International ad agencies: Early players in the globalization game

Long before globalisation became a buzzword, large international advertising agencies had already gone down that road starting in the 1990s. By aggressively expanding their domestic and international networks through mergers and acquisitions (M&A), these large communication agencies pursued a strategy to place multiple agencies under an umbrella holding company. The evolution of the global network communication agency (GnCA) resulted both from large agencies acquiring small agencies and also from mergers between large agencies.

Singapore Management University (SMU) corporate communications professor Mark Chong, in a working paper on International Diversification of Communication Companies, states that this development was driven by agencies who believed they could gain a foothold in the international market in combination rather than individually.

Benefits of globalisation

The preference of clients to streamline and integrate their brand communications across countries spurred communication agencies to take the globalisation route. Citing a 2005 article by Nooren O’Leary in Adweek, Chong highlighted the fact that agencies with global reach have the advantage of offering a single point of contact for coordinating marketing activities, improved cost efficiencies, greater coherence in marketing “voice”, and access to the agency CEO in times of crisis.

Another advantage of the holding company arrangement, states Chong in his paper, is to allow companies to offer one-stop global communication services while avoiding a conflict of interest. The Interpublic Group in the world’s first communication holding company set up to get around the conflict of interest issue. Member agencies would function autonomously and handle competing accounts without compromising client confidentiality, according to the paper.

Economies of scale are another driver for the globalisation trend. Clients became increasingly likely to have bigger budgets and reached lower rates than were previously common. Thus, selected agencies were guaranteed a certain annual volume of business but at lower rates. With consistent volume that could be projected, larger agencies avoided the “hit-and-miss” cycles associated with gaining and losing accounts, says Chong.

As large agencies continued to build up capabilities, clients benefited from gaining access to specialist and other emerging services, especially in the digital media arena. Such firms became targets of acquisition by communication holding companies. The strategy to offer services in emerging communication services like digital advertising enabled the holding companies to mitigate against a decline in traditional advertising businesses in the more mature markets. Chong cites a 2007 article by Ken Whiston that shows that Omnicom, WPP, Interpublic, and Publicis generated and grew worldwide revenues in 2006 from emerging marketing services.

Agency and client perspectives

According to the paper, whilst the push for M&As was initially client-driven, subsequent industry alliances were prompted by other dynamics that were mainly agency-driven.

Among the key goals were greater profitability and higher turnover provided the incentive for subsequent alliances, whereas other initiatives were prompted either by defensive or aggressive causes to counter competing agencies. Defensive acquisition can be seen in some of WPP’s activities such as the purchase of Grey Worldwide and attempts to prevent the expansion of M Boelé’s empire. One other development has been the industry’s entry into the stock market making it necessary for companies to achieve critical mass to meet financial targets. The advent of global product branding began in earnest in the late 1980s and early 1990s. Citing a 2001 study by Marje Tharp and Janeide Jeong, the paper notes that multinational advertisers generally prefer working with agencies able to design, implement and manage global campaigns. This led communication holding companies with headquarters in New York, London, Paris and Tokyo to acquire national agencies to provide better global services to international clients.

Paradoxically, according to Chong, globalisation also gave rise to another development known as “globalisation”, intriguing demand from clients for a hybrid strategy that emphasised controlled globalisation-setting together with decentralised local implementation.

This allowed for the development of a creative strategy centrally with flexible execution to suit a variety of socio-cultural settings in different markets. Hence, national or local agencies acquired by holding companies generally continued to be headed by local managers with good understanding of the local market and established relations with the media and advertisers.

According to Chong, the number of global communication agencies has been reduced from eight in 2002 to only six agencies in 2005. “Following acquisition of Bcom3 and Greer, the globalisation of the industry today concentrates power within a handful of players. The six global communication companies comprise Omnicom and Interpublic from the US, WPP from the UK, Publicis and Havas from France, and Dentsu from Japan,” he says.

Measuring success

Data for international diversification of the six companies were collected from three archival sources: company annual reports, the DDC Platinum Mergers and Acquisitions database (a standard industry source for information about such alliances) and the Thomson One Banker database. The analysis covers the period 2000 to 2006.

Apart from reviewing the strategy of international diversification from three perspectives, namely, extent, direction and mode of diversification, annual financial results were also examined to measure performance in terms of sales, annual growth, profitability and management effectiveness.

In terms of overall ranking, the data reveals that Publicis was the most internationally diversified of the holding companies for this five-year period, followed by WPP and Omnicom as second place and Havas, Interpublic and Dentsu in third place.

With regard to the number of countries entered by companies through M&A transactions, WPP was found to be the most aggressive with Omnicom and Publicis in second and third place respectively. These were followed by Interpublic, Havas and Dentsu. Interestingly, the data shows the continued importance of domestic markets for the six holding companies; they carried out more M&As in their home markets as compared with international markets.

The three most important regions for the six communication holding companies were Western Europe, North America, and Central Asia/Asia Pacific. WPP was, by far, the company with the most acquisition activity, followed by Dentsu in Western Europe, followed by Publicis, Omnicom, Havas and Interpublic.

Based on percentage of revenues derived from international markets, Publicis was the top company followed by WPP, Havas, Omnicom and Interpublic. European holding companies are less dependent on domestic markets than their US and Japanese counterparts. For the five-year period, Dentsu derived almost 90% of total revenues from Japan while Omnicom and Interpublic earned more than half their revenue from the US market.

As for overall financial performance, Omnicom enjoyed the highest revenue and second highest revenue growth rate. WPP had the second highest revenues and the third highest revenue growth while Publicis showed the highest revenue growth with relatively modest total revenues. Havas showed both the lowest total sales and revenue growth.

With regard to profitability, Omnicom was the best performer followed by WPP, Publicis, Dentsu, Interpublic and Havas. Where management effectiveness was concerned, Omnicom showed the best return-on-assets (ROA) and the second highest return-on-equity (ROE). On the other hand, Interpublic had the lowest ROA while Havas showed the lowest ROE. Thus, Omnicom demonstrated the most effective management with Interpublic and Havas the least effective.

Future research areas

Chong says the study offered several hypotheses that could be tested further in research. The current study reveals that the most internationally diversified companies achieve better profitability, sales and management effectiveness, whereas less internationally diversified ones do poorly on at least one of the three measures of company performance. There was also scope for looking at the relationship between some measures of company performance and international diversification, Chong adds.

He highlights another potential research hypothesis — that companies with less geographically related international operations enjoy a greater degree of diversification and, thus, higher profitability across regions compared to their counterparts with greater geographic concentration.

Comments Chong, companies “must take into account country-specific factors such as regulatory, economic, technological, cultural and social environments as well as the media infrastructure and demand for communication services”. More research into international diversification in the regions below will yield richer results and more specific results as compared to Asia as the only region where all six companies had M&A transactions from 2002 to 2006, Europe growing in prominence since 2007 onwards, and Asia (especially China and India) experiencing accelerating growth.

First published in Feb 4, 2008. Reproduced with permission from The Edge (www.theedge.com.my). Copyright 2007 Singapore Management University. All rights reserved.