

## Future Financial Prospects

# SURVEY

Since the beginning of the recession the last few years within the media and marketing services industries have been a bit of a rollercoaster. No one is quite sure whether we have completely avoided a double dip recession and things are finally starting to look rosy or whether there is more bad news around the corner. Planning for the future, whilst perhaps a little easier than in 2009 and 2010 is still difficult. Everyone is therefore naturally interested in the views of the industry as to what the future holds.

Earlier this year we conducted a survey into the views of managing directors and finance directors of marketing services, media and consulting businesses on the future financial prospects of their industries.

**THE OVERALL FLAVOUR OF THE SURVEY RESULTS WAS A POSITIVE ONE - ALTHOUGH THERE WERE INEVITABLY SOME MORE DOWNBEAT VIEWS**

It was encouraging that after such a gloomy few years the overall flavour of the survey results was a positive one - although there were inevitably some more downbeat views  
The majority of respondents thought that both

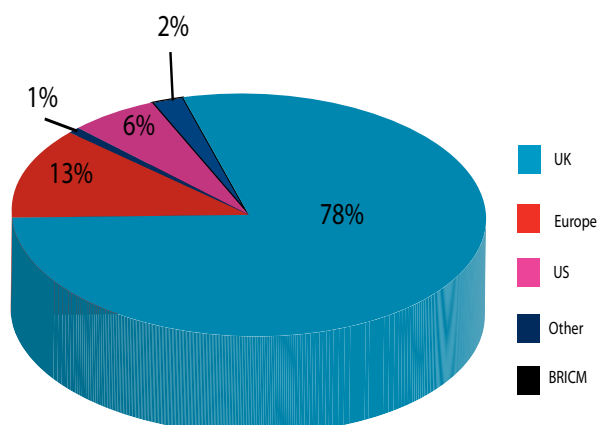
**NOT MANY WERE HOPEFUL THAT MUCH OF THIS INCREASED OLYMPIC SPEND WOULD FLOW THROUGH TO THEIR REVENUE STREAMS**

income and profit levels would be higher in 2011 than in 2010 and most were also looking to recruit to expand. Most agreed that the Olympics would also have a positive impact on marketing spend, but were divided over whether this would be seen in 2011 or 2012, however not many were hopeful that much of this increased Olympic spend would flow through to their revenue streams.

Our survey comprised answers from agencies representing the major marketing services disciplines as well as a number of market research agencies, consultancies and TV production companies of a variety of sizes. Of those responding the majority, 83%, were independent agencies or part of an independent group.

Whilst the geographical footprint of the sample was mostly UK at 78%, there was a healthy 13% coming from other European countries and 6% from the US.

### Where does your business come from?



## Revenues Predictions

An encouraging 60% of respondents predicted that revenue levels in 2011 would be higher than 2010. The more positive attitude towards revenue growth came mostly from those working in digital, design and branding and general consulting.

It is not surprising that digital agencies are forecasting that income levels will continue to grow, they were probably the least badly hit during the recession and digital marketing budgets are generally still on the increase. Design and branding were hit pretty hard during the recession and so perhaps their optimistic look at 2011 will merely restore income levels rather than reflecting any actual real growth since then.

Advertising and PR agencies were moderately positive about growth. As media spend starts

to recover one would expect advertising agencies to benefit. PR seemed to just about hold its own throughout the recession with the exception of consultancies exposed to the public sector or to M&A work and so no real bounce back to be had for most. Moderate growth for both sectors therefore seems realistic.

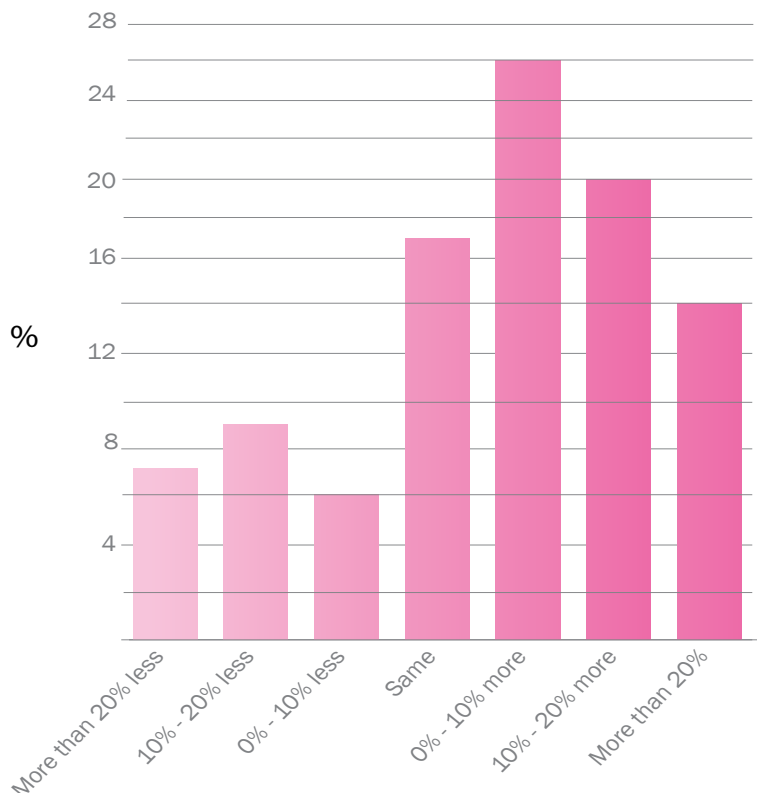
### THE MORE POSITIVE ATTITUDE TOWARDS REVENUE GROWTH CAME MOSTLY FROM THOSE WORKING IN DIGITAL, DESIGN AND BRANDING AND GENERAL CONSULTING

Of the remaining respondents a pessimistic 22% are expecting 2011 revenue levels to be worse than in 2010 and the remaining 17% expect revenue levels to remain the same

as 2010. Whilst there was a positive flavour to the responses overall it is concerning that over a fifth are expecting revenue levels to decline.

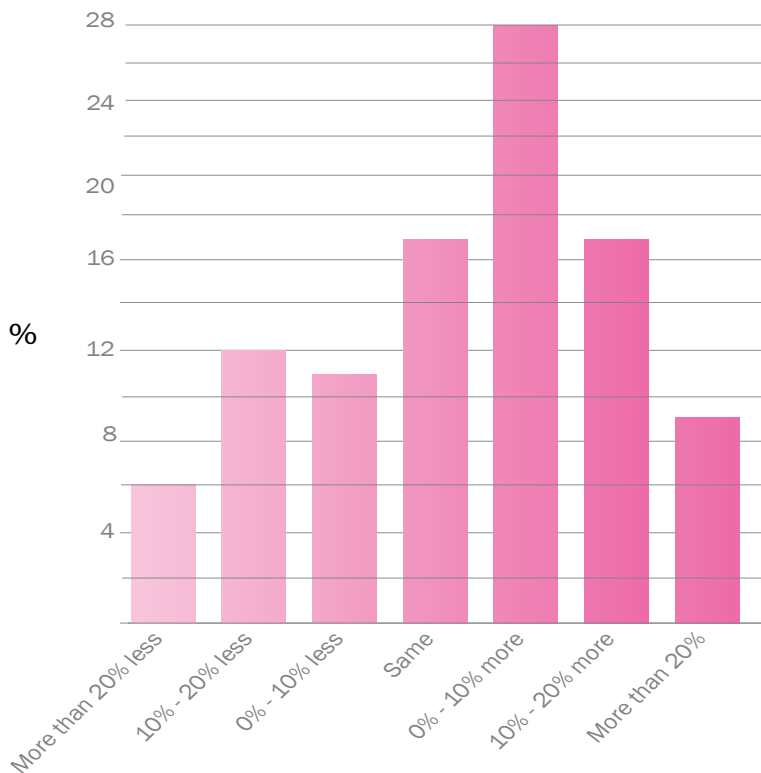
Overall DMSP was the most pessimistic category of respondents with almost as many forecasting that revenue levels would be worse in 2011 as those who thought that they would be better. However, they were also the category with the widest range of predictions. Nearly a third of DMSP agencies predicted their revenue levels would increase by more than 20% in 2011, and the same number thought they would likely be down by over 20%. It is important that DMSP consultancies invest in digital capabilities and don't lose big chunks of marketing spend to the digital agencies. Perhaps the extremes of responses here reflects those consultancies who either have or haven't yet invested in that area.

How much better or worse do you think your revenue levels will be in the calendar year 2011 compared to 2010?



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How much better or worse do you think your profit levels will be in the calendar year 2011 compared to 2010?



## Profit Predictions

How did businesses think that changes in revenue would affect the bottom line? Only just over half forecast that profits in 2011 would surpass those in 2010. Although most of these were cautious in their prediction and considered profit would only improve by up to 10%. Over a quarter of respondents thought profit would fall in 2011 and just under a fifth predicted profit would remain broadly constant.

In the branding and design and digital categories of respondents there was almost unanimous agreement that profit levels in 2011 would be better than those in 2010. However, advertising agencies were a little more downbeat and slightly more thought profit would actually be lower than those who thought it would improve.

Generally throughout the marketing and media industry profits dipped dramatically from 2008 to 2009. Following lots of redundancies, cost cutting and restructuring during 2009, the profits delivered in 2010 generally showed some recovery.

However some were still undergoing changes in early 2010 and so the full benefit of this will be expected to be seen in 2011 results. However, despite this, and the fact that most are expecting revenue levels to increase, this will be countered to some degree by the pressure still being exerted by procurement departments wanting a lot more for their money. So perhaps it is no surprise that most thought any profit improvement would be modest.

## Staffing Up or Down?

Just over half of respondents expect to be recruiting to expand during 2011, whilst just under a fifth predicted a recruitment freeze.

It was no surprise that both samples of brand and design and digital agencies almost unanimously agreed on across the board expansion in staff numbers, following their positive predictions regarding increases in levels of income. However, more surprisingly,

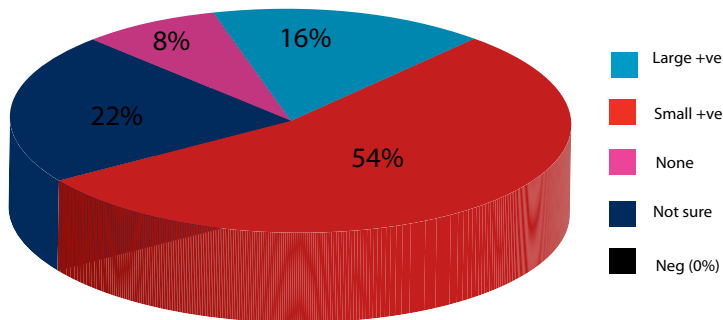
whereas DMSP agencies were undecided about whether income and profit levels would be higher or lower in 2011 than 2010, they almost all said they would be recruiting to expand rather than keeping staffing levels the same.

Whilst PR agencies were mostly more positive about income growth than not, most said that they would be holding staff levels, a shame then that they were not generally more positive about growth in profit.

It is very important that marketing and media agencies keep a close eye on staff costs as they are likely to be the biggest part of the cost base. At Kingston Smith W1 we recommend that marketing services agencies do not spend more than 55% of revenues (being turnover less cost of sales) on staff costs. Those who do manage to contain it to this level are those that have consistently high levels of profits.

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Do you think the Olympics will have a positive impact on UK marketing budgets?



## The Olympic Effect

So, we have the much talked about Olympics in a year or so. But how does the marketing and media industry think it will affect them?

The majority of respondents, 70%, considered it would have some positive impact on UK marketing budgets. However, although the majority of those thought the impact would be small only consultants generally thought the impact would be higher. Some 8% of respondents thought it would have no impact at all.

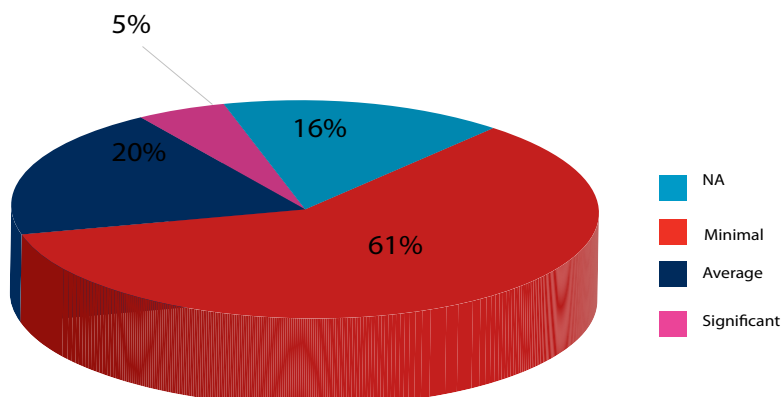
Of those predicting a positive effect, the majority, 54%, thought the impact of increased spend would occur during 2011 whilst 44% considered it would be in 2012.

Disappointing though, that when asked specifically what impact, if any, marketing budgets would have on the participants' own revenues, most, 77%, said the effect either wouldn't effect them or the effect would be minimal and only 20% thought the effect would be average.

Many who specifically commented on this thought that most of the upside in spend would be enjoyed by some of the larger network agencies as these tended to be those who held the accounts for the larger international brands who would be sponsoring the Olympics.

A few who did happen to already work with some of the sponsoring brands thought that they would benefit modestly, however similarly there were those that predicted most Olympic spend would simply replace other spend rather than be in addition to it.

What do you think will be the extent of any positive Olympics impact on your revenues?



## Anyone for M & A?

Since around the time we launched our Kingston Smith W1 Corporate Finance offering we have seen a marked increase in M & A activity, particularly within the marketing services industry. This followed a long period of fairly low activity during the back end of 2008, throughout 2009 and into the first half of 2010

However, when asked, only 5% of respondents

**SIGNIFICANT LEVELS OF ORGANIC GROWTH OVER THE NEXT FEW YEARS WILL BE TOUGH AND SO BUSINESSES WITH AN AGGRESSIVE GROWTH STRATEGY WILL NEED TO CONSIDER ALTERNATIVE WAYS OF INCREASING REVENUES.**

said they were considering a sale, and these were only in the advertising, PR and DMSP sectors. I suspect the truth will be that certainly a number of the digital agencies, even if not specifically looking to sell, will be courted and succumb to the charms of either one of the fully or AIM listed groups or even one of the private equity investors that appear to be coming back into the market now.

14% however said that they were considering an acquisition, which considering that the majority of respondents were independent agencies or part of an independent group is quite high. In fact nearly a quarter of advertising agencies and 30% of digital agencies responding said they were looking to acquire.

That acquisition is on the minds of many is perhaps not all that surprising. Significant levels of organic growth over the next few years will be tough and so businesses with an aggressive growth strategy, perhaps in order to facilitate their own exit, will need to consider alternative ways of increasing revenues. Trying to identify financially weak targets but with future potential on the cheap seems to be on the minds of many that we speak to.

I suspect that expansion into other territories will also be on the cards for some businesses. We are holding a seminar on expansion into BRICM territories this June and so I see another survey into geographical expansion coming on! support.

## About us

Kingston Smith W1 is based in London's West End, and the seven partners specialise in advising creative, communications and consulting businesses on all aspects of finance, audit, accountancy and tax. Kingston Smith W1 is a specialist division of Kingston Smith LLP, one of the UK's top 20 audit and accounting firms.

Many of our clients are advertising, digital and other marketing services agencies but we also work with many TV and commercial production companies, consulting firms, live entertainment and music agencies. Our clients range from sizeable independents and multi-nationals, to start-ups, which we have advised on a range of financial and business issues.

The businesses we work with have similar sets of challenges and opportunities, and with people being their key asset, employee incentive schemes and succession planning are just a few of the areas where Kingston Smith W1 regularly gives tailored advice. Other issues such as recruitment, HR and remuneration are also very important. As part of Kingston Smith we can provide recruitment services through Balanced People, HR consultancy through HR Insight, and employee benefits advice through Blacktower Financial Advisers (authorised and regulated by the Financial Services Authority (FSA)).

Kingston Smith W1 and Kingston Smith W1 Corporate Finance also regularly advise in many other specialist areas such as business valuations, profit improvement reviews, business planning, due diligence on acquisitions, fundraising, grooming for sale and pre-sale tax planning. Through the data we collate in our annual survey 'Financial Performance of Marketing Services Companies', we are also able to give invaluable benchmarking advice on numerous key performance indicators. By working with businesses with similar challenges, we can understand our clients better and are able to advise on a wide range of financial and non-financial business issues to a greater depth.

## Contact us

If you would like to discuss any of the matters arising in this edition or how we can help you, please contact one of the Kingston Smith W1 partners by email or on 020 7304 4646.

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