



the profitability triangle

white paper

resource optimization in the marketing communications industry

Paper 1 in the Maconomy Profitability Triangle Series on resource optimization, pricing and compensation management in marketing communications organizations





introduction to resource optimization

The cost of compensating the people who produce the services sold to clients is by far the biggest cost item for marketing communications businesses. And it is less fixed than most other cost items. Therefore, compensation is by nature in focus when discussing how to improve the performance of the business.

Fundamentally, there are two ways of impacting compensation costs:

- Costs per hour
- Number of hours employed to deliver a given service

This paper will focus on the latter, which to a great extent has succeeded in escaping the debate up until now, despite its vital role for improving business performance. The “hours employed” takes into account the share of a total employment which can be related to delivering a given service.

The paper further explains how to boost utilization and achieve dramatically improved profitability. It also presents why making the change is urgent and what will happen if ignored.

Profitability Triangle Series

Big changes have taken place in the marketing communications industry during the last 10 years. Clients have become extremely conscious about what they get and at what price. Ownership has consolidated into about a handful global holding companies dominating the market. And new performance standards have emerged both for the big groups and the smaller independent agencies.

This paper is the first in a three-part series from Maconomy on the “Profitability Triangle” in the marketing communications industry, which is based on three drivers of profit: Resource Optimization, Pricing and Compensation Management.

By focusing on making these three drivers truly profitable, agencies can survive, and thrive, in their industry.

This paper focuses on resource optimization, in particular, the use of free agents. It should be read together with its companion papers on Pricing and Compensation Management.



Free agents at core of future capacity management

When taking a really hard measure of utilization – such as paid hours/total hours – a result significantly below 50% is not unusual. And it is not unusual that it is combined with considerable pressure for salary increases. Under the current pricing logic (defined as the relation between the price and the number of hours used) in most markets this would most likely prevent the business from becoming profitable.

A simple way of solving this problem is for marketing communications companies to buy just the amount of capacity needed to produce the services clients pay for. This means stop filling each of the functional silos in the organization with a hierarchy of employees with high salaries, long notice periods and unpredictable leave of absence.

Previously this has been difficult because the best people went for the positions with the best compensation, the most attractive fringe benefits and an appealing career path, rather than for the positions offering the most interesting professional tasks. This is no longer the case. Free agents are about to wash over the marketing communications industry like a Tsunami. A few years ago most free agents worked as such because they could not find a full-time job, rather than out of a desire for this work style. Today it is a lifestyle chosen by many of the very best individuals who want the challenge of shifting environments, tasks, clients and teams – and do not want the hassle from being a part of the increasing bureaucracy of a bigger organization.

This change makes a transition to a more temporary staff pool possible where capacity is bought by the hour or by the project.

Some will ask: “Is this not what we have always done with freelancers?” No, it is dramatically different. Freelancers are typically used to fill in the gap at the occurrence of illness or at an unforeseen peak in the capacity need. Or to do the jobs that the employees do not really care about and/or at hours employees do not want. As opposed to freelancers, free agents can be used as the very core capacity of the business.

Of course, it must be carefully considered how far this conversion from fixed staff to free agents should and can be taken. For example, management may want to retain some very top creative resources in an agency to make sure that such resources do not become unavailable at an uncomfortable time. Management may also find that it is better to keep in-house simple “production” aspects of the business that already run efficiently. In general, it should be all layers except the highest and lowest levels of the organization that should be evaluated when considering extensive use of free agents.

So how could this new organization look? The middle layer should be reduced but the top and the bottom layers of the hierarchy kept – the top because of its strategic importance and the “clerical” bottom because there is simply too little to be gained by outsourcing it. A traditional advertising agency without special services requiring particular competences is divided into client service staff, creatives and support staff. With about 50 people on payroll, two to three of the creative people should stay on – those who are excellent at pitching and those who are extremely critical to key accounts. Three to four of the client service critical to key account should also stay as permanent staff. With management and a few clerical staff, the permanent staff will be reduced from 50 to around 10.

There are even some unexplored competitive positions in this new world. One is to become excellent “orchestrators” of free agents and integrate them flexibly with your own resources. The best free agents will be able to pick and choose (just as the best employees do today) and the businesses could create an advantage in this market by becoming fully geared towards working with free agents as their main capacity.



How it will work

Businesses that want to prepare optimally for this new trend should start redesigning their infrastructure in a way that is attractive to the best free agents.

This implies establishing an interesting physical environment with full project orientation and mobility. Following only a few minutes of planning, team members will want to be able to work together and plug their laptops into a network that allows access to all relevant data and material.

But more importantly it increases the need for being able to match the competence needs arising from a detailed mapping of phases, tasks and activities on a project with a team that can operate optimally at all times. The businesses will need to know in detail which free agents in the market have which competences, who work efficiently together, who has what track record – alone and in teams – and what are the constraints in availability.

The companies that establish this first and best will get an enormous competitive advantage, because they will be able to offer the only element of the daily work life that the free agents will miss and need being free agents rather than employees.

Even in a world without free agents much of this will be needed anyway. Looking to the consulting industry – typically ahead of the marketing communications industry when it comes to adapting to market trends – the best of the consulting firms already have built an organizational model supported by advanced IT solution and infrastructure, where employees are not automatically assigned to certain tasks – and where they let the best suited at any time get the challenge.

Objections and obstacles to new free agent business model

It has been hard to drive utilization to desired levels for internal reasons – some call it the “prima donna employee syndrome”. Some people have an unrealistic self-esteem and claim little responsibility whatsoever for the commercial viability of their presence. Management has let this happen. A lot of managers are scared stiff by the thought of losing key employees and will allow almost everything to prevent it from happening.


Luckily, there is a shift in attitudes. Managers seem to have become more commercially aware and so has a younger generation of employees – they will more easily accept pressure for higher utilization. But these changes are no way near significant enough to balance the pressure from the free agent trend.

Utilization has also stayed low for external reasons:

Clients split their engagements in much smaller pieces than just a few years ago. This is of course troublesome and expensive to handle for the businesses that now need to pitch and price 3-4 times as many projects to achieve the same total volume.

These historic reasons for low utilization not only represent good arguments for moving towards a free agent set-up. They will also represent arguments against going there. Managers will still be scared stiff of the thought of not “owning” their key employees and clients will still require the business to do a lot of pitching.

That is all true, but if performed intelligently managers will actually be able to work with an improved palette of skills, not a reduced one – and clients will gradually reduce their distrust and award the business with bigger projects. Therefore, the business that converts to more free agents will survive and move into a much more interesting position.



Skeptics will also claim that the “culture” of an agency is vital to its position and will not be able to thrive and evolve if its human resources do not have a strong relationship to the company. “Culture” will likely become more important than it is today but take a different form where the physical infrastructure, the professional network, and the quality of the work become important elements. Free agents’ loyalty will be expressed by their enthusiasm or through their “bragging about who they are representing” – almost like the modeling industry.

A valid objection will be that abiding by clients’ demand of not working for competing companies will be impossible to control – how can one be sure that a free agent isn’t going to work for a competitor of the client? In certain cases, free agents will have to sign an exclusivity agreement where they promise not to work for a competitor of a client for a period of time. However, this “paranoid” attitude will become less and less prevalent just as it is seen in the Consulting industry – even in the management consulting area where strategic issues are in focus of the engagement.

Another objection will be that IT systems are not ready to support such a business model. That is also quite often true. A dramatic organizational change like this will only deliver full impact if supported by the right IT infrastructure that:

1. Provides access to project information anytime and anywhere
2. Offers skill-based capacity planning across internal and external resources
3. Makes handling of free agent compensation easy.
4. Fortunately such systems indeed exist.

Conclusion

It is unlikely that the marketing communications industry will allow the current set-up to prevail for much longer. Whether the proposed business model is adopted or not there will be lots of pressure to improve utilization and thus profitability both from owners and clients.

The large regional and global players will have absolutely no patience with poor performing core markets. The corporate governance standards will ensure that stakeholders will know of the details, ask questions and require action.

The huge investments that have been made acquiring companies include the geographical markets that are not considered core to the acquirer. Nevertheless, for many acquirers these non-core investments have become substantial and therefore they have also become a substantial problem when the non-core markets are poor performers. And they quite often are. The large players have lost their patience with the non-core markets and will demand that they perform up to the same standards as the major markets.

The independent businesses will in most cases be owned by people who are well informed about the benchmarks of the big players – and they will want to do significantly better because they are able to run lean.

As marketing communications companies have consolidated so have their clients. Clients have simply become bigger and so has the likelihood that the engagement is covered by an international agreement requiring full transparency and equal terms and conditions on all markets. Clients want to know what they are paying for, and marketing communications businesses will need to make sure that they are only buying what clients are willing to pay for.

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