

# What we think

## After the threat of apocalypse, new centres of gravity

WPP CEO Sir Martin Sorrell reports

**I**t's an acronym, but one that carries more than a little truth. The expression 'L-U-V' was coined\* to describe the way the world's regional economies would pull out of recession, but it serves equally as a reminder of where we are going. It works like this – a flatter 'L' or italic 'L' for Western European growth, a speedier 'U' for the US and a sharper, more rapid 'V' for the BRICs nations and the Next 11 as identified by Goldman Sachs. The letters approximate the fragile recovery of 2009 – very much a year of two halves – but also the shape of things to come, as the planet's economic tectonic plates shift into a new pattern. With apologies to Paul Young, LUV is in the air.

Over a quarter of a century, WPP's strength has been our ability to identify trends and capitalise on them for our clients and ourselves. It's how we began with two people in a room all those years ago. It is how we have weathered the recent crisis. And it is how we will position WPP for sustained growth in the years ahead – albeit with nearly 100,000 people directly with us, access to over 138,000 and rather more rooms than we started with.

\* By Stella Dawson of Thomson Reuters in July 2009.



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Boys

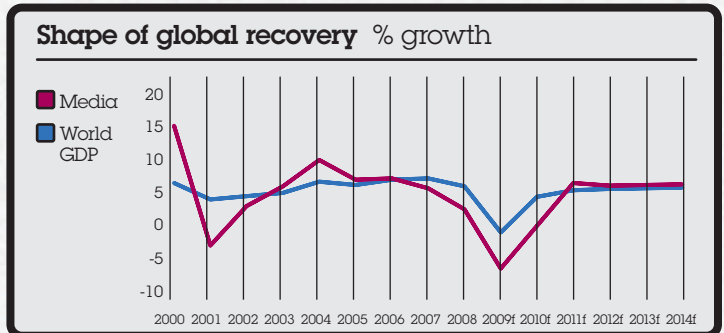
the bond ♡

## What we think

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It is essential that we identify geographic, functional and technological changes and adjust our business to make the most of them. For that reason, we expect the balance of our work to move from the 'L' shape of Western Europe and other established, slower-growing economies towards the 'V' of dynamic new markets. They include China with its possibly 1.5 billion and rising population, along with India and the other BRICs nations, Brazil and Russia – not to mention the Next 11.

The process is unstoppable. Cynics can no longer argue that the inevitable power shift from West to East is just about cheap labour and low-cost manufacturing. Indeed, the old assumption that China and India will remain mere makers of cheap generic goods could prove life-threatening. Both countries are cultivating their own global brands and service



Sources: IMF; GroupM  
f: Forecast.

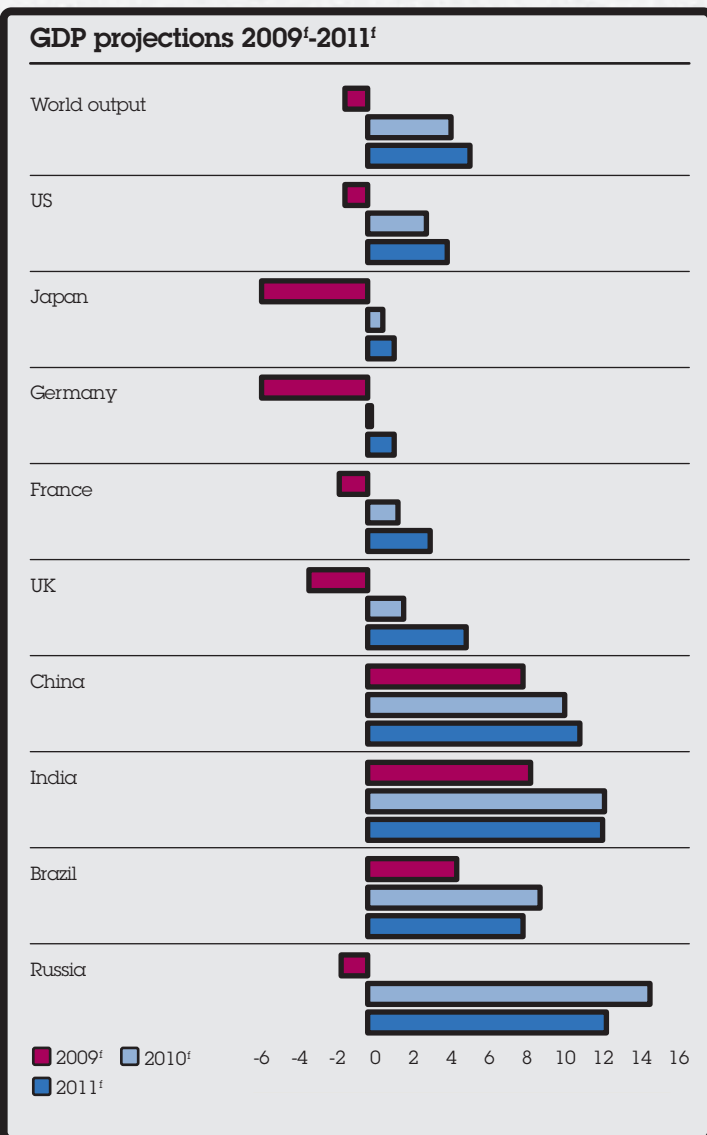
industries and they will be as good as anything the West can muster. After all, we used to say the same thing about Japan or Hong Kong.

Fortunately, WPP has leadership or near-leadership positions in all these countries (other than Iran, one of the Next 11), a position we will maintain. In India, for instance, we have a substantial market-leading share and in Greater China a market-leading share, making the latter WPP's fifth largest market already after the US, UK, France and Germany. That can only grow as the global financial crisis fades.

Other changes are remaking our world. Of these, the most important is the continuing expansion of those parts of our business that sit outside traditional advertising. More of our work will be in marketing services, the so-called below-the-line areas such as Consumer Insight, Public Relations & Public Affairs, Branding & Identity, Healthcare and Specialist Communications – particularly direct, interactive and internet communications. Public Relations & Public Affairs, also, can expect a prosperous future as its traditional skills – building relationships and influencing opinion-formers – are brought to bear on the new internet frontiers of blogging and social networking. These shifts in the balance of our business are inevitable as audiences fragment, the costs of television airtime continue to fluctuate, gadgets like the iPad or e-readers change media consumption habits and – most importantly – as the internet's reach extends, promising more measurable, predictable results.

Understanding what will keep our clients awake at night in the 21st century is crucial. Overcapacity in almost all areas of manufacturing – too many cars still chasing too few customers, for example – casts a cloud over prospects, forcing discounting and a profitless prosperity on key industries. This was true before the credit crunch; it is all the more so now.

Clients are equally troubled by the dominance of global retailers and the consequent pressure on prices. Some companies rely on sales in Walmart stores for a large part of their turnover. These sales may be crucial to the company, but for Walmart the numbers may be no more than a rounding error. Understanding of distribution and retail is crucial for survival.

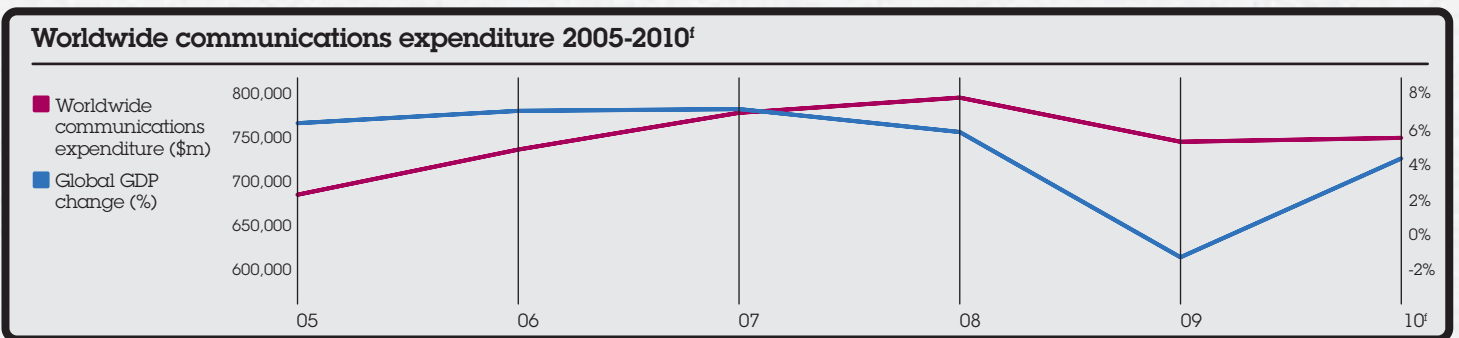


Source: IMF  
f: Forecast.



Worldwide communications services expenditure 2009<sup>1</sup> \$m

	Advertising	Market research	Public relations	Direct & specialist communications	Sponsorship	Total
North America	155,797	8,582	3,589	82,437	16,790	267,195
Latin America	24,307	1,750	300	21,000	3,500	50,857
Europe	123,885	15,000	2,350	85,920	12,100	239,255
Asia Pacific	126,818	4,300	1,010	31,156	10,100	173,384
Africa, Middle East and Rest of world	13,802	–	–	–	1,900	15,702
<b>World total</b>	<b>444,609</b>	<b>29,632</b>	<b>7,249</b>	<b>220,513</b>	<b>44,390</b>	<b>746,393</b>



Source: GroupM

f Forecast.

<sup>1</sup> Estimate.

Revenues cited here represent an estimated 80-90% of the worldwide market. Estimates exclude certain unmeasured trade/consumer promotional expenditures and very early stage economies.

Internal alignment is another essential as global companies react to new markets in the East and stagnant economies in the West. Getting everyone in a company facing the same way, working for the same vision, is key. As the geography changes, so will old-fashioned management structures. Regional silos can expect a shake-up and local managers, sensitive and knowledgeable about their local markets, may well come to the fore again. Consolidation also poses threats and opportunities to our clients – and is changing our industry with the rebirth of superagencies or full-service agencies and changes in the way we structure ourselves to meet companies’ needs.

Large clients are increasingly looking to parent or holding companies that draw on the strength of their individual subsidiaries to present integrated solutions to their marketing needs. We are winning such pitches. All this dictates that hiring and retaining the right talent will remain crucial for us and our clients. And here is a paradox. It is almost as if the shortage of human capital runs in inverse proportion to excess manufacturing capacity. People and skills are always crucial.

Corporate responsibility is another concern for clients – although in truth a no-brainer. Only those seeking a fast

buck and subsequent oblivion would surely think otherwise. While globalisation, free trade and scientific advance, within reasonable environmental and social constraints, will still be the most efficient way of enriching the most people in the world in the fastest time, the current economic crisis underlines the importance of corporate responsibility and responsible consumption.

Where 2009 was a very, very tough year, 2010 has already seen stabilisation, if not growth, perhaps only because of the massive amounts of money – \$13 trillion and counting – pumped into the system one way or another. Most of that money has come from governments, who because of this increased spending have themselves become major clients for us.

In uncertain times, branding or differentiation and innovation – essentially, what we do – are everything. The first requirement is always a brilliant idea. Then you need co-ordination. Without the first, however, the second is pointless. You can’t, after all, co-ordinate a lousy idea. So creativity and imagination win every time. There is a limit to how much you can cut costs; there is no ceiling on innovation.

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### Tough times, but market share will increase

Although 2009 was an extremely challenging year, the Company responded well, particularly in the second half. That was all the more gratifying, given that 2009 had none of the maxi-quadrennial stimulative events of 2008. That year was a record in terms of billings, revenues and profits, bolstered by a summer Olympics, a European football championship and an American presidential election. Neither did 2009 have the mini-quadrennial events of 2010 – a winter Olympics, a FIFA World Cup, or mid-term US Congressional elections, not to mention the Shanghai Expo and the Asian Games in Guangzhou.

Overall, in 2009, spending on worldwide communications services – advertising and marketing services – shrank by 6.3% to \$746 billion from an actual spend of \$797 billion in 2008, based on more rigorous data now available to our Media Investment Management parent company, GroupM. WPP's market share stood at nearly 10%. Given the continued economic pressure, the industry will probably remain flat in the current year. GroupM forecasts a small 0.8% rise in advertising, which now accounts for approximately 40% of our business. GroupM also forecasts a 0.3% increase in marketing services, which affects the other 60%. Relatively flat revenues this year thus mean increased market share.

As a proportion of worldwide GDP, communications services probably stayed constant in 2008, falling again in the sharp recession of 2009. Neither 2010 nor 2011 will be easy years, particularly in the 'L'-shaped economies of Western Europe, where it is likely to be a slog, but we believe WPP is well placed to make the most of it. On the following pages, we explain why.

### The compass changes direction

Nothing is constant. The way the world – and our industry – does business is changing as its economic centre of gravity shifts. The US has hitherto accounted for about half of worldwide advertising and marketing services spending, with the most prominent non-American markets being Japan, Germany, the UK, France, Italy and Spain. Now Asia Pacific, Latin America, Africa, the Middle East, and Central and Eastern Europe are becoming more and more significant. This will continue as multinational corporations build their businesses where populations are large and growing faster – seeking to drive top-line like-for-like sales growth, a primary driver of total shareholder return. Even Cuba, with a population of 11 million, may become an opportunity. And also perhaps in due course, if political differences are overcome, Iran with more than 70 million people.

Goldman Sachs, which first identified the BRICs nations – Brazil, Russia, India and China – now focuses on the

Next 11 – Vietnam, Bangladesh, Indonesia, Iran, Mexico, Nigeria, Pakistan, the Philippines, Turkey, South Korea and Egypt. WPP has leadership or near-leadership positions in nearly all these countries.

Latin America, Africa and Central and Eastern Europe, while impacted by the global downturn, remained our strongest-performing regions. Pakistan, with a population of 174 million, Vietnam with 88 million and Indonesia with more than 230 million – of which 200 million are Muslim – also remained faster-growing markets and became even more influential in 2009. Extrapolate WPP's current revenues in the BRICs countries (despite the currency challenges in Russia) or BRICI (including Indonesia) at the rates of GDP growth predicted in recent Goldman Sachs research and assume moderate rises in advertising to GDP ratios. The result is that Asia Pacific, Latin America, Africa, the Middle East, and Central and Eastern Europe will take a growing share of our business: probably 34% by 2015, excluding acquisitions.

Currently, China and India are home to more than one-third of the world's population. Asia Pacific represents half. By 2014, Asia Pacific will account for more than two-thirds. WPP already has a strong position in the region. Greater China is WPP's fifth-largest market, in which we have a significant advantage over our competitors. In India, our market share is very significant, with a similarly significant market share in South Korea. In Japan, it is almost 10%, behind both the dominating although challenged Dentsu and Hakuhodo DY Group.

There is no doubt the marketing world is becoming two-paced or even three-paced, geographically and functionally. Asia Pacific, Latin America, Africa and the Middle East, and Central and Eastern Europe are outpacing the US and Spain (post-Franco Spain was a standout market in Western Europe, although the current real estate bubble has laid it low). In turn, the US and Spain have been outpacing the rest of Western Europe.

Such shifts are not new. At other times in history, when a country or empire seemed to have total political, social or economic hegemony, as the US has, things changed and the vacuum was filled by another power. China and India will take that role, in the context of the growth of Asia Pacific. They are already enjoying their new stature. Over the past few years at the World Economic Forum in Davos, the Chinese and Indians exhibited a greater degree of self-reliance and independence – perhaps even over-confidence. Both are now quick to blame the US for the recent crisis. Both no longer seem to rely on handouts or support. Both have reached or are reaching a size and rate of growth that may be self-sustaining and certainly more independent of US influence. Both now believe they have little to learn from the nations that got us into this economic mess in the first place.

While decoupling has not, in our view, arrived, there is probably less coupling. But as the credit crunch demonstrates,



### The 30 largest companies in the world\*

Rank	Company	Country	Market value \$bn
1	Exxon Mobil	US	325
2	Industrial & Commercial Bank of China	China	271
3	Microsoft	US	266
4	Ezdan Real Estate	Qatar	259
5	BHP Billiton Limited	Australia	226
6	PetroChina	China	225
7	Apple	US	219
8	Wal-Mart Stores	US	207
9	China Construction Bank	China	207
10	China Mobile	Hong Kong	205
11	Berkshire Hathaway	US	199
12	General Electric	US	198
13	BHP Billiton PLC	UK	196
14	Bank of America	US	186
15	BP	UK	185
16	Royal Dutch/Shell Group	Netherlands	185
17	HSBC	UK	185
18	JPMorgan Chase	US	183
19	Procter & Gamble	US	182
20	Google	US	180
21	Johnson & Johnson	US	179
22	Petroleo Brasileiro SA – PETROBRAS	Brazil	174
23	Nestlé	Switzerland	172
24	Wells Fargo	US	167
25	International Business Machines	US	167
26	Chevron	US	160
27	AT&T	US	156
28	Cisco Systems	US	152
29	Vale S.A.	Brazil	150
30	Rio Tinto	Australia	145

Source: *CorporateInformation.com*  
 \* Market values as at 9 April 2010.  
 (Figures rounded up to nearest billion.)

problems in America still exert a powerful influence on the rest of the world. On my most recent trips to Shanghai, Beijing, Mumbai, Bangalore (first time) and New Delhi, many Chinese and Indian companies with national and overseas ambitions appeared much more assured and less over-awed by the capabilities of Western competition. In the past they listened and learned; it clearly has paid off.

We will probably still rely on the strength of the US, but increasingly we will see the growth of Asian-based multinationals. Not only Japanese-based multinationals like Sony or Mitsubishi, or South Korean-based chaebols such as Samsung, LG or Hyundai (the Samsung of the car industry), but also Chinese multinationals such as Lenovo, Haier, Konka, Bird, Bright Dairy, China Mobile, China Unicom and CNOOC. Four of the top 10 companies in the world

by market capitalisation are already Chinese. Consider also Indian multinationals such as the two Reliances, Tata, Wipro and Infosys. The last's headcount has grown from 25,000 to 105,000 in the past five years and shows little sign of slowing. There is no shortage of eager candidates: Infosys still receives more than one million applications for jobs each year.

No longer a maker of cheap, generic goods, China will increasingly become a service-based economy. In 2005, the mayor of Shanghai asked the 55 CEOs on his International Business Leaders Advisory Council to suggest how Shanghai might become the world's leading services centre. In 2006, the focus was on innovation, 2007 on climate change and planting trees in Shanghai, 2008 reviewing 20 years of progress in Shanghai and releasing sturgeon into the Yangtze River. In 2009, the CEOs reviewed the lessons of the past 20 years of the Mayor's committee (amazing when you think the mayor has been calling for advice for 20 years) in preparation for Shanghai Expo and WPP will be holding one of its 2010 Board meetings in Shanghai later this year around the Expo. Similarly, India will seek to be a manufacturing centre for the world and not just focused on services. Who would have thought that Ratan Tata would buy Corus, the re-branded British Steel (the name created by one of our Branding & Identity companies), or that the underbidder would be a Brazilian company? In addition to Tetley Tea, Tata also acquired Jaguar and Land Rover at the top end of the car industry. At the bottom end, it launched the Nano last year at 100,000 rupees (\$2,500) – the cheapest car in the world. And most recently, Geely, the Chinese car manufacturer, acquired Volvo from Ford.

### Here – and here to stay

Understandably, the West has difficulty grasping the scale and complexity of Asia Pacific's potential development. China is, after all, not just one country; it consists of more than 30 provinces, with so many languages and dialects that even Mao Tse Tung had to take an interpreter when travelling. Incidentally, the population may well be closer to 1.5 billion rather than 1.3 billion. The Chinese government consistently seems to underestimate its statistics, like those for GDP growth, but, whatever the true figure, it is still equivalent to four or five Americas. Likewise, India's 1.2 billion plus population covers 27 states.

Of course, only 200-300 million Chinese can currently afford the goods and services being marketed to them, but even this is already almost equivalent to all of America and is a dynamic situation, one that will change rapidly in the coming years. There are over 700 million mobile phone subscribers in China. Of those, over 500 million subscribe to one company, China Mobile (one of the top 10 most valuable world brands) – equivalent to more than one and a half times the population of the US.

## What we think

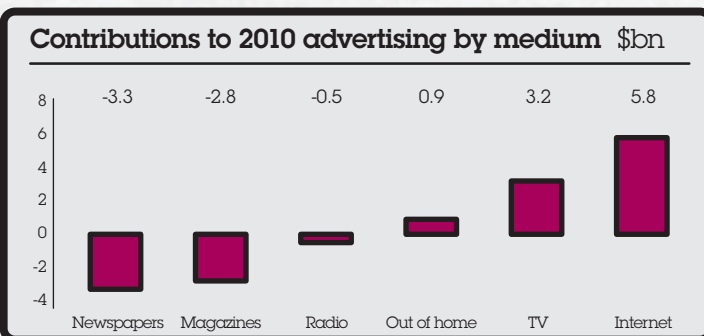
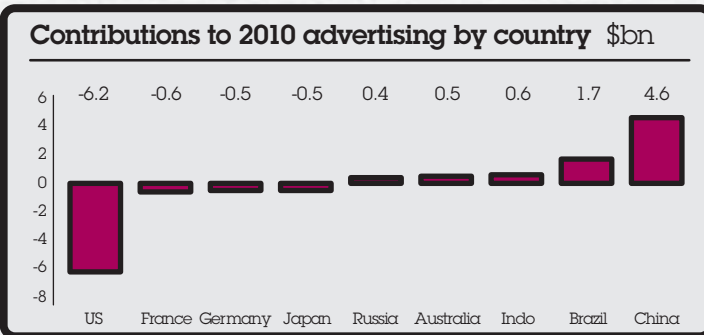
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### BrandZ™ Top 20 risers 2010

Year-on-year brand value growth

Rank	Brand	\$m Brand value	% Brand value growth
1	Samsung	11,351	80%
2	Baidu	9,356	62%
3	MasterCard	11,659	57%
4	Next	2,569	54%
5	Visa	24,883	52%
6	HP	39,717	48%
7	Verizon Wireless	24,675	39%
8	Apple	83,153	32%
9	IBM	86,383	30%
10	Amazon	27,459	29%
11	Goldman Sachs	9,283	25%
12	HSBC	23,408	23%
13	O <sub>2</sub>	10,593	23%
14	Skol	2,722	22%
15	Corona	5,196	21%
16	Evian	907	21%
17	Budweiser	15,991	20%
18	T-Mobile	13,010	20%
19	Barclays	8,383	20%
20	VW	6,994	20%

Source: Millward Brown Optimor (including data from BrandZ, Datamonitor and Bloomberg)



Source: GroupM

Furthermore, India, itself equivalent to three to four Americas, seems to have been stimulated into more rapid growth, driven perhaps by neighbourhood envy and the Chinese model of state-directed capitalism – although India bills itself as the world's fastest-growing democracy. Look at the dogfight for the Indian phone operator Hutchison Essar, which Vodafone won in a market growing now by 15 million subscribers a month, even more than China at eight million a month. There are now 540 million subscribers, with Airtel having 124 million and Reliance and Vodafone having around 100 million subscribers each.

This really is back to the future. In 1820, China and India generated around 49% of worldwide GDP. But by the early 19th century, Meissen and Wedgwood were undermining the high-quality, high-price Chinese porcelain industry with similar quality, but cheaper products. It is the exact reverse today. China and India are heading for the same share of world GDP in 2025 that they had in the 18th century, having bottomed out at 8% in 1973. China's development has been rapid and will continue, but not without bumps. The government is conscious of overheating, and an imbalance in rates of development between the coast and the hinterland. There has, it is true, been a slowdown in 2008 and 2009, but the recent Party Congress has set an 8% target for GNP growth in 2010. Fears of social unrest will push the government to implement more fiscal stimulus if necessary.

Evidence of China's arrival on the world stage is everywhere – its confidence at Gordon Brown's G20 summit last year, President Obama's low bows to the Chinese leadership and, most visibly, the Beijing Olympics. Few self-respecting multinational companies bent on expanding into China or national companies seeking to grow inside or outside China missed out on the branding opportunity presented by Beijing 2008. The Chinese government committed \$45 billion of investment around the Games, in contrast to London's \$14 billion for 2012. Beijing was a whopper but it will not end there. The Municipality of Shanghai is investing \$3 billion in Expo 2010 and there will be the Asian Games, in Guangzhou, this year.

Watch out for increasingly subtle Chinese military and economic influence, too. Take the recent economic contact with Fidel Castro in Cuba to counterbalance Taiwanese tensions. Or Chinese investment in Galileo's GPS systems, which drew a coruscating response from the Pentagon. Equally, Beijing will not be prepared to rely on America to defend its vital and growing energy supply interests in the Middle East and Russia, as its recent energy deal with Russia showed. It is busily building trade bridges throughout the oil- and energy-producing regions of the world, particularly Latin America and Africa.

It is in Africa that China is changing trade relations, with more than 800,000 Chinese reportedly participating in projects there. Increasingly, Africa is the continent of opportunity, rather than war, disease and poverty. President



Muammar Gaddafi's volte face has energised North Africa and Egypt, and China's focus has drawn the attention of Western governments seeking to curry favour, too. We at WPP have invested in Smollan and The Jupiter Drawing Room in South Africa and Scangroup in Central and North Africa. In Africa, as well as China, sport plays a symbolic role. The 2010 FIFA World Cup in South Africa is an iconic event for the African continent and one in which our agencies dominate.

There is another challenger to American dominance – the Muslim world. Already, Muslims number 1.6 billion people or a quarter of the world's population. By 2020, they will account for 2.1 billion or approximately 30% of the world's projected population. The recent struggles in Afghanistan and Iraq and continued tension with Iran, really only continue the 1950s Suez conflict, the oil crisis of the 1970s and the invasion of Kuwait in the 1990s.

Westerners have made little attempt to understand the Islamic mind and assume that Muslims share their value systems. This is wrong-headed and short-sighted. Muslims are different and it will be increasingly necessary to make a serious and sincere attempt to understand them – something President Obama's administration clearly grasps. WPP will be announcing new Muslim marketing initiatives at the Muslim conference in Kuala Lumpur in May 2010.

**But don't dismiss the US just yet**

Past Annual Reports have featured work by artists from China, India, Africa and Latin America. This year's report shows works from acclaimed US painter, Wayne Thiebaud. The choice is appropriate, for America is at a crossroads, one not dissimilar to that which it faced in the 1980s and the turnaround we have seen in the first quarter of 2010 almost looks like America bites back.

The growth of China and India might lead some to underplay the continuing importance of the US. That would be a mistake. Failure to understand its significance remains a risky move even in these troubling times. Take investment banking. A quarter century ago, SG Warburg, Morgan Grenfell, Schrodgers and Flemings could be counted as strong European brands. Today, they have all but disappeared. Despite recent catastrophes, large American banks, such as Goldman Sachs, Morgan Stanley, Bank of America, JP Morgan Chase and Citigroup (but no longer Bear Stearns and Lehman Brothers), dominate the industry, although boutiques focusing on investment banking relationships, rather than trading, may become fashionable again.

A few years ago, strong European talent might have expressed misgivings about working in American multinationals. Today, these businesses are more sensitively run and still offer more interesting, intellectually-stimulating global opportunities and challenges. The European-based businesses that remain, such as Deutsche Bank, UBS and

**BrandZ™ Most Powerful Brands 2010**

Top 20 global brands by value \$m

Rank	Ranking change	Brand	Brand value 2010	Brand value 2009	Brand value 2008	% chg vs. 09	% chg vs. 08
1	=	Google	114,260	100,039	86,057	14%	16%
2	2	IBM	86,383	66,622	55,335	30%	20%
3	3	Apple	83,153	63,113	55,206	32%	14%
4	-2	Microsoft	76,344	76,249	70,887	0%	8%
5	-2	Coca-Cola*	67,983	67,625	58,208	1%	16%
6	-1	McDonald's	66,005	66,575	49,499	-1%	34%
7	3	Marlboro	57,047	49,460	37,324	15%	33%
8	-1	China Mobile	52,616	61,283	57,225	-14%	7%
9	-1	General Electric	45,054	59,793	71,379	-25%	-16%
10	-1	Vodafone	44,404	53,727	36,962	-17%	45%
11	1	ICBC	43,927	38,056	28,004	15%	36%
12	5	HP	39,717	26,745	29,278	48%	-9%
13	-2	Walmart	39,421	41,083	34,547	-4%	19%
14	2	BlackBerry	30,708	27,478	13,734	12%	100%
15	11	Amazon	27,459	21,294	11,511	29%	85%
16	-1	UPS	26,492	27,842	30,492	-5%	-9%
17	4	Tesco	25,741	22,938	23,208	12%	-1%
18	18	Visa	24,883	16,353	n/a	52%	n/a
19	6	Oracle	24,817	21,438	22,904	16%	-6%
20	14	Verizon Wireless	24,675	17,713	19,202	39%	-8%

Source: Millward Brown Optimor (including data from BrandZ, Datamonitor and Bloomberg)  
\* Value includes Lites, Diets and Zero.

**Top 20 US advertisers 2009**

Ranked by total measured ad spending\* \$m

2009 rank	2008 rank	Advertiser	2009	2008	% change
1	1	Procter & Gamble	2,714	3,217	-15.6%
2	2	Verizon Communications	2,238	2,403	-6.9%
3	3	General Motors	2,198	2,168	1.3%
4	4	AT&T	1,904	1,986	-4.1%
5	10	Pfizer	1,397	1,053	32.7%
6	5	News Corp	1,252	1,401	-10.6%
7	6	Sprint Nextel	1,250	1,369	-8.6%
8	14	Johnson & Johnson	1,227	945	29.9%
9	7	Time Warner	1,205	1,293	-6.8%
10	16	Wal-Mart Stores	1,170	864	35.4%
11	12	Ford Motor	1,087	1,010	7.6%
12	8	Walt Disney	1,064	1,215	-12.5%
13	9	General Electric	998	1,199	-16.7%
14	13	Macy's	908	982	-7.5%
15	20	McDonald's	890	829	7.3%
16	25	L'Oreal	849	776	9.4%
17	29	Unilever	842	732	15.0%
18	11	Toyota	830	1,209	-19.3%
19	17	Berkshire Hathaway	818	847	-3.4%
20	18	Sony	791	835	-5.2%

Source: Kantar Media  
\* Measured spending in TV, magazines, newspapers, radio, outdoor.

## What we think

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Credit Suisse, still face the hurdle of establishing a good market position in the US.

Neither is it easy to find European-based global companies. BP and Shell certainly get it, as do Unilever and Nestlé. So does Daimler, although Jurgen Schremp's global strategy has been dismantled. Vodafone, GlaxoSmithKline, AstraZeneca, L'Oreal and Sanofi-aventis are other good examples, although doubts in some cases remain. There are not many more. American influence is still ubiquitous.

The world has not been globalised in the way the late Professor Theodore Levitt forecast, where consumers around the world bought similar products, marketed in the same way. Indeed, Levitt admitted as much in an interview to celebrate the 20th anniversary of his article, saying he was exaggerating to make a point. Truly global products only account for around 10-15% of our worldwide revenues. In fact, consumers are probably more interesting for their differences than their similarities.

Recent political developments support this – the collapse of the Soviet Union, the break-up of Yugoslavia, devolution in Scotland and Wales and Basque nationalism. Moreover, the European Union is really a supply-side led phenomenon, harmonising production and distribution, rather than demand. On January 1, 1993, a Euro consumer was not born. What has been going on may well not be the globalisation of world markets, but their Americanisation. Not in the sense that upsets the French or the Germans, and results in the banning of Americanisms from French commercial language – an objection to the cultural imperialism of Coke, the Golden Arches or Mickey Mouse. More in the sense of the power and leadership of the US. In most industries, including our own, the US still accounts for almost half of the world market. And given the prominence of US-based multinationals, you could argue that almost two-thirds of the advertising and marketing services sector is controlled or influenced from there. If you want to build a worldwide brand you must establish a big presence in the world's largest market – the US. At WPP, 21 of our top 50 clients are headquartered in Europe, three in Asia Pacific and 26 in the US. Almost all of the latter are located in the northeast quadrant created by Chicago, Detroit, New York and Washington.

That American strength is based on three factors. First, the size and power of the American market: more than 300 million people in a relatively homogeneous market. The European Union at 500 million is over one and a half times that size, but much more heterogeneous. Second, the power and size of US capital markets. Recent difficulties aside, America is still the cheapest place to raise debt or equity capital, although more detailed disclosure requirements are discouraging some. Finally, because of its strength in technology, it is hard to think of many areas where it does not lead. Third-generation mobile phones are one, but, given the prices European companies paid for the privilege, the distinction is dubious.

## BrandZ™ Top categories 2010

Year-on-year growth in total category value

Category	Brand value growth
Financial institutions	12%
Beer	10%
Technology	6%
Fast food	1%
Retail	-1%
Soft drinks	-1%
Mobile operators	-1%
Bottled water	-2%
Gaming consoles	-3%
Spirits	-3%
Luxury	-3%
Apparel	-4%
Personal care	-4%
Coffee	-6%
Insurance	-7%
Cars	-15%

Source: Millward Brown Optimor (including data from BrandZ, Datamonitor and Bloomberg)

## Back to the country

The world's multinational companies must develop new thinking to deal with the issues described above. As US-centric corporations, for example, seek to develop their businesses and extend their reach into more heterogeneous markets, the balance of organisations will shift. This will not mean that everything changes. There will continue to be a focus on global, max or core brands, with sales of more than \$1 billion, to counterbalance the power of global retailers and allow companies to become less dependent on the US markets. For instance, Coca-Cola's geographic coverage of around a third in North America, a third in Asia and Latin America and a third in Europe, Middle East and Africa will become more the norm, rather than Pepsi-Cola's 52% in the US. At the same time, more sensitive local organisations that can respond more readily to national opportunities and challenges will be required.

The past 10 to 15 years have seen, probably quite rightly, a diminution of the power of country managers, as companies sought to reduce needless duplication and stimulate the sharing of knowledge. Eradicating geographic silos and fiefdoms made sense. But as country-based organisations have become more complex and sizeable, there may be a need to develop more focus at a local level. Several clients have started to re-build country organisations and re-appoint country managers or ambassadors, particularly as they need to cultivate governmental or academic influence or be more locally sensitive.

As a result, regional management has come under scrutiny. With the development of technology and communications,



organisational span-breakers may not be so necessary. In addition, given the complexity of regional tasks, regional managers become no more than glorified financial directors. The average advertising agency regional director in Europe, for example, may have to cover 100 offices in a 250-day working year. It would be difficult to add significant value while spending an average of one to two days in each office a year, even if he or she travelled constantly.

At WPP, we are experimenting with two new organisational responses. First, Global Client Leaders to manage at least the 30 biggest clients across WPP on a worldwide basis. Second, WPP Country Managers focusing on three key issues – people, local clients and acquisitions.

Both responses cause angst to our operating company or tribal leaders, who continue to have primary organisational control. Both cut across traditional organisational structures. Both demand new ways of working together, denying turf, territory and ego. Both raise questions about motives, methods and values. But both are necessary, responding to client needs and developments. Organisations are becoming more and more networked, less and less pyramidal.

Furthermore, as the balance of economic power shifts, there will have to be similar shifts in power within corporations. Salary increases, benefits, STIPs, LTIPs, share options, restricted stock allocations, capital expenditure, for example, will have to be allocated more fairly, as growth favours these faster-growing markets. This will mean that Anglo-American or American-Western European management cliques will have to open up, as, for example, Unilever has done, with over 400 Indian managers already exported around the world in senior positions. There will be more.

### The rise of marketing services

While Advertising and Media Investment Management – which historically has concentrated on traditional areas such as television, radio, newspapers, magazines, outdoor and cinema – has thrived in recent times, its overall share has declined. In its place, supposedly less sophisticated, less global and less-developed marketing services have gained as a proportion of our total business. These areas are Consumer Insight, Public Relations & Public Affairs, Branding & Identity, Healthcare and Specialist Communications – particularly direct, interactive and internet communications.

Marketing services have grown more quickly for two reasons. First, network television pricing has risen faster than inflation, to the disquiet of big advertisers. Procter & Gamble, the world's biggest advertiser, Unilever, Coca-Cola and American Express have all registered voluble protests in recent times. They are sick and tired of paying more for less and hence their laser-like focus on value in the recession.

Although the pressures on US network television intensified in 2006, network cost per thousand probably rose by 4-5%, still faster than general price inflation of 3%. In 2007, network cost per thousand again rose faster than general price inflation and, even with the acute economic pressures of 2008, US network television may have increased in cost relatively. 2009 was the only weakening in the trend, as network pricing probably fell for the first time for a long time by approximately -3%. In the UK, ITV pricing may have fallen back to prices achieved as much as five or 10 years ago, the biggest bargain for a long time.

Nevertheless, the trend is clear. Imagine what would happen in the car industry if the price of steel rose consistently by 10% against general price inflation of 3%. Manufacturers would use less steel or find a substitute. That is what is happening in our industry, too. Marketing services, digital and even other traditional media such as radio, outdoor and cinema advertising are becoming more acceptable substitutes.

Don't expect network television, however, to disappear any time soon. It will remain important. If we were starting a multinational packaged goods company from scratch, we would still use network television to influence the largest number of people in the shortest time at the lowest cost. Clients still need reach, but it isn't what it was. In the US, for example, primetime network television used to claim 90% of households. A few years ago it was 50%; today it is perhaps only 33%. There are, of course, still programs with significant global or national reach, such as the World Cup final (500 million); the Olympics (400 million in a normal year – but an audience of over two billion for the opening ceremony in Beijing in 2008); the Super Bowl (106 million); and the Academy Awards (42 million).

The largest regular live event audience, however, is none of the above. It is the Chinese New Year Gala on CCTV in China, Asia and elsewhere, watched consistently by more than one billion. These events remain in relatively fixed supply, while the pools of money chasing them are stable or growing. As a result, their prices are bid up. That's why a 30-second Super Bowl advert still costs around \$2.8 million and an Academy Awards slot around \$1.3 million.

This is not a situation that can last, particularly when significant segments of the viewing population seem to go missing. Phenomena such as the disappearance of young American men on Monday nights – perhaps to gaming on the internet or watching sport in bars – and the defection of housewives from soap operas have prompted changes to the way audience figures are compiled.

## What we think

After the threat of apocalypse, new centres of gravity

### The age of many media

There is another reason for the growth of marketing services – media fragmentation. The old media have become more sophisticated and the new media have proliferated. Technology has improved the effectiveness and development of cable and satellite television, newspapers and periodicals, radio and outdoor, while spawning new media in direct,

interactive and the internet. Many of these new media are more measurable and more targeted.

Media consumption habits change with every generation. Even small children know their way round the internet. Decision-makers in media owners and agencies tend to be in their fifties and sixties; their children and grandchildren are shifting in ever greater numbers to multi-tasking on the web, personal video recorders (PVRs), video-on-demand, iPods,

### Growth of media\* in major markets 2005-2010 %

Television	2005	2006	2007	2008	2009 <sup>f</sup>	2010 <sup>f</sup>
North America	0.8	7.7	-2.2	0.9	-5.2	-3.9
Latin America	15.1	13.2	10.9	9.9	7.0	10.3
Western Europe	4.0	2.6	4.4	-3.2	-13.3	-1.1
Emerging Europe	22.2	24.4	21.0	12.5	-13.3	5.0
Asia Pacific (all)	7.0	8.9	6.7	6.1	-0.7	5.6
North Asia <sup>1</sup>	16.8	22.3	13.3	15.0	3.3	7.9
Asean <sup>2</sup>	13.9	13.7	8.1	10.0	8.4	11.3
Middle East & Africa	3.2	18.8	25.8	29.4	6.4	9.2
World	4.7	8.1	4.0	3.5	-4.6	1.5

Radio	2005	2006	2007	2008	2009 <sup>f</sup>	2010 <sup>f</sup>
North America	0.2	1.6	-3.3	-9.1	-13.3	-6.8
Latin America	15.2	5.1	11.0	12.8	2.3	7.0
Western Europe	4.5	2.0	5.0	-1.2	-12.0	-1.9
Emerging Europe	14.1	34.7	24.6	3.1	-26.4	2.6
Asia Pacific (all)	2.4	16.5	4.9	5.8	2.3	3.2
North Asia <sup>1</sup>	1.5	157.9	21.1	24.4	9.1	8.6
Asean <sup>2</sup>	7.1	3.2	1.9	9.7	16.7	9.2
Middle East & Africa	20.4	11.1	23.5	18.8	5.8	9.3
World	3.1	5.3	2.5	-1.8	-8.8	-1.4

Newspapers	2005	2006	2007	2008	2009 <sup>f</sup>	2010 <sup>f</sup>
North America	1.8	-0.5	-4.9	-10.2	-18.4	-13.4
Latin America	17.3	7.2	14.5	4.1	9.0	10.9
Western Europe	1.7	2.4	3.6	-5.7	-16.0	-4.5
Emerging Europe	-10.1	16.0	10.4	6.1	-28.0	7.6
Asia Pacific (all)	1.7	-4.6	2.4	-2.2	-3.6	0.0
North Asia <sup>1</sup>	2.4	-14.9	5.9	4.9	6.4	7.5
Middle East & Africa	15.2	10.5	18.1	12.5	-7.2	3.1
World	2.2	0.3	1.7	-4.8	-12.4	-4.1

Magazines	2005	2006	2007	2008	2009 <sup>f</sup>	2010 <sup>f</sup>
North America	7.1	2.7	3.4	-6.5	-9.6	-2.0
Latin America	22.5	12.1	4.1	18.2	0.7	4.4
Western Europe	1.1	2.8	1.1	-5.7	-21.0	-7.0
Emerging Europe	48.6	16.9	8.2	6.5	-28.4	3.2
Asia Pacific (all)	18.6	2.3	0.2	-3.5	-7.9	-3.5
North Asia <sup>1</sup>	15.7	16.5	11.5	14.2	-7.4	4.2
Asean <sup>2</sup>	7.7	8.8	-1.4	6.1	-3.1	6.3
Middle East & Africa	23.5	13.6	11.3	10.8	-9.0	1.1
World	7.9	3.5	2.5	-4.6	-13.4	-3.1

Cinema	2005	2006	2007	2008	2009 <sup>f</sup>	2010 <sup>f</sup>
North America	6.3	4.0	7.5	5.0	0.0	0.3
Latin America	17.0	20.4	2.1	17.4	0.4	6.1
Western Europe	-0.9	-3.5	-0.2	-11.1	-15.5	-4.2
Emerging Europe	32.8	26.0	15.4	19.5	-11.8	-1.3
Asia Pacific (all)	23.0	6.1	53.1	0.9	-3.7	9.8
Middle East & Africa	55.7	-27.3	-4.4	22.3	-17.8	-1.4
World	5.0	-0.6	7.5	-4.3	-11.3	0.2

Outdoor	2005	2006	2007	2008	2009 <sup>f</sup>	2010 <sup>f</sup>
North America	10.1	8.5	6.0	-0.7	-7.6	-4.6
Latin America	18.9	6.9	0.3	7.0	6.6	9.6
Western Europe	4.5	5.0	4.3	-3.1	-11.8	-1.7
Emerging Europe	21.7	31.1	17.0	13.5	-27.7	8.7
Asia Pacific (all)	19.9	10.1	6.2	8.4	-5.3	6.2
North Asia <sup>1</sup>	12.9	21.6	8.9	35.2	1.8	10.8
Asean <sup>2</sup>	14.8	33.1	7.8	11.9	6.6	13.5
Middle East & Africa	19.7	30.7	66.3	21.5	-4.2	8.9
World	13.4	9.8	7.3	4.5	-8.8	3.0

Internet	2005	2006	2007	2008	2009 <sup>f</sup>	2010 <sup>f</sup>
North America	31.0	27.0	26.7	11.6	4.1	3.6
Latin America	24.0	47.8	57.5	52.9	31.0	35.2
Western Europe	89.2	60.1	45.1	22.2	5.4	8.0
Emerging Europe	91.1	80.3	74.2	59.9	9.6	16.1
Asia Pacific (all)	92.4	34.1	32.8	25.6	14.3	15.7
North Asia <sup>1</sup>	66.6	41.5	52.0	45.6	23.4	28.8
Asean <sup>2</sup>	50.3	39.1	72.6	29.7	27.4	29.0
Middle East & Africa	533.7	22.9	-4.2	61.0	35.3	35.5
World	54.0	36.7	33.7	19.2	7.5	8.9

Source: GroupM  
f Forecast

<sup>1</sup> China, Hong Kong, South Korea, Taiwan.

<sup>2</sup> Indonesia, Malaysia, Philippines, Singapore, Thailand, Vietnam.  
(Figures rounded up.)



video iPods, iPhones, iPads, Kindles, mobiles, podcasts and multi-player internet games. Declining newspaper readership, particularly among younger people and the resultant collapse of established titles are alarming trends.

Among the many new technologies, one of the most interesting is the PVR. This device enables viewers to download television programs on to a hard disk, creating their own television channel, recording programs for

screening when they want to see them, and building a library, as an iPod does with music. A PVR also allows you to time-shift programs as you watch, stopping for breaks when you wish. It cannot be long before they are standard equipment in television sets.

What has made observers particularly excited – or worried – about the PVR is its ability to fast-forward or skip commercials. Market research in the US indicates that consumers like to fast-forward advertisements – although they stop at beer commercials for fun and car commercials for information. We could do most of this previously with video recorders, of course. The key question remains the amount of time viewers will continue to devote to television. In some PVRs, the skip button has been omitted and fast-forward speeds limited. In others, little boxes on the PVR screen will contain details of the ads being fast-forwarded. However they develop, such devices will exert more pressure on network television and on agencies to create stronger programming and sponsorship opportunities, along with even more creative advertising ideas. The same will be true of video-on-demand, another new and fast-developing technology. The premium on creativity can only grow.

Many executives are in denial. They believe – or hope – that radical change will not happen on their watch. Yet I know my consumption habits have altered over the past few years – more daily newspapers like *The Wall Street Journal* and the *Financial Times*, fewer periodicals. More cable and satellite television, less network. More web surfing and BlackBerry® e-mail. More continuous streaming of CNBC or Bloomberg and now the iPad. More downloading of newspapers and books on my Kindle and now the iPad. I am less willing to wait for detailed analysis in weeklies or fortnightlies. I want news, together with commentary now. Why should I wait 10 days for in-depth analysis of a merger announced on Thursday night? By contrast, though, women seem to be increasing their magazine readership and *The Economist* powers ahead, having gone well past a one million circulation with increasing advertising revenues, even in these threatening times.

### Principal sources of annual media growth

Absolute contribution in %

	2007	2008	2009 <sup>f</sup>	2010 <sup>f</sup>
<b>North America</b>	<b>1.3</b>	<b>-1.9</b>	<b>-7.8</b>	<b>-4.0</b>
US	0.8	-2.4	-8.0	-4.3
<b>Latin America</b>	<b>11.1</b>	<b>10.6</b>	<b>7.0</b>	<b>10.5</b>
Brazil	8.6	12.9	10.5	12.7
<b>Western Europe</b>	<b>6.6</b>	<b>-1.7</b>	<b>-12.8</b>	<b>-1.6</b>
<b>Emerging Europe</b>	<b>18.8</b>	<b>12.5</b>	<b>-18.2</b>	<b>6.3</b>
Russia	26.5	17.7	-19.6	5.8
<b>Asia Pacific (all)</b>	<b>7.3</b>	<b>5.8</b>	<b>-0.4</b>	<b>5.3</b>
India	20.2	14.0	1.1	6.1
<b>North Asia</b>	<b>14.4</b>	<b>18.1</b>	<b>5.2</b>	<b>10.3</b>
China	17.9	22.6	8.4	12.0
<b>ASEAN</b>	<b>9.3</b>	<b>10.2</b>	<b>6.5</b>	<b>11.6</b>
<b>Middle East &amp; Africa</b>	<b>23.6</b>	<b>20.9</b>	<b>0.2</b>	<b>7.0</b>
GCC and Pcn Arab	28.4	29.6	-8.9	10.6
<b>World</b>	<b>5.7</b>	<b>1.8</b>	<b>-6.6</b>	<b>0.8</b>

### Principal sources of annual media growth

Contribution in \$bn

	2007	2008	2009 <sup>f</sup>	2010 <sup>f</sup>
<b>North America</b>	<b>172,321</b>	<b>169,007</b>	<b>155,797</b>	<b>149,640</b>
US	161,515	157,633	144,975	138,752
<b>Latin America</b>	<b>20,526</b>	<b>22,712</b>	<b>24,307</b>	<b>26,860</b>
Brazil	10,788	12,175	13,454	15,161
<b>Western Europe</b>	<b>124,241</b>	<b>122,121</b>	<b>106,520</b>	<b>104,848</b>
<b>Emerging Europe</b>	<b>18,862</b>	<b>21,220</b>	<b>17,364</b>	<b>18,455</b>
Russia	7,864	9,256	7,437	7,872
<b>Asia Pacific (all)</b>	<b>120,348</b>	<b>127,329</b>	<b>126,818</b>	<b>133,583</b>
India	4,223	4,816	4,867	5,164
<b>North Asia</b>	<b>40,427</b>	<b>47,740</b>	<b>50,202</b>	<b>55,388</b>
China	28,730	35,223	38,181	42,771
<b>ASEAN</b>	<b>8,936</b>	<b>9,845</b>	<b>10,480</b>	<b>11,694</b>
<b>Middle East &amp; Africa</b>	<b>11,395</b>	<b>13,780</b>	<b>13,802</b>	<b>14,774</b>
GCC and Pcn Arab	2,886	3,740	3,408	3,768
<b>World</b>	<b>467,693</b>	<b>476,169</b>	<b>444,609</b>	<b>448,159</b>

Source: GroupM  
f Forecast.

### Technology and tradition

Web activity, broadly defined, currently accounts for around \$4 billion of WPP's revenues, or 27%. It is growing rapidly and will continue to challenge us and our clients. There are a number of reasons for this.

One is disintermediation, an ugly but useful word. Let's take an example from our own business. More than \$4 billion of WPP's revenues (post-TNS) comes from market research. Traditionally, research has been done on the phone and through the post. The process was long and cumbersome. A questionnaire had to be designed, distributed and filled in by consumers or interviewers. Then data were collected, analysed and conclusions developed. That could take three

## What we think

After the threat of apocalypse, new centres of gravity

to six months. Many CEOs despaired that by the time the solution had been identified, the problem had changed. Using the internet, however, the research process can be transformed and responses obtained almost instantly. WPP's Lightspeed panel interrogates more than 17 million consumers globally and can deliver answers inside 24 hours. You may also be disintermediated by lower-cost business models. The gambling industry, for instance, has been shaken by the emergence of peer-to-peer sport betting sites, cutting out the traditional bookmaker.

Despite the relatively recent vicious compression in valuations and consequent losses, the financiers of new media and technology companies still focus on sales, sales growth and market share, rather than on operating profits, margins, earnings per share and return on capital employed. The hour of reckoning, however, could be coming for some Web 2.0 companies. All, or virtually all, depend on advertising revenues for their growth and survival. There will be losers in the battle to capture those revenues and we may have reached a point in the investment cycle where revenues, operating profits and cash flow become paramount. Financing institutions and strategic investors may no longer continue to support excessive valuations by re-financing cash burn, particularly after a financial crisis. Even venture capital companies will be more picky about matching or raising pricing in the next round of financings and may cut off funding altogether and admit their mistake. AOL recently announced that it will no longer finance Bebo, the social networking site it bought for \$850 million two years previously. It will either sell it or close it.

These conundrums, however, are nothing compared to those faced by traditional media owners, few of whom have managed to deal with new technologies. Take Craigslist, for example. Established in 1995 by Craig Newmark, the site provides largely free classified advertising to millions of users across the globe. The result – a massive reduction in classified advertising revenues for the traditional players. It is estimated that Craigslist costs newspapers in the San Francisco Bay area up to \$65 million a year in lost employment advertising.

The response from traditional classified advertisers is to produce their own free classified sites. The effect: a permanent reduction in classified advertising revenues, as established classified media owners justify their activities as necessary cannibalisation. If they don't eat their own children, someone else will. The internet is probably the most democratic phenomenon we have seen: free information or nearly free information breaking the tyranny or monopoly of distance.

Few newspaper or periodical publishers have mastered the connection with the new internet platforms. Rupert Murdoch's rapid and successful purchase of internet assets such as MySpace is one example, although the growth rates are in decline. Similar initiatives have come from network television: NBC owned by GE with iVillage, and ITV in the

UK with Friends Reunited (since revoked). Others such as *The New York Times* have made similar moves, but none seem to have been able to replace the lost revenues by new ones. For several years in our Annual Report we have questioned whether NBC would still be a part of GE in a few years? Would it be sold or spun-off? Would it merge with Yahoo! or another internet company? In 2009, we found out the answer – a sale to Comcast. Will even *The New York Times* survive or face the fate of some US newspapers? *The Chicago Tribune* filed for bankruptcy protection in 2008. *The San Francisco Chronicle*, whose owners have warned of a sale or closure, claims to have improved its finances with a new business model and the *Seattle P-I* has gone wholly online.

It is no longer enough just to be in the newspaper or network television business; you have to be in the communications business. This idea is not dissimilar to Professor Theodore Levitt's analysis of the horse and buggy in the context of the transportation industry. Rupert Murdoch is one of the few who seems to understand this. Perhaps the mistake was not to charge for newspaper content on the web in the first place. It is easier to take the consumer down in price, rather than up. If you can't charge for content as strong as Condé Nast's *Vogue* or *The Wall Street Journal*, for example, when can you? Now media owners seem to have shifted gears, deciding finally to charge for online content – Rupert Murdoch leading the way, Arthur Sulzberger and others have finally realised the need. Paying for content, further media consolidation and the possible subsidy of traditional content by government are all current trends that will probably continue to develop. The internet has resulted in a permanent reduction in the revenues and profitability of traditional media owners, but if consumers value content they will pay for it.

As a result, clients are re-examining the relative levels of their advertising and marketing services investment. The econometric analysis of media investment is becoming increasingly important. How much should we spend and through which media, have become ever more critical questions – the Holy Grail of advertising, the answer to which half of advertising is wasted.

The application of technology and the data it provides are important components to succeed in the new technology-based media. We had already invested through WPP Digital, GroupM, Kantar and our direct and interactive businesses, such as Wunderman, OgilvyOne and G2, before purchasing 24/7 Real Media. This was more than the acquisition of a digital agency – such as the acquisition of jewels like AGENDA, Aqua, Blast Radius, Bridge, BLUE or Schematic. This was about the development of search technology, advertiser and publisher websites, the application of technology in general and media sales, and followed, on a much smaller and less lavish scale, Google's acquisition of DoubleClick and Microsoft's purchase of aQuantive,



although all had the same proportional impact on WPP, Google and Microsoft.

With enough investment, we can reproduce any of the media planning and buying technology developed and have already accessed search revenues effectively. Unlike most media owners, we are not investing in a single technology or making technological bets. We are purveyors of any and all media investment alternatives and, as long as we are not excluded from any single, powerful technology and have the talent to analyse and optimize these alternatives for our clients, we will remain not only relevant but increasingly valuable to them. In contrast, media owners, unless they cover the media waterfront, are exposed to one technology or another. Increasingly, our business is about combining the full range of our marketing and communications creativity, insights and skills with the application of technology and the mastery of data.

Warren Buffett used to say in the 1970s, when he invested directly in IPG and Ogilvy (at three times earnings), that agencies represented a royalty on the international growth of US-based multinationals. Perhaps today, parent company investment also represents a royalty on the growth of new media technologies.

### The web brain drain

The internet and other new technologies will affect another area – recruitment. Young, bright talent will always seek out new, flexible, un-bureaucratic, responsive companies. Staying with one company for 40 years or so – as my father did and my parents advised me to do – no longer seems the best career choice. Clearly, the era of apprenticeship inside large corporations is finished. It was weakened by the corporate downsizing of the 1980s and 1990s, the final nail in the coffin coming with the internet boom of the late 1990s. However, some recent polling and attitudinal analysis in the UK shows younger people want a better work-life balance. Hedge funds, for instance, have until recently proved more attractive than investment banks, offering fixed work times and not demanding all-night toil, while making massive trades.

After the bankruptcies and failures of Web 1.0, many young people returned to the more traditional businesses they had left. WPP lost a number of such bright talents and later welcomed some back to the fold. I conducted re-entry interviews, and hoped to hear that the returnees were relieved to have their jobs back. Far from it: few grovelled. Worse, they admitted that given the opportunity again, they would take it or seize a similar one. And recently, in the last year or two, with the emergence of the second internet boom, it is clear there is another wave of bright, young people attracted to new technologies and opportunities within those companies.

### Google: signs of mortality?

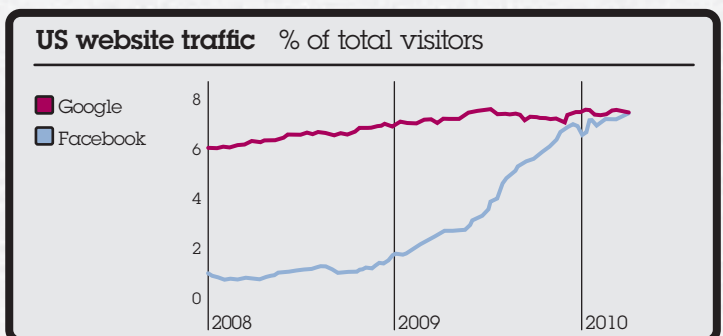
Google's success is clear and its economic power substantial. It has a market capitalisation, despite recent volatility, of \$180 billion, projected 2010 revenues of around \$22 billion, approximately 20,000 people and growing, and 65 offices. The stock markets are saying something about Google's valuation in relation to our own \$14 billion valuation, with approximately 60% of the revenues at \$14 billion and nearly 100,000 people (excluding associates) in over 2,000 offices.

Put together the four largest communications services parent or holding companies – WPP, Omnicom, IPG and Publicis. You will have approximately \$37 billion of revenues and a \$38 billion market capitalisation – almost twice the revenue of Google, but only a 21% of the market value.

So is Google a frienemy or foe? On the amicable side, we are forecast to spend approximately \$850 million this year (the Dell and AT&T search accounts are the third and fourth largest after eBay and Amazon). That tells you a little about the nature of Google's business. Normally our media market share, according to RECMA, the independent organisation that measures scale and capabilities in the media sector, is around 25-30%. With Google it is around 5%, indicating a long tail and a heavy small- and medium-sized business-to-business connection. In a sense, Google is a mechanical Yellow Pages – opening up advertising to small- and medium-sized companies that did not advertise before.

In any event, Google clearly wants to work with us on building relationships with our biggest clients. We have run joint seminars on both sides of the Atlantic for some of our largest and most important clients to try to nurture mutual relationships and are building joint sales programs with a Google sales team designed specially for us. We have also initiated, with Google, Harvard Business School and MIT, a \$5 million yearly research program on the effectiveness of advertising on the internet.

There is no doubt that Google has become friendlier as it has focused its business in the teeth of the recession and renewed its efforts on the digital areas, where it draws its strength rather than the traditional media areas, where it



Source: Experian Hitwise

## What we think

After the threat of apocalypse, new centres of gravity

had stumbled. Having hired a new CFO and cut \$1 billion in costs, its renewed focus on search, digital display and particularly mobile indicates the future, with the launch, for example, of Nexus One (which, by the way, disintermediates both the mobile handset industry and the mobile operator networks at the same time). On the less friendly side, CEO Eric Schmidt says Google is targeting the advertising sector. Google experimented in many traditional areas such as print and TV, signing deals with Clear Channel and Echostar, though recently scaling back in some traditional areas. It has hired creative people to write ads and one of our creative directors to head up its creative efforts. It has approached US clients to see if it can set up a direct, electronic media-buying exchange. Google is also looking at electronic media planning and buying models, which can be accessed through the web.

Google has also concluded a billion dollar deal with AOL and Time-Warner has indicated in internal memos that it plans to co-operate with Google in television, print and other media. The opportunity exists, although it is doubtful if the traditional Time-Warner operating company verticals will be easily persuaded to give up on digital expansion and opportunities to meet their budgets and targets. It also offers, through Google Analytics, a free analytical service.

In 2006, Google made Rupert Murdoch's purchase of MySpace a stunning success with a \$300 million per annum, three-year deal for internet revenues. This against a purchase price of around \$680 million. And then it overcame its lack of success with video by buying YouTube for \$1.65 billion, despite little or no revenues and a bunch of copyright lawsuits, part of which were solved by making three music companies momentarily YouTube share owners and \$50 million richer on the morning of the sale. Finally, it gave Warren Hellman and Hellman & Friedman a return of 800-900% over two years on DoubleClick, paying over \$3 billion – 10 times revenues and 30 times EBITDA. Entry to the first round of the auction was 13-14 times EBITDA, which we could not reach. Through DoubleClick, Google may control more than 80% of targeted and contextual internet advertising, along with much valuable client and publisher data.

This last transaction awoke the dragon. Microsoft initiated a heavy response, not only on regulatory fronts, but from transactions, too. 2007's rumours were confirmed, as Microsoft bid for Yahoo! (and then partnered with it in search), aQuantive and others. Already, Yahoo! has paid an infinite EBITDA multiple for Right Media. Sane strategic moves or irrational exuberance?

All in all, Google has opened up an attack on many fronts. Perhaps too many, particularly when you consider the other theatres it is fighting in, such as book publishing and robots to the moon. One gets the impression it was throwing a lot of mud against the wall to see if any sticks – maybe confining itself to search and mobile search would be best, as it now seems to be doing. Yahoo! has a different approach,

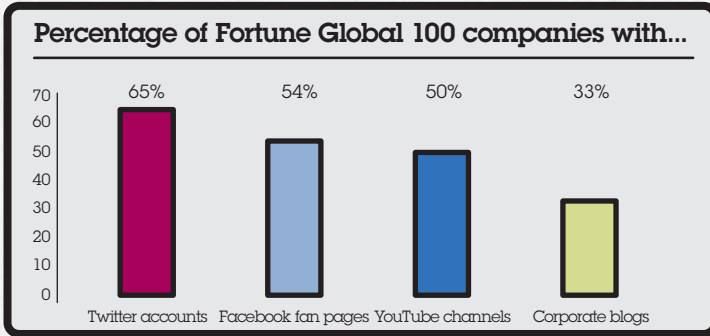
working through its agency partners and believing in the power of people, rather than Google's greater focus on technology. Certainly, the combination of Microsoft and Yahoo! in any way has brought greater balance to the markets. Our clients and our agencies favour a duopoly rather than a monopoly. Google's poor handling of Chinese government relations and withdrawal from the Chinese market and issues in the EU with business practices, specifically in France, Italy and Germany, do not help, along with Federal Trade Commission issues over the AdMob acquisition in the US. The latter reflects the emerging battle between Google and Apple, highlighted in recent press articles that cover the increasingly fractious relationship between the companies that are both collaborators and competitors or another example where Google has become a frienemy.

Perhaps, the biggest threat to Google is from within. As Warren Buffett recently pointed out in China, if Google was worth \$250 billion then (more than his own Berkshire Hathaway and in the top three US companies by market capitalisation after only 10 years), it would have to be worth \$350-400 billion in two or three years to justify that valuation. After that comment, Google's market capitalisation fell, although it has now recovered significantly. It may be the frustrations of a 76-year-old (and friend of Bill Gates) fuming that it took him 40 years to build a company to a value of \$200 billion – rather than 10 years. What's more, Sergey Brin and Larry Page were worth \$14 billion each and only in their mid-30s.

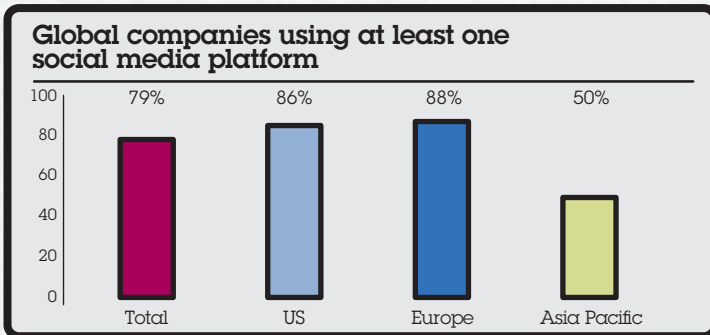
In any event, recent data on click-through rates makes even Google look mortal and volatility of market value on this scale threatens internal motivation and loyalty. Bright young computer engineers may be tempted to try venture capital opportunities in Silicon Valley, rather than continue to hold vulnerable equity. The answer to the question whether Google is a frienemy or foe, is probably both. Short-term friend, long-term foe although, more recently, Google has become a friendlier frienemy to us while making more friemies on the way.

### Where public relations wins

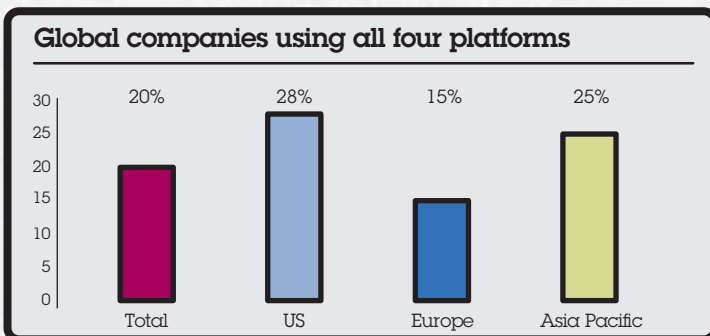
Good editorial cannot be bought, only influenced, making one marketing discipline increasingly important – Public Relations & Public Affairs. The growth of the internet and the growing sophistication of polling techniques play to the traditional strengths of Public Relations & Public Affairs, where relationships need to be built with opinion formers. Blogs, social networks and customer websites are a new form of editorial, as important if not more important than *The New York Times*. Because they are fast and have a more intimate relationship with their readers, blogs can cause disproportionate harm to a brand – or conversely



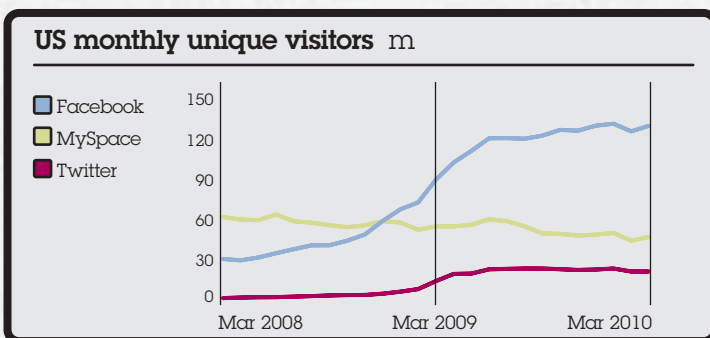
Source: Burson-Marsteller



Source: Burson-Marsteller



Source: Burson-Marsteller



Source: Compete.com

bring great benefit. PR can influence them in a way paid-for advertising cannot.

PR will never replace traditional advertising but in the new electronic media, it is a measurable way of building a brand. Chinese and Indian manufacturers will need its services to bring their products to the West, as they go beyond being makers of cheap generic goods to creators of value-added brands. Equally, burgeoning global powers will need PR to smooth their ways to places of influence in the world. And the financial institutions blamed for the credit crunch will need to buff up their tarnished reputations.

**PR will never replace traditional advertising but in the new electronic media, it is a measurable way of building a brand**

In all these cases, PR will help, as we have seen over the past five years with the continued growth of our Public Relations & Public Affairs businesses.

### Too much stuff, too few customers

Most sectors are facing problems similar to those in the car and truck industry, where companies can still make 80 million units and consumers buy 60 million. This happens even after recent rationalisation among the Big Three in Detroit. (Amazingly, it seems that to be successful in capitalist America, you have to take government money and go into Chapter 11 bankruptcy!) The contraction in supply in the US has been balanced by expansion in China, India and South Korea. Geely buys Volvo, Tata buys Land Rover and Jaguar, Hyundai becomes the new automobile Samsung.

It is difficult to find many cases where overcapacity is not a big, long-term issue. Tequila, perhaps, where it takes seven years to grow the herb. Or high fashion companies like Rolex and Hermes, where historically supply is limited – although conspicuous consumption is less acceptable after the fiscal crisis. It is also true that commodity-based industries such as oil and steel faced undercapacity issues for some time, being overwhelmed by Indian and Chinese demand.

Overcapacity issues are particularly difficult to deal with in politically-sensitive industries like automobiles. Governments are not enthusiastic about shutting down capacity and increasing unemployment. They also like to increase capacity by offering inducements to locate new production facilities in development regions. Thus the best thing for the European car industry would probably have

## What we think

After the threat of apocalypse, new centres of gravity

been for GM to absorb Fiat's production capability. But Silvio Berlusconi, Italy's Prime Minister, could not countenance more unemployment in the Mezzogiorno. The same issue faced the British government with Rover, resulting in it subsidising workers to stay in work during the 2005 election campaign and it faced the Obama administration with GM and Chrysler.

The critical issue in the 19th and 20th centuries was how to produce goods and services and to make sure they reached the consumer. In the 21st century, it is convincing the consumer to purchase products, services or brands in the first place. In such circumstances, differentiation becomes critically important and differentiation is what our business is about.

Historically, maintaining technical or product differences was easier. Today, keeping a technological lead is difficult. Product life cycles are being shortened and brand cycles lengthened. Here is another example from the car industry. Less than a decade ago it took, perhaps, five years to design, produce and market a car. Today, it can be done in 18 months. Facing faster and more aggressive Japanese, South Korean and German manufacturers, the Americans have been obliged to play catch-up. In future, Chinese and Indian manufacturers will stimulate further response.

So intangible differentiation is becoming more important. Psychological, lifestyle and emotional differences are significant. The suit or dress you wear, the car you drive, the holidays you take, how you spend your leisure time – all say a lot about your personality and preferences. Some say such

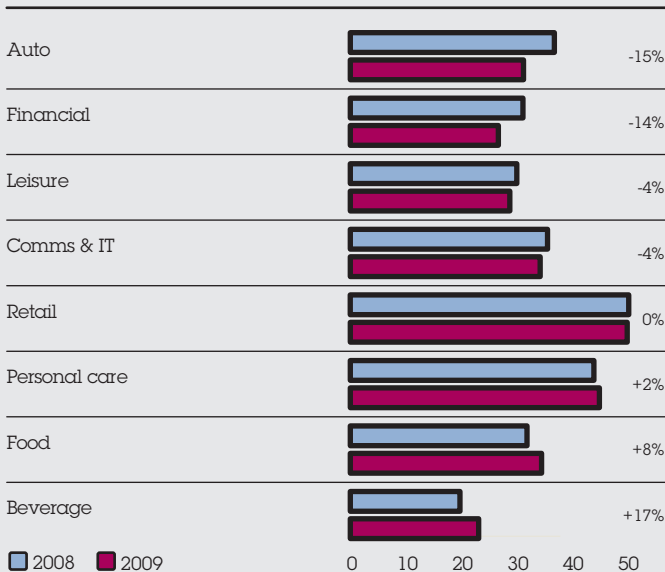
intangible appeal is unsavoury. Preying on people's vulnerabilities, it is argued, is unethical. Not so. We believe that fulfilling people's desires or dreams is almost always justifiable and satisfying for the consumer – and it is a key role for the advertising and marketing services industry.

### The great giveaway

In a low-inflation, overcapacity market with little or no pricing power, many manufacturers have turned to price promotion and discounting. The best example is the car and truck industry. General Motors still seemed to believe until recently that it had a balance sheet advantage over its competitors, particularly in Detroit. Why else would it introduce heavily price-based competition such as five-year zero-coupon financing or discounts of \$4,000 to \$5,000 a unit? Probably, the most extreme case was Hyundai in Korea offering negative interest rates on financing – a form of cash giveback. One dealer in America offered a buy one, get-one-free deal on sports utility vehicles (SUVs). Luckily, it was a failure. Even Toyota, with its current recall and branding difficulties, has resorted to discounting to maintain dealership loyalties and clear excess inventory.

If you give cars away it is only to be expected that consumers will buy them. No surprise, then, that the American auto market stood at 16 or 17 million units before the credit crisis, or that housing markets and house prices showed similar buoyancy, when fixed-term money was being

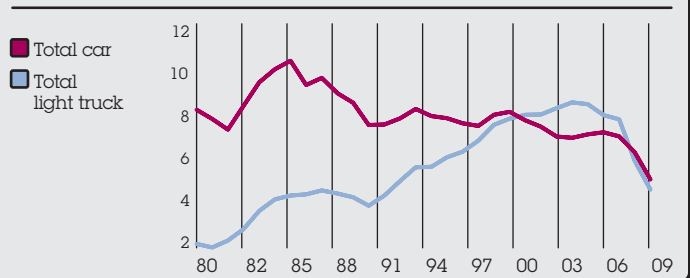
#### Advertising categories 2009 vs. 2008\* \$bn



Source: GroupM; Kantar

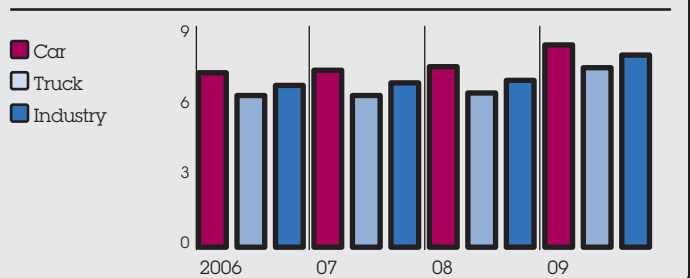
\* These categories together represent 64% of measured ad investment in a sample of 17 countries representing 83% of 2009 global ad investment.

#### US sales of new vehicles 1980-2009 units, m



Source: Ward's AutoInfoBank

#### Average age of disposed vehicles, US



Source: NVCS



given away at such low interest rates, despite the shudders in the sub-prime markets.

The problem is that consumers grow used to such discounting and wait for new car or truck introductions and the discounting that goes with them. Auto manufacturers face profitless prosperity and break-even economics at full capacity. Hence the decision by Dieter Zetsche at Daimler to dispose of Chrysler (what did Cerberus do on branding?), and the strategies of General Motors and Ford to cut capacity.

Interestingly, Japanese and Korean manufacturers, and some German ones too, have tended to resist excessive discounting, offering only \$1,000 or \$2,000. Instead, they concentrate on design, new products and branding to build a price premium, although even they have problems now.

If you focus on price, you build commodities. If you focus on innovation and differentiation, you earn a price premium and create brands. This seems to be the approach of Alan Mulally at Ford, as he brings a laser-like focus on the Blue Oval and has disposed of peripheral brands. Conclusive evidence of the inadvisability of discounting came when General Motors had to lower its earnings forecast for 2008 by 80%. Recent comments and actions by GM do indicate a slight difference in approach and a shift to more focus on product although, even after having taken government money, GM (and Chrysler) entered and exited Chapter 11 bankruptcy. Of the Big Three, only Ford, who resisted the siren calls of government aid, looks strong. More competition from the Chinese and Indians, particularly Tata, will ram the point home. Price promotion just does not work. The product is key.

A similarly unfortunate trend is occurring in the food industry. Packaged goods companies continue to try to build share by discounting and price competition, particularly as distribution concentrates. They pay higher trade discounts and slotting allowances and fund increased promotional activity. Just like the media owners, the food manufacturers are being squeezed by two factors – the other is obesity. Diabetes is a pandemic and a huge area of public concern. Increasingly, commodity-like food companies find themselves in a weak position, in contrast to the health-based or wellbeing segments of the packaged goods industry, which do not suffer from the same phenomenon. Here, companies are more focused on product innovation, research and development or science, along with branding, to build stronger market shares. As a result, brands and margins are more robust and volumes greater.

Recent accounting changes in the US forced companies to show gross and net sales, at least temporarily. As a result, more data is available on the balance between advertising and promotional spending. According to Cannondale, our marketing and channel management consultancy in the US (now part of Kantar Retail), the average consumer packaged goods company spends 16.4% of sales on trade promotion (price cuts basically) and only

9.0% on brand-building advertising. Many CEOs know what they spend on advertising, but not on trade promotion. Often the latter exceeds the former, even in heavy-spending above-the-line companies.

It may well be that manufacturers will seek to cut trade spending and boost brand-building advertising, particularly at a time when the trade is consolidating at such a rapid rate. Bribing customers for distribution is a recipe for ruin. Again, it is branding and product differentiation that must come to the fore.

### The hegemony of Big Retail

One of WPP's media partners sells 10% of its cover sales through Walmart. To the media owner, this is life or death. To Walmart it is a rounding error and the province of the third or fourth level of procurement, making the publisher's life a misery. More people visit Walmart in the US in a week than go to church on a Sunday, leading some to suggest that the supermarket chain is the new religion. Walmart, with \$408 billion of sales, is the seventh largest 'country' by retail sales, just after China. It accounts for 10% of US retail sales, while Tesco takes 14% of UK retail sales. Both enjoy 30% of grocery sales in their domestic markets. At a recent Microsoft CEO conference, Lee Scott, then boss of Walmart, targeted a doubling of its US market share to almost 20% of retail sales.

Some 15% or \$12 billion of Procter & Gamble's worldwide sales already go through Walmart. If this was a business unit on its own, it would rank among the world's top 50 FMCG companies. Other examples include Kellogg at 21%, Kraft at 16% and PepsiCo at 13%.

Influence over and control of distribution is not a new issue. After all, advertising was developed in the 19th century by manufacturers to appeal over the heads of wholesalers or retailers direct to consumers. Increasing retail concentration – not only in the US but also in Europe and Latin America – will emphasise the importance of focusing on product innovation and branding, along with better understanding of point-of-purchase consumer behaviour and emphasis on packaging, display and retail design. As a senior Asia Pacific Procter & Gamble executive has said, depending on which P&G brand you are talking about, something between 30% and 80% of purchasing decisions are made at the point of sale. Procter calls it 'the first moment of truth'.

PepsiCo chief executive Indra Nooyi calls for concentration on 'retail theatre', rather than lavish, costly TV commercials. Other FMCG leaders call for agencies to start with the shelf and not a 60-second TV commercial. WPP believes an understanding of distribution and retail is essential and it is one of our core practice development areas. The Store, our global retail practice, links more than 900 professionals working on retail business and issues around

## What we think

After the threat of apocalypse, new centres of gravity

the world, updating them on the latest developments and trends – subject to client confidentiality. Management Ventures – with more than 50 global retail analysts – along with Cannondale and Glendinning Associates, both experts in channel management, supplement and consolidate our knowledge of global retailing.

In addition, OgilvyAction gives WPP an even broader distribution offer with its focus on product categories that have been denied access to traditional media. Our new investment, Smollan, has over 15,000 people focused on retail brand management in South Africa, China, India and, next, Brazil. Recent comments by Walmart, for example, seem to indicate an even greater focus on global purchasing discounts and co-ordination with manufacturers, spelling more price pressure and referred pain for suppliers. At the same time, Procter & Gamble has taken a minority stake in Ocado, the UK's leading online home shopping, direct delivery food network to move closer to the customer.

### A quest for talent

Attracting, recruiting, developing, training, motivating, incentivising and retaining human capital remains crucial. While there is certainly too much production and capacity in general, one resource is in ever shorter supply in the 21st century – talent. Every statistic points to a reduction. The slowing birth rate, declining marriage rates, more working women, higher divorce rates, more single-parent families, smaller families, ageing populations – all these factors are reducing the supply of talent.

Even countries with strong, younger demographics, such as Mexico, will face similar situations by 2020. Some governments are trying to stimulate the birth rate. The Chinese government is said to be reviewing the one-baby policy and Russia is worried about its ageing 141 million population. Western Europe and Japan face significant longer-term economic growth issues as a result of the declining proportion of young people and an overall population decline. The elected and then rejected Prime Minister Shinzo Abe of Japan wanted to stimulate the Japanese birth rate, as one way of strengthening the economic growth rate. That is one reason why the rapid inclusion of Turkey into the EU is so important: another source of population growth, as well as immigrants to stimulate economic growth and access to the Muslim world.

In a less differentiated world, it will become more and more important for companies to stand out through the quality and responsiveness of their people. Making sure that your people buy into your strategy and structure will be increasingly important. Living the brand – operationally – will be critical.

### It's what's inside that matters

Probably the biggest block to progress for our clients – and indeed ourselves – is internal politics. Turf, territory and ego prevent productive change. If the chairmen or CEOs of our clients saw what we saw, they would be horrified. If they and we devoted half the time that they or we spent on internal politics on the consumer, client or competition, they and we would be considerably more successful.

You could argue that most of the communication we co-ordinate is aimed at internal audiences rather than external ones. Some people, such as David Ogilvy and Allan Leighton (when long ago he was at retailer Asda) have maintained that ensuring your internal constituencies are on side is often more important than external ones. Only when internal communications are working can your company talk positively to customers, potential customers, suppliers, potential employees, journalists, analysts, investors, government and NGOs.

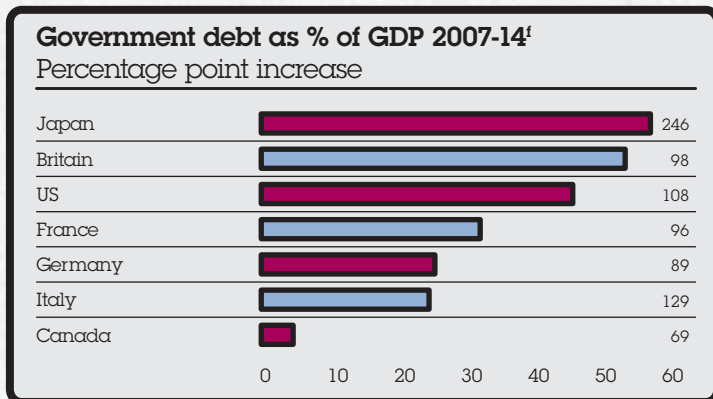
Building such virtuous circles in a uni-branded company is one thing. Inside a multi-branded company such as WPP, which has grown by acquisition, our tribes operate independently to deal with dis-economies of scale and client conflict. Things are far more complicated. Trying to ensure 100,000 people face in the same direction at the same time is not easy. On the other hand, once achieved, internal unison and common focus make a very powerful army. It may not be fashionable to talk about charismatic or strong CEO leadership; the focus is more on the CEO as coach, mentor or team leader. But our experience is that the most successful companies with which we work have CEOs who understand the importance of the brand, have a strong vision and implement that through a strong CMO.

After all, at long last, it is understood that all business strategy is really marketing strategy, starting with the consumer and working backwards from there. Most of our companies develop internal communications through Advertising, Media Investment Management, Consumer Insight, Public Relations & Public Affairs, Branding & Identity, and Healthcare and Specialist Communications. However, no single operating entity exists within WPP to execute internal communications on a worldwide basis. Still an opportunity for the future.

### The government as client

The speculative blowouts around the internet in 2001 and 2002, and sub-prime and insurance monoline crises starting in October 2007 were perhaps inevitable and, given their size, lengthy corrections were necessary. Overall, the past seven or so years have had their share of pain.

The US economy was in a political cycle in 2004, as the government used fiscal spending to stimulate the economy.



Source: IMF  
f Forecast.

Rates of growth in US government spending were back to where they were 35 years ago at the height of the Vietnam War. In 2005, the tragedy of Katrina, and the continuing demands of the wars in Afghanistan and Iraq continued to fuel the government spending spree. In 2006, the latter conflict continued the acceleration in government spending. It is no accident that governments in many countries are the largest advertising spenders: ministries use marketing to reinforce their policies and build electoral popularity. Perhaps for political reasons, former President Bush failed to deal with the twin fiscal and trade deficits. He chose not to raise taxes and Federal Reserve chairman Ben Bernanke did not hike interest rates even further.

All this was thrown into sharp relief by the sub-prime, insurance monoline, private equity and house price crises that started to hit hard in the third quarter of 2007. Everyone but Goldman Sachs seemed caught unawares – and, for a short time, even the masters of the universe were. Economic policy is in sharp reverse, with massive injections of liquidity and significant lowering of interest rates being the cornerstones of the new economics, as banks continued to refuse to lend to one another and third parties.

Given the massive Keynesian fiscal stimulus of around \$13 trillion and counting being pumped into the world's economy through government spending and guarantees, there was little doubt that the post-Lehman difficulties would be overcome in the short term. After all, the US and UK have even resorted to quantitative easing or printing money. But what happens in the long term? There seem to be two possible routes. First, the hair shirt route of reducing government deficits by cutting state spending and increasing taxes, thus increasing unemployment and encouraging a higher propensity to save. All very painful stuff as we saw on a smaller scale in the 1970s and 1980s. (The three-day week and rubbish piling up in the streets is the nearest we have been to the current crisis since the Great Depression.)

Or, which seems more likely, we inflate our way out long term. It will be difficult for government or even central banks to know when to withdraw the current support, particularly

as President Obama faces mid-term elections in 2010, the UK's Prime Minister Brown goes to the polls in May 2010 and Germany's Chancellor Merkel faces a crucial state election at the same time. It would be very unpopular politically to wear the hair shirt by increasing unemployment. Much easier to inflate our way out of it, reducing the real value of debt and increasing long-term interest rates. It is doubtful, however, that the redistributive and healthcare policies of the new US president will be effective to deal with the debt burden and, in any event, may have harmful effects on entrepreneurial motivation and corporate activity or eventually be rejected at the ballot box. If this scenario plays out, the high-saving countries – Brazil, Russia (getting its act together again as oil prices rise), India, China and even Japan – will benefit and pull further away from the West.

Inflation, of course, as long as it is controlled, is not bad for our clients or us. By giving our clients pricing power, branding and innovation become even more important, as long as private label does not become too dominant. Another consequence of massive government stimulus, effectively state directed capitalism (akin to the Chinese model) is government as a client. Country branding, foreign direct investment, tourism, export stimulation, reinforcement of government policy are all examples of marketing needs at government level – witness GroupM's win of the COI's media buying in the UK recently. The British government is currently the country's largest media spender but maybe not for long.

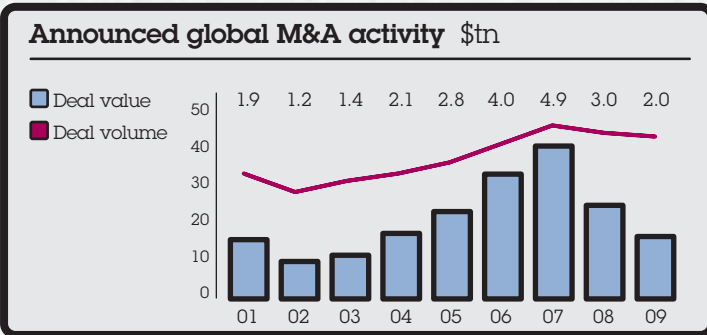
### Mergers are still with us

The credit crisis may have slowed activity, but mergers continue apace. NewsCorp took Dow Jones, Google took DoubleClick, Microsoft snapped up aQuantive, Yahoo! took Right Media, Microsoft took Yahoo!, Pfizer took Wyeth, Merck took Schering-Plough, InBev took Anheuser-Busch, Vodafone went for Hutchison Essar, Danone took Royal Numico, Bank of America took Merrill Lynch, Carphone Warehouse linked with Best Buy, Thomson Corp merged with Reuters, Kraft ate Cadbury.

Consolidation among media owners also continues unabated. NewsCorp takes and disposes of DirecTV, Comcast tried to take Disney and takes NBC. Legislation has favoured more consolidation in the US and the UK, although recent events and changes in administrations may alter that. Even in Brazil, which has been fiercely protectionist, you can buy 30% of Globo or Editora Abril. And in Australia, recently introduced legislation relaxing media ownership rules triggered a media asset bidding frenzy. Germany allows foreign ownership of TV; Italy concentrates further through the Gasparri Bill. In Spain, the government allows a 25% share of the free-to-air market and the Polanco family sells a television stake to Berlusconi's Mediaset and Antenna 3 and La Sexta discuss a merger. Clients and media owners are

## What we think

After the threat of apocalypse, new centres of gravity



Source: Thomson Financial as of March 2010

not alone: retail consolidates, too. Morrison takes Safeway; Boots and Alliance merge and go private shortly thereafter. In Latin America, Walmart enters the north east of Brazil by acquiring part of Ahold's interests, Lider consumes Carrefour's Chilean interests, and Jumbo buys Disco in Argentina. Rumours surround Walmart and Carrefour and Home Depot and Kingfisher.

In line with the laws of big numbers, the challenge to Wal-Mart, Tesco and Home Depot will be how they can successfully manage expansion outside their home markets. Tesco already has over half its square footage outside Britain (but much less of its profits) and has sent its UK managing director to the West Coast to manage its US expansion as Fresh 'n Easy. It will not be simple; the demands are different and the model will be significantly based on rehabilitating blighted areas on the West Coast. Early signs are mixed.

It is no surprise that agencies are also consolidating. Havas and Aegis, IPG and Publicis, Dentsu selling its 15% stake in Publicis in 2012 to buy a global network of its own (effectively a rolling \$1.2 billion equity put on Publicis by Dentsu), Ipsos, gfk and Nielsen being involved in significant consolidation activity in market research are all current rumours. Certainly in the one area where there are big economies of scale – media buying – consolidation is significant. To negotiate with a Rupert Murdoch, Sumner Redstone, Mel Karmazin, Bob Iger or Jeff Zucker, larger scale is essential. Media buying, or what we call Media Investment Management, is one of WPP's fastest-growing businesses, driven by clients looking for media-buying efficiencies – rather than reductions in agency's commissions. Like-for-like revenue growth in the last four years has consistently been well above WPP's overall like-for-like growth. Often savings on gross media budgets of 5-10% are achievable.

Media savings are driving client centralisations and are a quick kill in showing efficiencies, as Nestlé and Unilever have shown. The traditional media owners are not only having to fend off disintermediation by new technologies, but the pricing pressure from significant consolidation of media budgets. But even on the creative side, voracious procurement departments and ill-judged price competition by agencies themselves are driving consolidation (the \$100 million pitch win headline in *Advertising Age* or *Campaign* is more

satisfying than real revenue). We have seen two of our competitors desperately write cheques or subsidise account pitches to the tune of \$20 to \$30 million to retain accounts globally or in the UK – one of which decisions has been reversed in 18 months in our favour. Competitors seem to ignore the exponential risks of going short in markets that may be becoming increasingly long, by giving undeliverable media pricing guarantees and failing to book consequent balance sheet liabilities.

### Outsourcing – a way forward?

Growing consolidation in our industry is reducing the available resources for clients. It is ever more difficult to find co-ordinated resources that can deliver what clients require, particularly if they are an international, multinational or global company. Smaller, country- or city-based operations cannot offer the depth of coverage or breadth of resources.

One interesting recent development is the growing interest in outsourcing parts or all of the marketing function. Clearly this is an opportunity for us and is being driven by CEOs' focus on costs and their analysis of their investment in marketing services. Instead of concentrating solely on amounts spent outside the organisation, closer examination is being made of amounts spent inside the company. WPP has become involved recently in outsourcing projects in the automotive and internet services industries. In a number of other areas, including advertising, direct marketing and research, there is interest in what can be done in outsourcing costs. Clearly this tends to make internal marketing departments more defensive about their functions. We have seen much of this, for example, in the media buying area.

### Super-agencies: coordinating the best idea at the best price

Formed initially in response to the pressures of consolidation and to house conflicting accounts, the super-agencies – or what we at WPP prefer to call the parent companies – really represent the full-service agencies of the 21st century. Long before the phrase 'integrated communications' came into common use, integrated communications were exactly what such full service agencies provided. Over time – and as a result of two pressures – these departments became unbundled. Clients sought to reduce costs and the media and craft specialists within agencies, feeling under-recognised as members of a mother agency's department, looked for greater recognition and reward in free-standing, specialist companies of their own. Importantly, this involved a split between the creative agency and the media agency, reducing costs from approximately 15% of gross media costs to about 12%. Good media people left and started independents such



as Carat, Media Planning Group, CIA and Western International, which grew organically and by acquisition.

The same pattern was seen among packaging, market research, merchandising, PR and other specialist skills. Many such companies have now been re-absorbed into the super-agencies, but in an inter-dependent or autonomous form. Strong media or marketing services specialists do not like, understandably, to be subsumed under advertising professionals, particularly when they have enjoyed a taste of freedom.

As the new specialist media investment management agencies have grown in power, new media technologies have developed and the media agencies have developed strong client relationships. The creative agencies have become increasingly discomforted and called for re-integration. This is not possible in our view; the toothpaste is out of the tube. Media agencies have declared UDI and won their independence. They will not report again to account, planning or creative management. Similarly, media agencies should not develop traditional creative capabilities, even under the guise of digital. If clients want better co-ordination between creative and media agency – which in some cases needs to be improved – the best way to do it is by housing the media planners in the creative agency, but with them remaining employed by the media agency. The creative agencies have paid a heavy price for ignoring the importance of media. The medium is increasingly becoming more important or as important as the message.

Today, the new super-agencies have a big opportunity. Clients still require, first and foremost, creativity and great creative ideas. Second, but increasingly, they want better co-ordination (although it is no good co-ordinating a lousy idea). Finally, they want it at the lowest possible price. The challenge is therefore to provide the best ideas in the best co-ordinated or integrated way at the lowest cost. Until recently, this might have been seen as a fad, but now the concept may be taking root. Four major multinational clients – three of them with origins or significant parts of their business in Asia – invited four or five of the largest holding or parent companies to present for their global advertising and marketing services business. In all cases the presentations included advertising and media investment management, and direct – and in one case research. All these clients were looking for an integrated global solution to their needs and for groups that can offer alternative solutions – potentially a weakness of the single network.

In all four pitches, a group or parent company solution was selected. WPP tribes were successful in two of them. In the third and fourth, we were constrained by significant conflict issues. The CEO of one eliminated parent company in the first round of the first pitch declared that this was not a trend.

After at least four similar pitches, he has changed his mind and is pursuing a holding company approach.

In addition, many other group pitches have taken place – particularly in pharmaceuticals, and Public Relations & Public Affairs – that have been under the trade papers' radar. The only issue preventing this from being a trend is whether clients can be convinced of the benefits.

The middle of the road is becoming an increasingly difficult place to be, with traffic coming from both directions. Agencies excluded from the super-agency pitches because they lack the scale and resources must be feeling uncomfortable. Our business is polarising between big and small.

### The pressure on creativity

The days of 15% gross commissions – 17.65% on cost – are long gone. Commission levels have receded to around 12% gross for full service, including media planning and buying, or, as we put it, Media Investment Management. Production commissions have largely been reduced or eliminated, although there are interesting procurement opportunities for agencies themselves in television production.

While commissions persist, fees are becoming more popular with clients, although that momentum seems to have slowed recently. They now represent at least 75% of our business. Usually time-based, with incentives, they are used almost exclusively in our marketing services business, which accounts for 59% of our revenues. In advertising, they account for well over half of our business.

Fees have a number of advantages and, on balance, we prefer them. They are not seasonal, in a business where spending tends to be concentrated in the second and fourth quarters. January, however, has generally become a more rewarding month. If clients cut or do not spend or continually re-brief us, we still get paid.

Finally, when fee-driven, we tend to plan our annual business better. Fees have also tended to dampen volatility in our operating margins.

I cannot remember a time, in the 35 or so years I have been in the industry, when clients have been so focused on cost. Given overcapacity, low inflation and lack of pricing power and high management turnover and, most importantly, the still current economic crisis and the near Armageddon or Apocalypse Now of the Lehman weekend, that is perhaps understandable. However, the question remains whether the procurement process can successfully purchase creative services in the way door handles or widgets are bought. The emphasis on procurement seemed to start in the pharmaceutical industry and then moved elsewhere. It may work in media buying, where there are clearly economies of scale, but not necessarily in media planning or other creative areas.

It is true we must improve our processes and eliminate waste, but can you buy ideas or our people's creativity in such a mechanical way? Increasingly, pressure on price will

## What we think

After the threat of apocalypse, new centres of gravity

drive our best creative resources to clients and categories where their services are rewarded appropriately. Many marketing clients still appreciate that great advertising ideas and copy deliver outstanding results. Reducing marketing costs indiscriminately, particularly in industries with heavy fixed production costs, will only result in having to spread those costs over fewer unit sales.

The procurement process seems to be based on the idea that what we provide is low value-added and that, because we are dependent on significant revenues from large clients, we can be squeezed. This thinking may be flawed. First, what we do is critical. There is a limit to how far costs can be reduced; but there is almost no limit (apart from 100% market share) to how far you can grow revenues. Second, in an increasingly undifferentiated world, what we do – differentiate products and services, tangibly and intangibly – is becoming more and more important, particularly in the slower-growth markets of the US and Western Europe, where overcapacity, commoditisation and retail concentration are more pressing issues.

### Corporate responsibility: more important than ever

Many companies have made an increasingly important virtue and value of positioning their brand, goods or services as corporately responsible. If you are in the business of building brands, products, services or corporate brands in the long term, this is surely a given. If you want to build long-term profitability, you cannot dismiss the environment, society, government, NGOs or the press. Indeed, you would only ignore these constituencies if you were in business for a quick buck or short-term profit. We already know from our market research agencies that consumers and people inside companies value socially-responsible companies more highly.

BP in the oil and energy industry, HSBC in banking, and Walmart and M&S in retail are good examples of corporate responsibility. However, three relatively recent events have heightened the importance and significance of CR or Global Corporate Citizenship and made them very fashionable. First, the deal between Warren Buffett and Bill Gates, involving an exchange of Microsoft and Berkshire Hathaway stocks, to enable the Gates Foundation to do even greater charitable work. Second, the decision by Sir Richard Branson, at the second Clinton Global Initiative in New York, to donate up to \$3 billion in profits from his Virgin companies to good causes. And finally, the decision by James Murdoch at BSkyB and his father Rupert Murdoch at NewsCorp to espouse carbon neutrality – along with Al Gore's influential film, *An Inconvenient Truth*. All of these events have made it fashionable for chairmen and CEOs to embrace corporate responsibility – and embarrassing for them if they do not.

People will not consume luxury in the way they did until recently, particularly in Western markets, at least for some considerable time in the future. Responsible consumption will become more important, rather than conspicuous consumption. Consuming less in a more socially responsible way will be crucial – in relation to society, the environment and economy. Thus social responsibility will be more significant to the consumer, our clients, governments, NGOs and all constituencies.

### Conclusion

2009 was an uncompromising year. As forecast last year, it was a game of two halves. We did not play particularly well in the first half, but picked up our rhythm in the second. We moved from staring into the abyss, to a less-worse performance. So far in 2010 we have seen a return of stability, but not growth as yet. The second quarter should see significant top-line growth for the first time for six quarters, but mainly because of easier comparatives. Overall, 2010 should be flat or up slightly. 2011 should see similar, but not spectacular improvement, as clients get further over the terrifying post-Lehman experience, which restricted 2009 budgets, and realise that long-term growth depends on top-line expansion, not cost cutting in their budgets for 2010, 2011 and beyond.

Governments are now faced with a dilemma, a choice between the pain of higher taxes combined with government cuts to reduce the deficit – or inflating our way out of trouble. We can make it easier in the long term by wearing the hair shirt now, slashing state spending and raising taxes, with the resulting loss of jobs. Or we can make it easier in the short term by stoking inflation, with long-term interest rates rising. It is worth pausing to consider this paradox: we are being asked to spend and lend our way out of this recession. That, surely, is what got us into crisis in the first place.

Whatever the conclusion, WPP's strategy remains appropriate. New geographical markets, new media and consumer insights will become more important. Furthermore, globalisation, overcapacity and the shortage of human capital, the web, internal communications, concentrating distribution, corporate responsibility, the government as a client, and a balance between global and local organisational structures, will continue to drive branding and differentiation, and advertising and marketing services. ■



# Why a Ruritanian Poltergeist can be as Valuable as an Automated Processing Plant



By Jeremy Bullmore

**W**e're in the boardroom of a company that makes fast-moving consumer goods. At the heart of today's agenda is budget allocation for the forthcoming year. The two most prominent supplicants are the Production Director and the Marketing Director.

The Production Director has a meticulously-prepared case for an increase in capital expenditure. A concerning proportion of the company's manufacturing capacity is obsolescent. Working together, Production and Procurement have put their requirements out for tender and have interrogated the competitive proposals within an inch of their lives. They are wholly satisfied that they've got the most cost-effective deal. Full-colour plans and scale models are on display to augment the imagination. Visits have been made to other sites where equivalent plant has been installed – to the complete satisfaction of the operators. The suppliers' calculations of expected ROI have been double-checked and audited: the predicted payback is mouth-watering. Unless this programme is fully funded, competitive pricing of the company's goods may soon become impossible.

The Production Director's case is a sturdy one: proposed investment

at its most responsible, with deeply reassuring numbers attached to every item. Like the assets it's designed to protect and enhance, it's wonderfully tangible: it's concrete. And so is the language in which the recommendation is framed.

The Marketing Director is responsible for the company's brands. On the company's balance sheet, they are categorised as intangibles. Marketing budgets have traditionally been decided on the basis of last-year-plus-a-little. The Marketing Director's most high-profile recent campaign is aimed at teenagers and features a Ruritanian poltergeist who wears a kilt and is called Feliks. Although there's evidence to suggest that this campaign is greatly appreciated by its target audience, and sales are indeed buoyant, not every member of the Board fully appreciates Feliks nor is familiar with the largely digital media on which he features. When compared with a new robotic processing plant, a kilt-wearing Ruritanian poltergeist doesn't intuitively strike them as being as deserving a recipient of precious, finite funds.

The Marketing Director makes an excellent case. He doesn't resort to jargon, sensibly plays down the creative awards that Feliks has accumulated and musters an impressive array of research that demonstrates a strong correlation

between levels of marketing spend and his brand's market share and profit contribution. The Board listens attentively to his presentation and asks intelligent questions. But as the Chairman puts it in summary: times are tough, and there's universal agreement that costs must be contained. So on balance, with economic conditions being what they are, and with the brand's momentum looking gratifyingly healthy, rather than the suggested increase, perhaps some modest reduction in promotional support would be the more responsible course of action at this moment in time.

At the end of the Board Meeting, the Marketing Director is not as happy an executive as the Production Director.



The above cameo, of course, is fiction. But it was prompted by a remarkable investors' note issued by the Consumer Staples Research team from Deutsche Bank, Europe, in January 2010\*. Its stated purpose was to analyse "the effect of advertising and promotional investment on the consumer staples sector, its impact on profit growth rates and the likely shape of profit recovery coming out of the recession."

Throughout their report, the Deutsche Bank team use 'A&P' as shorthand for this investment.



Here are three of their conclusions.

■ **“Brands are critical in consumer staples** Intangible assets account for more than 100% of the market value of the consumer staples sector reflecting the power of brands built up over many decades. Indeed, just as Capex protects the tangible assets, advertising and promotional spend builds and protects the value of consumer brands.”

■ **“The importance of A&P is not well understood** A&P spend is the second largest cost for the staples industry and critical to the health of brands and thus valuation. However, financial disclosure of these items is generally poor and 73% of respondents in our investor survey said that they did not have a good idea of how the industry spends its marketing budget.”

■ **“Actions in recession key to shape of recovery** Our analysis shows that companies who continue to invest, grow faster, and we can see clear trends in terms of A&P investment during the downturn. The actions of companies through the recession have diverged significantly and it is those actions that we believe will drive the trajectory of subsequent profit recovery.”

Their analysis of over 30 large European and US consumer staples companies over more than 15 years shows “that companies that increase A&P to sales ratios deliver sales

growth 30% faster than those who do not.” And while it’s self-evident that cutting marketing spend delivers an immediate cost benefit, “companies that increase A&P deliver profit growth faster than those that cut A&P.” They add the chilling comment: “Losing market share can be quite a profitable experience – it is the cost of stabilising and rebuilding a brand that is expensive.”

What the Deutsche Bank note does, among many useful things, is to remind us of the remarkable differences in vocabulary, in the use of language, that are employed when we talk about a company’s different assets.

A company’s tangible assets are exactly that. They’re tangible. The money that is commonly agreed to be necessary for the maintenance and enhancement of those assets has a commonly agreed name: capital expenditure, or Capex. A public company’s Capex is necessarily disclosed.

A company’s brands, perhaps representing more than 100% of its market value, are called intangibles. Synonyms for intangible include insubstantial, elusive, vague, ethereal and indefinable. The money that every company knows to be necessary for the maintenance and enhancement of those assets has no commonly agreed

name. Among the 30 companies scrutinised, Deutsche Bank identified 10 slightly different terms for A&P expenditure. The precise composition of different companies’ A&P expenditures also varies widely – and in several instances, their expenditures are not disclosed at all.

To attempt to compare the relative values of Capex and A&P would be as pointless as attempting to determine which is the more important wheel on a bicycle. To be unable to make what you sell is neither better nor worse than being unable to sell what you make. But because of their uniquely elusive quality, the value of brands – rather more than the value of machinery – badly needs periodic championing; and so, it follows, does the importance of A&P.

Mere products may have life cycles – and tangible assets certainly do. But if nurtured and nourished by its A&P, a brand can be for ever.

It seems somehow appropriate that the only company asset capable of returning a profit for all eternity should be called an intangible. ■

**Jeremy Bullmore is a member of the WPP Advisory Board**

\* *European Consumer Staples: The Importance of A&P*, 15 January 2010. Deutsche Bank AG, Consumer Staples Research team. Extracts from Deutsche Bank note reproduced with kind permission.