Maconomy White Paper

Pricing management in the marketing communication industry

Paper 2 in the Maconomy Profitability Triangle Series on resource optimisation, pricing and compensation in marketing communication organisations

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– people made profitable

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

These changes will require a much more conscious management of the operating units in the marketing communication industry as businesses – not only as proud suppliers of professional services.

This paper is the second in a three-part series from Maconomy on the "Profitability Triangle" in the marketing communication industry, which is based on three drivers of profit – utilisation, pricing and compensation management.

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

This paper will explain how marketing communication businesses can work actively with pricing and the pricing mechanism. It also clarifies why attention on pricing is an urgent matter, which cannot be ignored. It should be read together with its companion papers on resource optimisation and compensation.

Pricing in the future

As in all other environments with fierce competition, future models for remunerating marketing communication businesses will not be based on one single system. Instead, a whole range of alternatives will exist from which clients can choose or even combine or modify according to their needs. The alternatives will range from: The simplest version of payment, payment according to consumed time at rate card level; 100% success related fees at various gearing aggressions and with more or less exotic success definitions; monthly retainers for a certain scope of work, share of media spend, share of production costs – or any combination hereof.

However, no matter what pricing mechanism is agreed upon with the client, there is a whole series of financially oriented tasks that marketing communication businesses need to go through in order to:

- Intelligently enter into pricing dialogues with clients
- Optimise the financial outcome of working for the client once the pricing has been agreed upon

Quite simply, these tasks are about understanding in depth the performance history working with clients and to allow this to have an impact on decisions about the future.

In most cases, a company will have some experience from working under a remuneration method equal or comparable to the one being discussed with its client. The systematic use of that experience and its profit implications will not only inspire the company to identify the terms for which it would want to settle for the new contract, it may also be an excellent piece of documentation which is highly relevant to share with the client. In particular when discussing the next project for the same client – but sometimes also in an anonymous version when it is another client. Clients will have respect for documented suggestions and concerns.

But the pricing issue is not over just because the terms are settled intelligently. Actually that's were the really big trouble starts: How can the business make sure that all action and behavior – on its own part as well as the client's – remain in line with the assumptions that constituted the basis for pricing the project?

Again, a systematic use of history – e.g. project history, client history, supplier history, collaboration history, product deliveries – is the answer, but for this purpose it need not only be systematic, it is also important that it is immediate. So in this context, history means yesterday. If a company has access to data that are up-to-date at all times and acts immediately on such data, it will gain the benefit from immediate impact from these actions. And its chances of involving the clients will be optimal – late involvement of clients in e.g. a perceived scope increase will rarely be unpunished.

Strangely, systematic use of history is a task grossly ignored by many marketing communication businesses today.

Another very different pricing tool which is grossly ignored is to organize and wrap the services in a way that makes them easier to buy. A huge chunk of marketing communication companies live from advising their clients on how to brand their products to make them easy for their customers to buy and to create loyalty. Yet they fail to take that medicine themselves and concentrate most efforts on the top level branding of their company name.

How it will work

Project scope management
The entry point to perform better on pricing is to look into the mechanism around the scoping of projects.

Most marketing communication companies today do perform a relatively detailed offer or budget per job they pitch to the client. That "document" is shared with the client and/or kept on file internally. But it is rarely recorded in systems of the company in a way designed for stringent automatic follow-up on the scope of the project. Scope management is considered a task for the IT industry but the marketing communication industry needs to get to a scope thinking mentality similar to the IT industry.

Company-specific standard expressions for the scope of a project need to be developed. The initial scope and subsequent changes need to be described in those expressions and the consequences evaluated. When processing a large number of projects, this can only happen efficiently if managed in a system with tight procedures on how to keep updated. Any client meeting should trigger a scope evaluation. Any change should be recorded and entered into the project management system immediately.

Financial Project Management
Today's understanding of the financial impact of the business activities typically arises from reviewing profit and loss information in a way characterized by the following:

- Low frequency – e.g. monthly
- Starting out at gross income (after all external project costs)
- Summary level – typically the entire business unit or at best by the big clients
- Performed by people who are not directly involved with managing client projects

This leads to situations where clear opportunities to act promptly on overruns and scope changes are not utilised, where the detailed knowledge about all spending recorded between billings and gross income (i.e. all the external project costs!) in reality sits only in the heads of the clerks keying in vouchers in bookkeeping, where the profitability of each project is not necessarily understood and where the people who actually make the decisions on the projects in reality work completely blindfolded.

It goes without saying that this is a big mistake which can (and does) lead to catastrophes in particular in situations where all of the above elements flourish.

The system used for managing the scope of projects should link into the financial management of engagements. Overall, the systematized processes must comprise all it takes to optimise a running project and to price the next project intelligently.

Financial management needs to be seen as a key management discipline, and steps need to be taken to ensure that financial impact of activities are reviewed in a way that has the following characteristics:

- Is done daily, with on-line access to real-time data
- Is all-inclusive – Comprises everything that hits a job number (i.e. including all external costs)
- Looks at details by project level and when appropriate even project phase level
- Is performed by client service employees

To get to this point it is often needed to rethink both systems and organization.

For many, it will represent a dramatic (but needed) change that a whole bunch of financial tasks are suddenly performed by client service rather than the finance department. Finance can produce numbers recorded and presented to the sharpest standards – and even help to interpret the numbers. But daily acting on the numbers must be handed over to the client service department who makes the daily business decisions.

In many organizations it will be a dramatic change that each and every employee – including management – needs to report time on a daily basis. This is necessary to allow hours to hit the job ledger instantly, thereby making the time spent visible real-time.

All of this is needed. Client service needs to know immediately when suppliers exceed their offers, when unexpected types of costs hit the project and when an individual who should be done with his tasks keeps on charging hours to the project. How else can client service make instant corrective actions? How else can client service learn and price the next project more intelligently? How else can client service know when the projects of a certain client always end up in losses and that the client is therefore contributing to the company with losses and cash drain?

Wrapping of services

Marketing communication companies need to not only teach their clients how they can organize and wrap their products. They also need to better organize and wrap their own services. Even law firms have started doing that. Every human being – private consumers as well as professional buyers – prefers to buy something that has a look and a name. The marketing communication companies need to closely examine their specific offerings to the market and make sure they have a look and a name. Some are already doing this with great success. For example, some PR consultancies are successful in selling a crisis readiness management package that gives access to certain resources within a certain number of hours against a monthly subscription fee. Certain marketing agencies are successful in selling a standardized marketing strategy review as a prerequisite first thing they do for any new client that they gain. Without it they will not start to work. Quite smart at a point where the client's barriers are low and the willingness to spend high.

But these are only examples on really nice bread and butter activity for communications companies. Only the imagination sets the limit for how far this can be taken.

How did the current situation arise and what are the obstacles to changing it

The marketing communication business has a long history with media commissions as the primary source of remuneration. It also has a long history of always pursuing the long and bumpy road towards the ultimate creative idea – with full acceptance of the clients, of course, as they were paying the same amount of money anyway. In this environment, creative people did not perform even simple, infrequent time reporting.

This has obviously not been an ideal environment for creating strong price/delivery consciousness and tightly run client handling and pricing mechanisms.

Therefore it is no wonder that it has taken so long to adjust to more lean and mean market conditions and that the fundamental barriers remain intact.

One such barrier is convincing client service employees to become project finance managers. To many client service people, financially oriented tasks are either low ranking, considered difficult or both. Very often the change will require staff changes in client service. Some may ask: "Can it be that finance issues are triggering the change of a client service person?" The answer should be: "Yes indeed – because project finance management is a top priority for client service people." Fortunately, it is not nearly as difficult to get the finance people to give up these tasks. They will see the point even though some of them will risk loosing their jobs as a consequence of the process.

Another objection will be that systems are not ready for it. That is also quite often true. A dramatic organizational change like this will only deliver full impact if supported by an IT system that:

1. Offers an advanced project scope monitoring facility
2. Provides access to detailed up-date financial project data anytime and anywhere
3. Allows for a product dimension across projects and clients.

Fortunately such systems indeed exist.

Conclusion

It is unlikely that the marketing communication industry will allow the huge potential profitability boost arising from intelligently managing the pricing process to remain unexplored for much longer.

Patience lost for poor performers

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 these non-core markets are clearly 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.

Demand for value and full transparency

As marketing communication 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 communication businesses will need to make sure that they are only buying what clients are willing to pay for.

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