AGENCYMANAGEMENTROUNDTABLE

MarketWise

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This was a "stinko" year.
Just awful, but filled with opportunity.

It *was* a stinko year.

There's no question about it that Q3 and Q4 of 2008, plus all of 2009 have tested the mettle of agency owners and put all of us in a precarious position.

As we finish 2009/Q4 we can look back on the trials and tribulations that agencies have gone through this last year. Some of it is pretty, some of it ugly, but still laden with opportunity for the future.

No one needs to tell you that the economy has been the major negative influence on the industry, particularly the "Mom and Pop" segment with fewer than 50 employees.

Add the negative influence of the economy to the force of interactive marketing and emerging media and you have a recipe for big problems. We got the double whammy: the down economy, plus the exploding influence of the internet in all forms. Most marketing communication firms just weren't ready for the impact.

The result? A year that had record business failures in our segment. I've read reports that say one in five marketing communication firms failed. Ouch! If you do any email marketing at all, just take a look at the number of delivery failures. The positive side? Those people who worked for defunct businesses have started new companies, are working freelance or have left the business altogether.

Recap the Year

"Confusing" is a good way to describe the start of the year and through the second quarter. We had a new President and an abundance of government programs to try to stimulate the economy. We still have to wait to see the full impact of those early decisions of the Obama administration. Whether you agree with the programs or not is almost immaterial. We all have to cope with the impact, or lack thereof, on our own businesses and our clients' businesses.

Although credit was supposed to be easier for the consumer to find, credit became more difficult for small business. Most agencies I'm in contact with regularly, reported a whole bunch of new "charges" from their banks that their lines of credit were shortened and interest rates increased. In some cases, the line of credit was cancelled.

Almost all companies I talked with reported that their accounts receivable increased because clients slowed their pay cycles. Another double whammy. Altogether many firms found themselves in a cash crunch, not knowing how to make the next payroll.

The AMR Magic Spreadsheet tool helped many forecast their cash flow against operations before they got into serious money problems. Watching cash flow has become a primary management tool.

From the spring through the early fall, there was significant improvement. Some of the promises made by clients seem to be coming to fruition, with project work coming back into the system. What is absent is the overall agency of record work.

The biggest gains are being made by the agencies that went on a mission to transition their focus from what they had been doing to more interactive work led by SEO, SEM and social marketing programs. Public Relations firms and agencies with good PR practices have enjoyed a smooth transition.

What we may be experiencing, and I sincerely hope we are not, is a "bubble" in work caused by year end needs that have gone unfulfilled. Clients are certainly more willing to talk about their business objectives with us and look for a solution… that's very positive. We'll know if it's just a bubble as we get into 2010.

Staff Size and Payroll Takes a Hit

Because payroll is our largest expense, this is the first place everyone has gone to reduce expenditures. Because agency owners are all such a positive group, hoping for the best, they probably hung on to staff longer than they should have. Overall, agency FTEs are down almost 25% on average with some reporting reductions of more than 50%.

The pressure on payroll expense forced AMR clients to be creative in making reductions.

- 95% Reduced staff size
- 95% Salary reductions by 10% or more
- 83% Salary reductions by 15% or more
- 55% Salary reductions by more than 20%
- 60% Reduced payroll by having staff take un-paid leave of up to 5 days per month (some of these firms reduced the work week to 4 days, thereby effective reducing payroll by 20%)
- 85% Owners took salary reductions greater than staff, or took no salary at all.

About 40% of AMR employees left the company following payroll reductions. I am amazed at this statistic. Where do those employees think they are going to get a job in this economy?

As we approach the end of the year, a small percentage of our clients are restoring some of the payroll reductions as well as hiring additional staffers. These companies have started to change their focus to include a solid position in the interactive arena.

The primary effect on staff-size reduction is that members are finding they can get a higher AGI$ per FTE than in the past. They have also effectively outsourced work to freelancers with the result being the cost of freelancers goes into cost of goods sold and not into the payroll categories.

Right now, AGI$ per FTE is increasing mostly due to reduction in lower paid positions. Even after salary reductions, owner and management earnings tend to skew the numbers higher. The good news is that the margin between the AGI$ per FTE and the Payroll per FTE has stayed the same or even expanded.

In most cases the reductions in payroll is not large enough to cover overhead costs, leaving the company in red numbers.

Changes in AGI$

In the first two quarters of the year, about 3 in 4 agencies AMR works with were within 15% of 2008 numbers. As the year went on, that number shrank to less than 50%. Through November, almost 80% are behind 2008 AGI$. The results sound like a disaster, but through good business practices of managing to AMR benchmarks, almost all firms have reduced expenses to at least stay in the black. About 12% of the members are in the red.

The good news is that roughly 18% to 20% are ahead of last year…some substantially.

Members with a strong footing in interactive are showing impressive results. It isn't a secret that the future is with the majority of AGI coming from the interactive segment. One firm, in particular, shows an increase of more than 50% over forecast because of their strong Whale Hunting new business development program.

What percentage of your AGI$ comes from interactive initiatives? You need to start tracking the contribution. Target 50% in the next year, and even more in the years to come.

Changes in Business Model

We are seeing a change in the business model. No longer do we think we must have a full time position for some functions, or at least not as deeply staffed. The availability of freelance talent and the high cost of full time employees complete with benefit packages have led us to using more freelance talent and creating strategic partnerships when the need arises.

The firms that are successfully migrating some of their business over to the interactive disciplines have reduced graphic design staff and replaced them with the beginnings of an interactive staff. The first of these positions seems to be an "an internet strategist" who can also fill in on the SEO and SEM work. After that position is solidified web designers and content developers join the team.

Another change is in the client services area. For the most part, weak account managers were caught in the staff reductions. We now see growth in this area. However, the account personnel are more strategic and prone to understand that their main objective is understanding the client's business and solving business problems…not just dealing with problems emanating from marketing communication issues. These new account personnel seem to have more business undergraduate degrees than a BA in other disciplines. They are intimately familiar with the emerging media. The majority of them are in their first or second job since graduating. Some have just recently graduated.

The downside of downsizing is that many more principals are spending more time working in the business than on it, but I think that is necessary in these times. With fluctuating cash flows, changes in staffing requirements and the pursuit of new business, everyone has a full plate.

There is no question in my mind that smartly run agencies will grow back to their original numbers, but the AGI$ per FTE will increase and the payroll per FTE will stay the same or even go lower. The source of the AGI$ will be different. I believe that the indicators are there for that to happen.

Market Confidence

Since July, I've seen a marked improvement in attitude toward business operations. As we approach the end of the year there seem to be more positive signs than negative ones. We are beginning to see some recovery. Of course, we'd all like to see a "V" shaped recovery – pulling out as fast as we got into this mess. Too many economic factors will probably hold that down into a more "flat" or slightly increasing recovery through the next 12-24 months. But, don't be discouraged, because there is definite opportunity out there. We just can't "do business as usual." There is a new normal that is not clearly defined.

My concern is that some clients are not devoting enough of their resources to develop the interactive and emerging media capabilities. They are stubbornly hanging on to old business models and are still billing time for creative and production services. By the end of 2010, everyone should be getting about 50% of their AGI$ from interactive initiatives.

Firms that have transitioned a good portion of their business into interactive are the most positive about impending recovery. They are producing good numbers and are challenged by learning new marketing tools; working on an annual fee or on a project basis; earning fees for bundled services; pricing according to an agreed upon value to the client; and, participating in some form of performance compensation.

I saw, in the newspaper today, that we are starting to dub this The Great Recession. One thing for sure… we always learn from recessions. Recessions ultimately become a "spark" to move up to another level, and I don't think this one is any different. Our businesses are being redefined. They are going to look different, define new offerings and change the way we are paid.

I've always felt that we (as agency owners) see the downturn in the economy first and are also first to feel the rumblings of a recovery.

It was a "stinko" year. Too many companies closing their doors; too many employees losing their jobs; too many clients trying to do more in-house; to many clients pulling back on their marketing and advertising plans; too many, too many, too many.

The good news? We are getting through this Great Recession. We will benefit from it because we will redefine our businesses and our offerings. We have all been forced to take a good, hard look at what our business is all about, and how we operate it. I think that this "stinko" year has done us a favor. In the long run our industry and our own businesses will be stronger going forward.

It was a "stinko" year, but the future is bright.

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