELATIONSHIPS AND THE KNOWLEDGE THAT'S BUILT UP - THERE ARE PEOPLE IN OUR AGENCIES WHO KNOW OUR BUSINESS BETTER THAN OUR OWN PEOPLE.

Marketing

WHEN YOU UNDERSTAND THE BUSINESS, YOUR IDEAS COME WITH RESPECT.

Marketing

It is well recognised that keeping an agency for a long time may result in less creative ideas, but for some this is preferable to too much chopping and changing, and the risks associated with working with a new agency.

SOMETIMES MEDIOCRE CONSISTENCY IS BETTER THAN BRILLIANT INCONSISTENCY.

Marketing

It should be noted that a philosophical commitment to a long-term relationship did not necessarily translate into longer contracts.

- **Openly sharing information:** understanding of the business is accelerated if clients involve the agency early on as strategic partners, sharing financial information, business plans, performance, etc.

HOW CAN WE EXPECT AGENCIES TO PRODUCE THE BEST IDEAS FOR US IF THEY DON'T KNOW OUR BUSINESS?

Marketing

- **Seeking to resolve problems** rather than change the agency: if the general philosophy of the company is 'Don't change the agency unless you really have to', it requires marketing actively to resolve problems. One client had used a mediator to resolve differences that

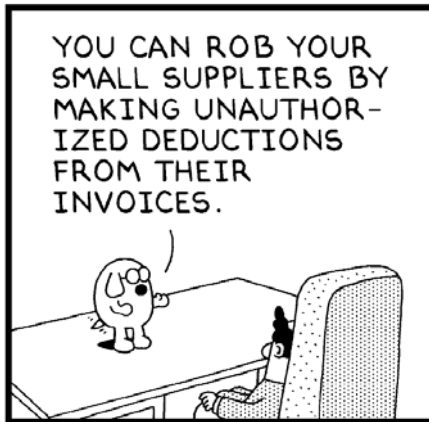
occurred with one of its agencies. Together, they produced a series of personal commitments that people signed up to, and a set of protocols about how to work together. This had worked extremely well.

- **Aligning the agency's remuneration with that of the marketing department:** this incentivises the agency to work to the same goals as the client.
- **Awarding business without a pitch:** best practice marketing understands that pitching is a time consuming and wasteful way of deciding who to work with. Much better is to get to know an agency and work with them to produce the desired outcome.

4.7 Have a constructive relationship with procurement

The degree to which Procurement has penetrated the marketing function varies enormously between companies. In some companies procurement plays no role in marketing, in some it has only recently been introduced, and in others it has been established for some years. In this last group of companies, it is generally well integrated into the marketing function and welcomed for the additional perspective and skills it brings.

Marketing sees procurement's role as being to support marketing by taking responsibility for the *logic* part of the relationship with agencies: this generally includes the contract and fee discussions, clarifying scope of work required, unpacking the agency's costs to make sure Marketing is getting what they want (for example, there's the right balance between creative and planning time), and to ensure third-party supplies are purchased more cost effectively. In some cases the company has a specific 'marketing buyer' who sits in the marketing department, and who reports in to marketing, but with a dotted-line relationship with Procurement. The relationship works best for Marketing where Procurement's Key Performance Indicators (KPIs) are the same as Marketing's – friction is more likely to occur if Procurement are only targeted on reducing cost.



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5

How do the best procurement people contribute to their agencies producing profitable ideas?

The history of procurement's dealings with agencies has generally not been a happy one; in fact, for many agencies, coming to terms with procurement has been a very painful process. Much of this pain was down to agencies themselves. On going into agencies, Procurement found companies that were not well run, not on top of their finances, with little insight into their own business, few principles, some decidedly opaque practices, and in a sector that was oversupplied and highly price sensitive – it was an easy win to pressure agencies on price.

FROM A COMMERCIAL POINT OF VIEW, AGENCIES SEEM LIKE SMOKE AND MIRROR OPERATIONS. THEY'RE NOT WILLING TO BE TRANSPARENT, WHICH JUST MAKES US THINK 'ARE THEY RIPPING US OFF?'

Procurement

It is creative agencies that come in for the bulk of criticism on this point. Through-the-line agencies and media agencies are considered easier to deal with, as their charging policies are more transparent and their performance is more auditable, and media people in particular are often seen as more commercially minded.

Some of the pain was due to Procurement's lack of knowledge of how creative businesses work and so inappropriately applying manufacturing procurement principles to agency services, and also to overly heavy negotiating tactics. However, in recent years, many procurement people have come a long way in marketing knowledge, and have moved from an

adversarial to a more collaborative way of working, and it is this mature approach and attitude that represent procurement best practice today.

From the research, we can identify those characteristics that define best practice in the procurement of agency services:

- They help Marketing deal more effectively with Agencies.
- They help Agencies improve their management and their processes.
- They understand how Agencies create value and their role in it.
- They look for win/win in negotiation.

5.1 Help marketing deal more effectively with agencies

Despite the increase in the number of procurement people who are now involved with agencies, one of the problems they face is a lack of acceptance by Marketing that they can add any value. In the opinion of some marketing people, many procurement people don't 'get' marketing, and they are seen as polar opposites culturally and are therefore antipathetic to each other. Marketing can resent the intrusion of Procurement, seeing their role as simply to cut costs and the result being a spoiling of the client/agency relationship. However, where Procurement has been willing to spend time building a rapport with Marketing, or where there is a dedicated marketing procurement person, they have developed a good relationship, and so are brought in from the beginning rather than simply being called in at the end to negotiate the price down. In these cases, Procurement seeks to add value to the marketing/agency relationship by bringing a more professional approach and mitigating some of the worst excesses of marketing behaviour referred to in the previous section.

CHARACTERISTICS OF SUCCESSFUL PROCUREMENT

- HELP MARKETING DEAL MORE EFFECTIVELY WITH AGENCIES
- HELP AGENCIES IMPROVE THEIR MANAGEMENT AND THEIR PROCESSES
- UNDERSTAND HOW AGENCIES CREATE VALUE AND THEIR ROLE IN IT
- LOOK FOR WIN/WIN IN NEGOTIATION

Particular ways in which best practice procurement contributes are:

- **Disciplines the process:** helps Marketing to specify more exactly what they want from the agency, and holds Marketing and Agencies to agreed ways of working. One example given was in relation to the number of changes that a client was making that resulted in extra cost. Here, Procurement clarified and agreed the number of amends included in a quotation before extra charges were incurred. This meant that the agency was treated more fairly and the client was inhibited from making arbitrary changes, which saved the client cost and time. Procurement can also clarify, simplify and police the approvals process. This can be especially valuable in a company with a complex management structure with many levels of reporting. Procurement can also bring consistency to briefing, especially where the agency is on the receiving end of many different briefs from different parts of a company, and can bring standardisation to contracts, reporting, and the other mechanics of the relationship, all of which can simplify the process.

One way of formalising what is expected of the *logic* part of the agency's work is to put in place a service-level agreement (SLA). This can include deliverables, response times, monthly reports, quarterly review meetings, satisfaction surveys, and so on.

A KEY ROLE OF PROCUREMENT IS TO COACH AND DISCIPLINE MARKETING TO BE MORE SPECIFIC ABOUT WHAT THEY WANT SO THAT PROCUREMENT KNOWS WHAT TO BUY. IT'S NOT THEIR ROLE TO CREATE A SPEC OR TO DEFINE WHAT MAGIC IS.

Procurement

PROCUREMENT IS RESPONSIBLE FOR BUILDING THE BUSINESS-TO-BUSINESS RELATIONSHIP THAT ALLOWS THE INDIVIDUAL PERSONAL RELATIONSHIPS TO FLOURISH.

Procurement

- **Helps Marketing to keep control of the agency.** Sometimes, the relationship between client and agency can get too cosy, and Marketing can feel reluctant to discipline the agency for fear of spoiling the relationship. Procurement can help here by relying more on rational process than on personal relationships, and can have the 'difficult conversations' with the agency that Marketing is reluctant to have.
- **Ensures consistency, rigour, and objectivity in agency dealings.** As has been mentioned above, Agencies sometimes feel aggrieved that they have been treated less than even handedly by Marketing. Procurement's more objective approach to business relationships can help to remedy this, as well as putting in place more formal processes to ensure decisions are taken and judgements made on a consistent basis (e.g. publish agency assessment criteria, formalise review meetings, and so on).
- **Ensures fair treatment for agencies** on such things as prompt invoice payment, performance related bonuses, and honouring contracts.

- **In pitching, Procurement ensures fairness** by limiting the number of agencies invited to pitch; establishing a level playing field (for example by not asking the incumbent to re-pitch if there is no chance of them winning); introducing a more formal assessment process; and ensuring commercial issues are included in the discussions.
- **After the fee is negotiated**, Procurement doesn't disengage, but helps Marketing to measure effectiveness of outcomes by using their analytical skills to develop appropriate processes and metrics, KPIs, targets, benchmarks, and so on. This is another area where Procurement could make a difference: many good intentions by Marketing and Agencies to measure performance fall at the hurdle of finding appropriate metrics.

5.2 Help agencies improve their management and processes

Procurement can bring those same skills of objectivity, analysis and discipline to help the agency improve the *logic* part of the agency process. Procurement can help the agency to introduce good practice, improve the efficiency of their processes, and to negotiate better deals with third parties, supplier management in particular being one area where improvements are judged necessary by Procurement.

PROCUREMENT CAN GET COST EFFICIENCIES FROM JOINT INITIATIVES WITH AGENCIES, FOR EXAMPLE LIKE THE BUNDLING OF SERVICES, AND CAN SUGGEST SMARTER WAYS OF WORKING WHICH WE WELCOME.

Agency

One client, somewhat dismayed at the poor administration and financial procedures in its agency, has put in place a formal service-level agreement (SLA) and a 'relationship manager' to act as an intermediary

between the agency and the marketing client. The manager monitors the agency's delivery of the SLA and co-ordinates between the client's different business divisions, thus making the whole account run more smoothly for both client and agency. This role was instigated by Procurement, but reports in to Marketing; the person's objectives are set jointly between Marketing and Procurement.

Another contribution that Procurement can make is to help agency finance directors get things done in the agency by putting pressure on reluctant agency managements where changes need to be made. In this regard, Procurement are not entirely happy to be cast as the 'bogeyman' in the relationship, but recognise that they can be a powerful lever for change.

In performing their 'consulting' role, helping agencies to improve, it is important that Procurement doesn't step over the line and attempt to run the agency's business. Procurement is entitled to clarity from agencies concerning the client's account content, but the agency view (shared by some client procurement people) is that this should not extend to sharing everything about the business, in particular the salaries and benefits of individual employees.

5.3 Understand how agencies create value and their role in it

Procurement's role in marketing has been relatively recent, and it is not surprising that many procurement people have not been sufficiently exposed to agencies for them to really understand what they are buying. One of the most critical contributions that Procurement can make to 'producing profitable ideas that make profit' is to make the effort to understand how Agencies create value, and Agencies could help by being better at articulating the mechanisms by which marketing communications create value.

GOOD PROCUREMENT PEOPLE UNDERSTAND WHAT THEY'RE BUYING AND WHERE THE VALUE LIES - THIS IS A FUNDAMENTAL PRINCIPLE OF EFFECTIVE PROCUREMENT. IT'S A BIT MORE DIFFICULT TO DEMONSTRATE VALUE WHEN BUYING INTANGIBLES, BUT IT ALL COMES DOWN TO HAVING THE RIGHT PROCESS, POLICY AND PROCEDURES, AND HOW MUCH YOU KNOW ABOUT THE MARKETPLACE.

Procurement

The best procurement people understand that communications is a creative business, and accept that creative judgement often has to be subjective and isn't fully amenable to science. They recognise the difference between the *magic* and the *logic* parts of what an agency does, and understand that the main value lies in the people who do the *magic*, but it's in the *logic* where Procurement can add most value and save cost by tackling waste and inefficiency.

WE ACCEPT THAT THIS IS A RELATIONSHIP BUSINESS AND MARKETING IS RESPONSIBLE; PROCUREMENT ARE BACK-ROOM PEOPLE AND ARE NOT ACTIVELY INVOLVED DAY-TO-DAY.

Procurement

However, Procurement *can* help Marketing to get the best *magic* out of the agency:

WE DON'T SPEND A LOT OF MONEY ON OUR CAMPAIGNS, SO WE HAVE TO CONSIDER HOW TO MOTIVATE AGENCIES TO GIVE US THE BEST TALENT.

Procurement

Best practice procurement respects Marketing's judgement of the creative ability of their agencies and recognises this is not part of their role; doesn't interfere in Marketing's judgement of whether the cost of a creative idea is worth it; takes the view that actual rates paid to agency people are immaterial – what should matter to Procurement is that the client is getting the time of the person they're paying for. In the same way, it is the job of Marketing to judge which is the right agency to choose in a pitch, and it is not appropriate for the choice to be made on the basis of who is the cheapest.

There is also a recognition in best practice procurement that in purchasing agency services, quality of output is important, and quality costs money. Mainly this comes down to recognising that cheap people are usually less likely to produce value-creating ideas than expensive people. The opposite attitude is neatly summed up in this quote from a consultant, who acknowledged that they were exaggerating to make a point:

IF PROCUREMENT RAN LONDON THEATRES, THERE'D BE UNDERSTUDIES ON EVERY NIGHT!

Consultant

Recognising that quality of output is important also means that Procurement respects the agency's quality control role, in particular when considering decoupling of agency services. Where decoupling works best is when the agency is allowed to retain some creative control over suppliers being used.

Another important difference between buying agency services and many other things is that each agency is different – they are not selling commodities but highly individual solutions. One leading agency told of a difficult negotiation with a large client after winning a pitch, where the procurement person said:

IF WE CAN'T DO A SATISFACTORY DEAL WITH YOU, WE'LL GO DOWN THE ROAD AND GET IT CHEAPER AT ANOTHER AGENCY.

Agency

In this context, the practice of benchmarking has become particularly pernicious recently, and only serves to drive down the price of time to an average, thus not acknowledging real differences in quality.

5.4 Look for win/win in negotiation

If encouraging 'profitable ideas' is the objective of most clients, some types of procurement approach are destined to fail. Many respondents (both Agency and Marketing) had bad experiences of dealing with crude bullying tactics from those who have no idea of the value-creation potential of agencies, but who think their job is simply to screw down the price. Similar cases also abound of the mechanistic 'time and motion' type of approach that only looks at the efficiency of the use of time and other inputs, as if the quality or value of an idea can be related to the efficiency with which it was produced. Clearly, in the agency world there are efficiencies to be gained from better processes, but these have to be achieved with due regard to the motivation of clever people and the fragility of creative ideas.

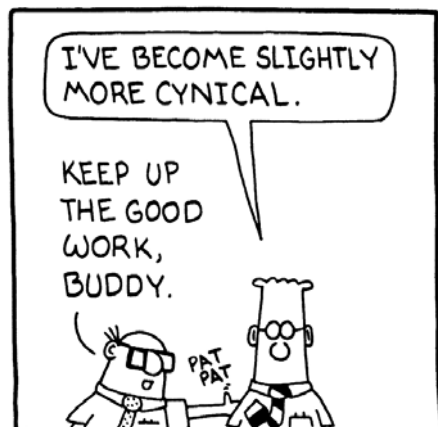
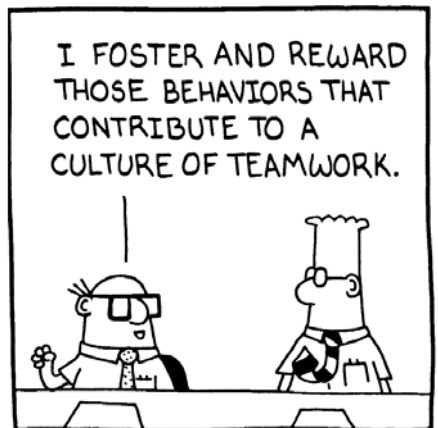
The more enlightened procurement people realise that what their company wants is the best ideas at a reasonable cost, and look for a win/win when dealing with agencies. They respect the agency's ability

to add value way beyond the fee, and they recognise that return on investment is as important as cost, focussing on getting better value rather than just cost savings.

THE GOOD ONES ARE THOSE ATTUNED TO THE BIGGER PICTURE OF WHAT MAKES UP VALUE - LONG-TERM RELATIONSHIPS, SHARED KNOWLEDGE, ADDED VALUE, FAIRNESS, TRANSPARENCY, OPENNESS, A SHARED AGENDA. WE'RE ALL CHARGED WITH GROWING THE CLIENT COMPANY'S BUSINESS - PROCUREMENT KNOW THEY NEED TO WORK WITH SPECIALISTS, MOTIVATE THEM, GET THEIR REMUNERATION RIGHT, FOR THE GREATER GOOD.

Agency

Although there are still many procurement people who see their role in relation to agencies purely as cost cutting, the more enlightened ones are looking for 'quality, value and continuity of supply', and that is a desire shared also by Agencies and Marketing. More transparency and openness from Procurement about their agenda would help.



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6 Key conclusions: what is required for the future?

This report was initiated by a recognition that Agencies, Marketing and Procurement were not working optimally together to deliver profitable ideas (for marketing services agencies) that make profit (for client companies/brands). From the interviews it is clear that this is not true for every client/agency relationship, as I have found many examples where it is working to the full satisfaction of all sides. The agencies and clients that have adopted the best practice processes and behaviours described in this report are showing the way forward to the rest of the industry.

Before detailing what is required of each of the parties to make this positive experience more widespread, two general points are worth making. First, the required behaviours and processes are not rocket science, or indeed at all surprising or novel; they are in fact simple common sense business practice. Second, the parties have a joint responsibility to act in ways that are more likely to produce a win/win; although much of the responsibility falls to agencies to change their approach and practices, agencies cannot create more profitable ideas **for** clients without best practice performance **from** clients. Many respondents, particularly the objective ones, commented that training clients (both Marketing and Procurement) to behave better was at least as important as anything agencies could do on their own.

6.1 Messages to agencies: how to make a profit from producing profitable ideas for clients

Despite being creative organisations, agencies are surprisingly conservative. Many (especially creative agencies) have been slow to

respond to massive changes in their industry brought about by technology (media fragmentation etc.), and to rise to the challenges presented by Procurement and the pressure in client companies to relentlessly reduce costs. The list of consultants employed by clients to audit and advise on the business relationship, working practices, pitches and negotiation, is a measure of the failure of the business to sort itself out. One illustration of this comes from a consultant advising on how to manage the process more efficiently; he has attracted major international marketing companies as clients, but not a single agency has called to speak to him.

AGENCIES ARE STILL REALLY A COTTAGE INDUSTRY IN TERMS OF THEIR MANAGEMENT. IT'S NOT TOO LATE FOR THEM TO CHANGE AND MAKE COST CONTROLLERS UNNECESSARY - THEY DON'T EXIST TO THE SAME EXTENT IN OTHER SECTORS.

Procurement

Fortunately, there is much that agencies can do to improve their situation:

- It is time to nail the industry myth that you have to be chaotic to be creative. Agencies need to run themselves in a more business-like way and to manage the *magic* and the *logic* equally well. Investing more in financial management and administration, and paying more attention to them, would help.
- Agencies need to acquire new skills. Agencies are good at solving clients' problems, but slow to recognise when they need specialist help themselves. Agencies need to acquire new business management skills (for example, in negotiation, project management, management information), and learn from the more professional practices of other sectors.

- More formality of process is needed. The history (for both agencies and marketing) is one of pragmatism, informality and oral tradition, but what is needed now is the adoption of project management skills (for example, describing work flows, how long processes take, identifying hot spots, etc.). Agencies need to formalise their working processes and explain to clients what they do. If Agencies understood better what they are selling, and articulated the value of their activities more clearly, they would find it easier to get paid properly.
- Agencies need to be more accountable for results and place more emphasis on effectiveness and return on marketing investment. If necessary, they should be converting clients who aren't focussed on effectiveness. The whole industry needs to find better ways to articulate and measure how ideas produce profits.
- Resolve to be financially transparent. The lack of trust greatly inhibits a truly productive relationship, and Marketing and Procurement will not trust Agencies fully until this happens. Agencies may need to re-engineer or re-structure their businesses to achieve this. The current dynamic of the financial relationship between agencies and clients could be changed dramatically if Agencies were to take the initiative to save clients money, and asked Procurement to help.

IF AGENCIES WERE VISIONARY, THEY'D LOOK AT HOW IT ALL WORKS, TECHNOLOGY ETC. AND DO IT DIFFERENTLY, VOLUNTEER TO TRY OTHER APPROACHES, INCLUDE PROCUREMENT IN DISCUSSIONS, TAKE THE INITIATIVE TO THE CLIENT, NOT WAIT TO BE SCREWED.

Consultant

- Avoid the trend of decoupling by demonstrating added value. The pressure to decouple some agency activities is a function of three factors: perceived lack of competence, lack of trust about the financial relationship an agency has with its suppliers, and failure on the agency's part to articulate the added value to the client of keeping the agency involved. If Agencies believe that the loss of creative control has a negative impact on the quality of their product, they must find a way to demonstrate it. Marketing would generally accept a well put argument of this nature with regard to photography or commercials directing, but may be less inclined to accept it in the case of print buying or catering. Agencies should recognise that decoupling is seen by clients as a rational decision, based on what's in their best interests. The way forward for agencies is to demonstrate that they have superior knowledge and relationship management skills, which impact directly on the quality of the output, and appropriate negotiation skills to procure third-party service costs effectively for clients. Otherwise they should not be surprised if this role is taken away from them. If Agencies hire their own procurement people, it's important that they have a role in managing supplier negotiation, and actually *do* procurement, rather than being used only on improving internal management. Another option for larger agency groups is to consolidate their purchasing across the group to use their superior scale, as some are already doing.

6.2 Messages to marketing: how to help agencies produce profitable ideas

As has been mentioned above, Marketing can do a great deal to help or hinder agencies in producing profitable ideas for them. It is ultimately in Marketing's own interests to change the way they work with agencies; the rewards are clear for clients who adhere to best practice.

Here are some specific ways in which Marketing can help:

- Aim to develop long-term relationships with a group of agencies selected on the basis of shared values and culture. Long-term relationships bring many rewards for client companies, more commitment from the agency to producing relevant and effective ideas. To maintain longer-term relationships, Marketing needs to find ways of resolving problems without recourse to simply firing the agency, for example, using a 'disputes procedure' or using professional mediation. Similarly, an assumption in favour of a longer-term relationship between the *companies* (as opposed to the *individuals*) would discourage the 'new broom' syndrome so prevalent in Marketing currently.
- Marketing needs to recognise that the more open they are about their business objectives and plans, the better able the agency is to produce relevant insights and ideas, and the more committed they are likely to be to achieving the client's goals.
- More formality is needed in dealing with agencies. Marketing is equally guilty with agencies of favouring a pragmatic, informal approach, but now needs to be better organised and more disciplined in order to allow agencies to work more efficiently. Procurement could help introduce better ways of working, especially in relation to clarity of objectives, briefing, approvals, measurement of results, and agency performance appraisal.
- Marketing needs to be more willing to invest in measuring effectiveness. This means finding budgets to pay for evaluation, being willing to work at finding relevant metrics, and publicising the effectiveness of work throughout the company.
- Resolve to deal more fairly and honestly with agencies. This means for example, ensuring there is a budget set aside to pay the agency for achieving PBR targets, using objective appraisal criteria in

pitches and agency reviews, dealing on equal terms with all agencies on a roster, and so on.

- Ensure remuneration policy is linked to appropriate objectives. Marketing objectives need interrogating more closely if Marketing is to ensure its remuneration policy is aligned with its objectives. There needs to be a ‘reality check’ that the objectives set are achievable, given the market conditions and budget available, through dialogue between client and agency. Provided this is done, both Marketing and Agencies should accept that it benefits both parties to be rewarded against business objectives as well as process management and relationship objectives. Agencies need to be properly rewarded if they are going to hire the best talent to produce the best ideas. Agency fees for the creation of ideas are a relatively small part of the total budget, and savings should be sought elsewhere if the quality of ideas is not to be compromised. If Marketing wants ideas from their agencies that will make a profit for the company, then they need to be more imaginative and flexible about inventing incentives.

6.3 Messages to procurement: how to contribute more effectively to producing ‘profitable ideas that make profit’

In many cases, Procurement’s relationship with Agencies and Marketing can be quite a distant and irregular one; nevertheless they too can be either a huge help or a major hindrance to how well the agency delivers for the client company. Here are some ways they could help:

- Procurement needs to make the effort to understand what they are buying when they buy agency services. This means becoming better informed about the agency marketplace, how agencies work, what they do, and the value of their unique contribution. It also

means appreciating that quality of output and outcome in our industry is highly related to cost, and that return on investment would be a better measure of success than a lower price.

- Procurement needs to be more open about their agenda. Much of the pain that has been experienced by Agencies (and to a lesser extent Marketing) in learning to deal with Procurement has been due to a lack of explanation and openness about the procurement agenda. As has been famously remarked, “A failure to communicate creates a vacuum that will be filled by lies, poison and drivel”, and nowhere has this been more apparent than in Procurement’s approach to agencies.
- Procurement needs to look for ways to work with agencies to help them be more efficient. It is hoped that the *magic/logic* distinction that has been made in this report will help Procurement see that it is in the *logic* part of what agencies do that they can add most value. This is the neglected area in many agencies and one where Procurement’s skills and processes can really make a difference.
- Procurement can similarly help marketing to be more disciplined, which in itself would improve the cost efficiency of the process.
- Procurement could have an important role in helping marketing to find ways to remunerate agencies that will incentivise them to produce profitable ideas.

6.4 The way forward for pitching

It is time for Marketing to lead a move away from the current approach to pitching and to find a better way of selecting agencies.

A huge amount of time and money is spent on pitching, particularly by agencies, but also by clients. Most of this time and money is completely

wasted, and could be reinvested by clients in more productive activities and by agencies in propping up their inadequate profits. Many in the industry believe that there is no alternative to a competitive pitch process where agencies produce ‘the answer’ to a client’s marketing problem in order to win the business, but there are many other businesses that need to select suppliers of original ideas and solutions where much more sensible methods of selection are used. Experienced procurement people could help here, as many have wide experience of purchasing all manner of different services and could contribute other models of pitching for our industry to consider.

No agency in our research has entirely succeeded in moving away from the traditional creative pitch, but several possibilities emerged from our interviews that deserve serious attention by the industry. Here are some thoughts as to how clients could select agencies other than by a full creative pitch, particularly bearing in mind the generally accepted principle that clients are buying people and their experience and skills:

- The agency’s reputation.
- Working meetings with the proposed team and agency management.
- Relevant case studies.
- The agency’s knowledge and experience of the business sector.
- The agency’s process and way of working to produce profitable ideas.
- An analysis of what needs doing to meet the client’s business objectives.
- Critical observations on the client’s marketing strategy, market position etc. from the client’s own research.
- A progressive selection process where, instead of having six agencies do a full creative pitch, six agencies might be asked to present credentials, then four of them go on to present case studies, then two are paid to produce initial strategic and creative proposals, from which one agency is then selected.

6.5 Getting paid for value

Much has been written elsewhere about agency remuneration and this issue was not specifically within the terms of reference of this research. However, it has emerged from the research that the way agencies are remunerated is a key factor in whether agencies are profitable and whether clients get profitable ideas at a reasonable cost. Several respondents stressed the importance of aligning the method of remuneration with the objectives of the parties as each method of remuneration implicitly contains an incentive for the agency to behave in a particular way. Undoubtedly, the good agencies do not feel they get paid fairly for what they do, and this must affect how well they deliver for clients.

IF AGENCIES WERE INCENTIVISED
DIFFERENTLY WOULD THEY WORK HARDER AT
FINDING REALLY BIG IDEAS AND MAKING
THEM WORK THROUGH THE BUSINESS?

Marketing

CHANGING THE PAYING MODEL
COULD CHANGE WHAT AGENCIES DO.

Agency

AGENCIES’ ABILITY TO CHANGE IS
CONSTRAINED BY HOW THEY’RE PAID.

Consultant

The main issue for agencies is how to get rewarded for the value they create.

ONE OF THE BIGGEST FAILINGS OF OUR BUSINESS IS THAT WE HAVE NOT CREATED A MODEL OF REMUNERATION THAT REWARDS VALUE CREATION.

Agency

Not surprisingly, it is less of an issue for clients, who generally believe they should own the Intellectual Property (IP) rights of the agency's work.

WE HAVE SPOKEN TO CLIENTS ABOUT RETAINING OWNERSHIP OF IP RIGHTS, BUT IT'S ALWAYS A VERY SHORT CONVERSATION.

Agency

OUR LOYALTY IS THE REWARD FOR VALUE THE AGENCY PRODUCES; WE HAVE TO PAY FOR THE DUD IDEAS TOO, SO WE COME OUT EVEN IN THE END.

Marketing

If this is to be solved, there is a need for some radical thinking on how to reward agencies for value creation: a few agencies and clients are showing the way. Some of our agency respondents have succeeded in negotiating to retain the IP rights in their work, and licence ideas to clients for a fee on the basis of a tariff for the use of the idea. The tariff is based on geographic usage and media usage and time. The most

commonly mentioned 'model' for this type of arrangement was the way photography is bought. Another approach that agencies have negotiated is to be paid a royalty based on sales. One agency, with a very experienced in-house procurement person, takes a very robust procurement-led stance in contract negotiation that has resulted in several arrangements where the agency owns the IP rights.

WE HAVE TO UNDERSTAND WHAT IT IS WE'RE SELLING. WE KNOW OUR IP HAS VALUE. NOBODY MAKES US GIVE OUR IP AWAY - IT'S OUR CHOICE. WE'VE DECIDED TO SELL IT. WE CHARGE A DIFFERENT AMOUNT DEPENDING ON WHETHER WE KEEP THE IP OR NOT; WE ASK CLIENTS TO DECIDE IF THEY WANT TO PAY LESS AND LICENCE THE IDEA FROM US, OR PAY MORE AND KEEP THE IP RIGHTS.

Agency

These kinds of arrangements seem to be more acceptable to clients when it is for work done by the agency outside of the normal ads or DM pieces. So agencies are beginning to own rights in such things as music, characters, brand names, properties, brand entertainment, content, games, and brand creation.

ONE SOLUTION TO GETTING PAID FOR VALUE IS FOR US TO REINVENT THE BUSINESS WE'RE IN SO WE CAN REINVENT THE WAY WE GET COMPENSATED. THE WAY TO GET A BIGGER RETURN IS TO OWN MORE OF THE OUTPUT.

Agency

However, one issue highlighted is that the way the agency is positioned in the client's eyes can determine how they are paid. For example, Agencies often create names for new products in the course of creating communications ideas; if a naming agency had been employed, they would have been paid for the idea, but because it came up as a part of a different brief, the idea was just 'given away'.

In digital agencies the situation is somewhat different, as here it is normal for the agency to retain ownership of the software IP used to create a website, and so they can re-use the 'Code' for other purposes (e.g. games design).

These examples show that the remuneration model can be changed. The challenge for agencies that want to own the IP rights in their work is to find the arguments and to stand firm in their negotiation.

The issues around rewarding agencies for value are different for clients than for agencies, and mainly revolve around budgeting and metrics. Some clients could accept the principle of paying agencies for the value of outcomes (rather than paying for the cost of inputs or outputs) if they could find ways to solve the 'annual budget problem'.

THE LOGIC OF HOW AGENCIES
SHOULD BE REWARDED IS EASY. THE
PROBLEM IS THE ANNUAL BUDGET
SETTING ROUND AND HOW TO FIND
A BUDGET TO PAY AGENCIES OUT OF.

Procurement

The other hurdle to be overcome is being able to demonstrate how the agency's output relates to the client's bottom line. The industry needs a clear model of how this works in theory, and better metrics for evaluating specific campaign effects.

6.6 Messages to industry bodies: CIPS, the IPA and ISBA

As has been mentioned above, the responsibility for improving relationships between Agencies, Procurement and Marketing is a joint one, and there are some things that individual clients or agencies cannot do on their own. CIPS, the IPA and ISBA should consider how they might support their members in making these changes, particularly through joint initiatives that encourage the parties to work more closely together.

Appendix I

Some signature practices of the most profitable client/agency relationships

In sections 2, 4 and 5 we looked at the broad areas of philosophy and attitude of best practice agencies, marketing and procurement. Typically, these are supported by many detailed practices and ways of working and below we show some of these ‘signature practices’.

1: Financial processes

Up front

- Basis of contract terms and budgets is discussed before the pitch, but agency does not submit remuneration proposal before scope of work is determined (or before the pitch even!).
- Broader team is actively involved in fee negotiation (agency FD, agency procurement, client procurement etc.).
- Scope of work/deliverables that the fee relates to is discussed in detail before contracts are drawn up.
- The resources that the fee relates to are tightly defined: team, skills, time allocated, what’s billable, what’s included (number of iterations, policy on rework, level of finish of creative/presentation materials).
- Agency uses a formal written document to describe to Procurement the agency’s approach to money. Transparency over how fees/costs are arrived at.
- Define metrics for agency performance measurement and for outcome measures relating to PBR.

Ongoing relationship

- Hold quarterly client/agency reviews of financial status.
- Have good time-management systems. Time sheets (where used) are completed accurately and on time. Keep accurate records of time spent (if basis for fee) and other costs so able to justify requests for extra fees.
- Review account profitability regularly and share with account team; motivate group directors to ask for more from clients where justified (results in less write offs). Share agency financial performance with staff.
- Are business-like in day-to-day financial dealings with clients: give precise estimates of costs to clients in advance; define grounds for increase or decrease in fees and give detailed breakdowns; are not reticent to ask for extra fees where they are justified; raise fee/cost issues at earliest opportunity.
- Are efficient at maximising revenue. Efficient at invoicing and debt collection. Bill all billable expenses; in some cases bills all expenses e.g. phone calls.
- Treat Procurement as an integral member of the client/agency team. Involve Procurement in negotiation with third parties, or willing to discuss 'decoupling' certain activities.
- Take the initiative to save the client's money. Negotiate effectively with third parties to minimise costs to client and merchandise the savings made to clients.

2: Work flow/management of the agency process

- They have documented processes.
- Agency doesn't start work till there's a signed contract.
- Agency doesn't start work until there's a clear client brief.
- Define approvals process: who involved, time needed for decisions, requirement for research, agree criteria up front (avoids major wastage by clients).

- Senior clients involved at early stages of creative development; work collaboratively, not the 'big reveal' at the end.
- Define roles of all parties involved (agency and client) to avoid overlap and conflict.
- Assign staff flexibly to the task (not a 'one size fits all' structure), resources applied to a job are managed/controlled, best people are put on top clients (aligning resources with customers).
- Clear about what level/grade of staff are assigned/paid for (not FTE's) – show what value the client is getting from a specific individual, their skills, experience etc. Each individual has his or her own rate.
- Implementation/back-office processes have been analysed for efficiency.
- Use technology to speed up process/save time/create efficiencies e.g. for online approvals, doing production work overseas where it's cheaper, sharing creative work internationally, using video conferencing.
- Involve media early to build in their ideas from the beginning, not at the end.
- Hire own procurement people to improve agency's internal processes and to better deal with Procurement; in-house lawyers to help with contracts etc. – professional support.
- Creative work is at the heart of the agency, but impose discipline on creative people to mitigate their tendency to over spend the client's money (e.g. arguing for a 60-second commercial over a 30-second, but with no rationale; not finding out a celebrity's availability for a campaign before presenting it – wasteful and annoying).
- Run training programmes and workshops to ensure the rest of agency is commercially aware.

3: Creating and demonstrating value: processes for producing quality outputs and outcomes

- Have people-management processes: six-monthly reviews for all staff, objectives, training, what's expected of people.
- Client briefing: insist on clear objectives (quantified), insist on clear understanding of the client's business.
- Build in processes for ensuring effectiveness.
- Keep records of past campaigns, case histories of results.
- Can articulate value to Procurement; uses case histories and examples to show how value is created, how much time it takes to produce ideas etc.
- Support Marketing in defending budgets and demonstrating the value of advertising. Give Marketing the tools to justify agency selection to bosses: agency processes for creating value, clarity over desired outcome, how success will be measured, etc. (the agency should develop these kinds of accountancy/management consultant skills).

4: Client/agency relationship

- Hold regular formal reviews of work and relationship (360 degree preferably), what worked, what could have been better – the aim is continuous improvement.
- Regular client/agency reviews are ideal, but it can be hard for agencies to raise issues; one agency has been experimenting with an external auditor/mediator to find out the truth of the relationship and identify priorities for action.

Much of the above is internal to the agency management, but those processes that are seen by the client, give clients confidence that agencies are managing the process properly and spending their money wisely.

Appendix II

How profitable are agencies?

To put the findings of the research in context, it is useful to take an objective look at how profitable agencies are in fact. This analysis is produced by Willott Kingston Smith (WKS), which is an accountancy practice specialising in providing financial and management advice to creative, communications and consultancy businesses. It is part of Kingston Smith, one of the Top 20 firms of chartered accountants in the United Kingdom, and has a client base of over 200 advertising agencies, media buyers, public relations consultancies, direct marketing and sales promotion houses, as well as branding and design consultancies.

Each year, WKS publishes a survey of the financial performance of Marketing Services Companies, focusing primarily on the Top 50 Marketing Services Groups in the UK. All the financial data used is drawn from audited accounts filed at Companies House or, in some cases, supplied to WKS direct.

For the purposes of the Value Framework Initiative we have focused on those sections of the WKS report relating to advertising agencies, media independents, and direct marketing companies.

1: Key Performance Indicators for financial success

WKS, in their annual review of agency performance, identify four main indicators for good financial performance:

Operating profit margin: this is the operating profit expressed as a percentage of gross income. It reflects how effectively a business turns revenue into profit, and will be influenced by how much a business can charge for its services, how efficiently it provides them and how well it controls operating costs.

Gross income (not turnover) per head: a measure of the productivity of employees. They note that in recent years the revenue line has been squeezed by pressure from Procurement on fees and discounts/mark ups. The most important ingredient in achieving profitability is to get the headline price right (i.e. initial remuneration).

Employment costs – gross income: a measure of whether there are too many people or salaries are too high; a key ratio showing the number of people servicing the income and what they are paid. To keep this within bounds, managements have to resist upward pressure on salaries and a tendency to be overstaffed. The ratio should be segmented into the costs of those adding value and those servicing the business. Some agencies are attempting to keep more of their employment costs variable by using freelancers and introducing performance related pay as a means of dealing with the variability in income produced by PBR.

Operating profit per head: a measure of how productive employees are and how efficiently costs are managed.

2: What does good performance look like?

According to WKS, good performance for a marketing services company on each of these KPIs is:

Operating profit margin of 15–20%

(35 agencies out of Top 50 did not achieve this)

Gross income per head of over £80,000

(27 agencies out of Top 50 did not achieve this)

Employment costs: gross income of 50–55%

(34 agencies out of Top 50 did not achieve this)

Operating profit per head of over £10,000

(28 out of Top 50 agencies did not achieve this)

Clearly, on the basis of this data, more than half of the Top 50 UK agencies are making less than adequate profits.

Some characteristics of more profitable agencies

From the WKS survey, some characteristics of the more profitable agencies emerge.

Consistency: outstanding agencies have produced consistently good performance that has endured through substantial changes in agency size, client list, structure, etc.

Growth: faster growing agencies tend to be more profitable because most of their costs (people and office space) lag their revenue. However, whereas income tends to grow steadily, costs tend to go up in steps: bigger premises, additional functions (e.g. HR), etc., so even a successful agency's performance can be inconsistent. It is harder for bigger, slower-growing agencies as they tend to have many more older, more senior, expensive people as the business matures, which can be a problem if the bigger clients are not willing to pay for experience.

Cost base: agencies that reported better profits last year had reduced their cost base, especially their non-employment costs. Regional agencies have the highest average profitability per head because they have lower overheads, but they also tend to be more through the line and diversified and so can ride out recession better.

Client list: fewer bigger clients are more profitable than many smaller ones, as the costs of servicing are proportionately lower.

3: Differences by agency type

The WKS survey also identifies some differences by agency type.

Media agencies: traditionally have made higher margins, partly because of the nature of the business, but also because media agencies tend to be more commercially aware and more financially focussed than creative agencies.

Integrated and digital agencies: tend to make higher margins as they are fast growing, more project based, owner managed, and more diversified in their activities.

Independent/owner managed shops: tend to be more profitable than big international group agencies: they do not have to work on unprofitable group clients, they have more freedom to refuse or resign business, owner managements are more entrepreneurial by nature and more committed, and they are closer to the business and so managed more tightly.

Larger/international groups: are constrained to take on accounts regardless of their profitability, have to service accounts at a price decided elsewhere, and cannot walk away from unprofitable business, though they can 'engineer' revenue around the group. Financial performance can be improved by winning 'independent' business. A recent trend in international groups is to have a smaller number of core offices rather than complete world coverage, which reduces overheads and the cost of servicing business significantly.

Appendix III

Organisations interviewed

Clients:

Coca-Cola
Diageo
Eurostar
COI
Honda
Tesco
Unilever
Vauxhall
Zurich Financial Services

Agencies:

23red
Agency Republic
AMV.BBDO
Bartle Bogle Hegarty
Fallon London
krow
Leo Burnett
Lowe London
Mother
Proximity
Young & Rubicam Group
ZenithOptimedia

Consultants:

Agency Assessments
MSC
White Door Consulting
Willott Kingston Smith

Appendix IV

About the Value Framework Steering Group

The Value Framework Initiative was launched in September 2004 by CIPS, the IPA and ISBA. It had an ambitious purpose: to improve professionalism in ways of working between all three memberships, through the development of an industry framework for relationship management and contract negotiation. The Value Framework Steering Group was formed in October 2004 and held its first inaugural meeting in January 2005. It has met quarterly since, rotating both meeting venues and chairmanship to fairly represent the interests of all three parties. Membership of the Steering Group is by the invitation of the whole group. Current membership includes:



The Chartered Institute of Purchasing and Supply (CIPS)

www.cips.org



Ian Taylor

*Director, Centre for Procurement Performance,
Department for Education and Skills
Former President, CIPS (2005)*



Alison Littlely

Global Marketing Procurement Director, Diageo



Michael Campbell

Director of Business Development, CIPS



Gerard Chick

Head of Knowledge Management, CIPS



Institute of Practitioners in Advertising (IPA)

www.ipa.co.uk



Jerry Hill

*Group Chief Executive, Initiative
Chairman, IPA 5 Year Plan Forum*



Jane Asscher

*Chairman and Managing Partner, 23red
IPA Council*



Hamish Pringle

Director General, IPA



Janet Hull

Head of Marketing, IPA



Jossy Elvidge

*Marketing Planning Assistant, IPA
(Secretariat support)*



Incorporated Society of British Advertisers (ISBA)

www.isba.org.uk



Nick Smith

*Chairman, Marketing Society
ISBA Council*



Simon Thompson

*European Marketing Director, Motorola
ISBA Executive*



Peter Buchanan

*Deputy Chief Executive, COI Communications
ISBA Executive*



Debbie Morrison

Director of Membership Services, ISBA

About the author



Marilyn Baxter has spent over 30 years in advertising planning and research. She recently retired as Chairman of the advertising research specialists Hall & Partners, and before that spent 15 years at Saatchi & Saatchi, where she was Vice Chairman and Executive Planning Director. Currently she is a Non Executive Director of the COI.

Whilst in the advertising industry, Marilyn served on the IPA Council and was Chairman of the Value of Advertising Group. She is a frequent writer and speaker on the advertising industry, research and planning, and was the author of the first IPA report on 'Women in Advertising'. She is a Fellow of the IPA, a full member of the Market Research Society, and an honorary member of the Account Planning Group.