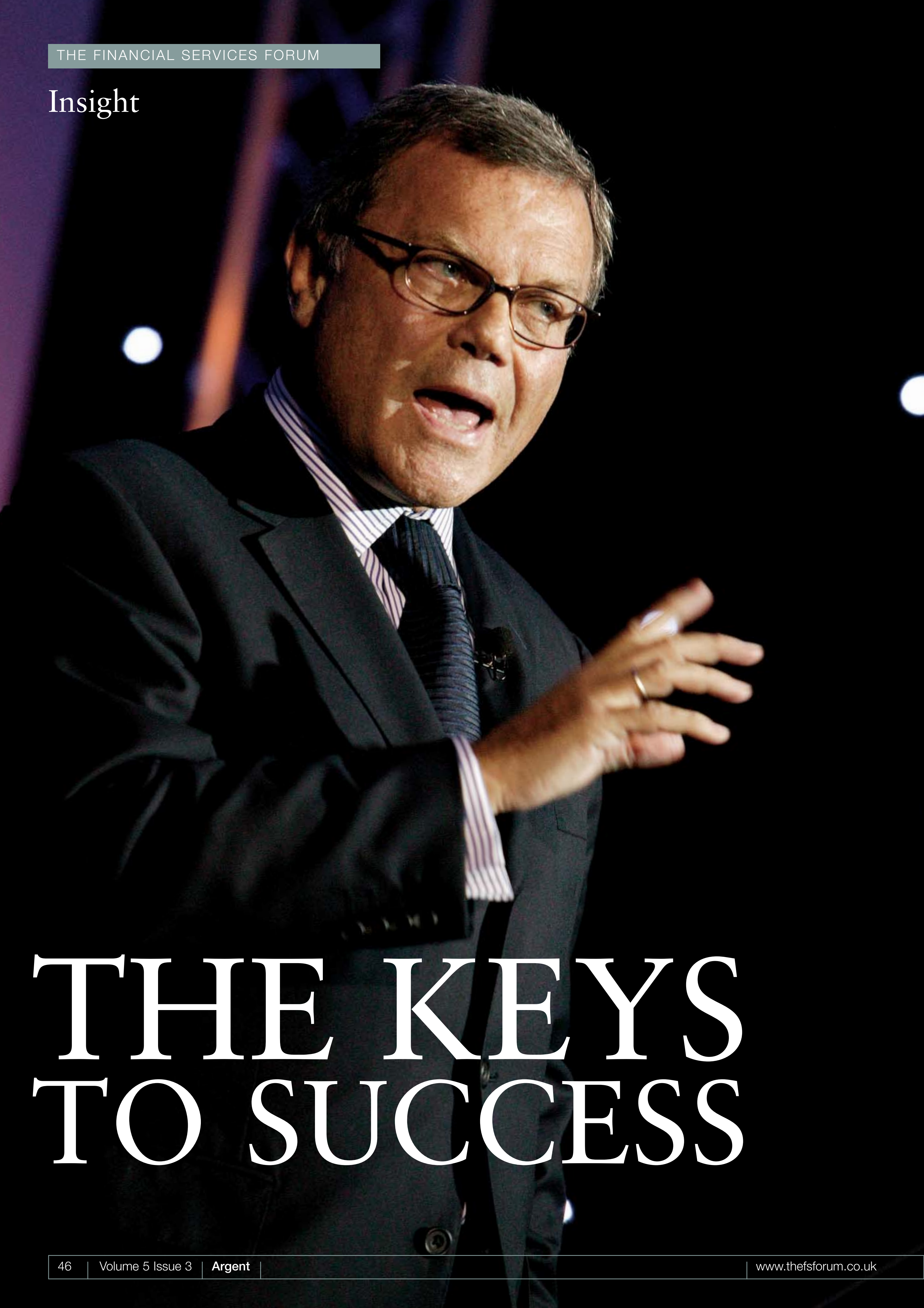

THE KEYS TO SUCCESS

Sir Martin Sorrell, chief executive of WPP, gave a thought provoking address to the members of The Financial Services Forum at their annual dinner which took place at the Royal Opera House on 19th September. He outlined the key challenges that face companies in the 21st century – and some possible solutions.

Some of you may not know that 21 years ago WPP didn't exist. We are now 95,000 people, if I include our associates, and 75,000 if I exclude them. We are in 106 countries, we have a market capitalisation income of $15 billion and revenues of $11 billion. Most importantly we buy about $50 billion of media around the world. One in four ads that you will see or read on the Internet would come from us. So we have about a 25% market share in most markets of the world.

There are three things that we are intent on doing over the next five to 10 years. They are equally important. The first is geographical. Today 40% of that $11 billion originates from the States, 40% is here in Europe and 20% is in Asia, Latin America, Africa, the Middle East and Central and Eastern Europe. Our objective in the longer term – in the next 5 to 10 years – is to have that equally distributed, a third in each major market.

Why? Two thirds of the world population will be in Asia by 2014 as opposed to the half as at the moment. So that's number one. The second stems from the fact that we are not actually an advertising agency anymore. If anybody wanted to offend me they would call us an advertising conglomerate.

I think we are a fairly focussed set of advertising and marketing services. We are half advertising – comprising brand advertising, creative advertising, media planning and media buying. The other half is in areas such as information insight and consultancy. This includes research, public relations and public affairs, in branding and identity, in healthcare communications, and last but not least, specialist communications – basically direct, interactive, Internet, which is becoming much more important.

In the longer run, that is five to ten years, we would like two thirds of our business to be outside advertising, because the cost of television advertising, despite what has been happening to traditional media over the last couple of years, continues to escalate at a rate faster than general price inflation.

Clients faced with inputs that inflate faster than general pricing inflation will do one of two things. They will either use less of it or they will find an alternative and that's what is happening in the context of network television. The travails that ITV are going through in the UK at the moment with forecasts that they will be down by 21% in the fourth quarter of this year are indicative of the frustration that many of our clients have with their increased costs.

As I mentioned earlier, the second objective is that marketing services should be two thirds of our business – first, because of the cost of network television and traditional media and secondly because of the fragmentation of the media and new technologies.

Our third objective is that measurable marketing services, that's market research and direct interactive Internet which is today one third of our $11 billion revenue, should be about half of our business. Why?

Clients faced with inputs that inflate faster than general pricing inflation will do one of two things. They will either use less of it or they will find an alternative.

Because we think that our clients, not just within financial services but also outside, will be using measurable media and will be using quantification justification of the decisions in a more and more effective way.

You will not make decisions unless you get quantifiable justification. Often that doesn't go down well in the creative departments particularly in advertising agencies. But it is a fact of life that we believe will become increasingly important. So if you said to me, 'what would WPP look like in five to ten years?' – it would be more Asian, more Latin American, more Middle Eastern, more African, more Central and Eastern European, more outside traditional advertising and media planning and buying, and finally more measurable – particularly in the areas of research, direct, interactive and Internet. As I talk about the five things that we think are very important to you and therefore to us I'd like you to think about those three objectives. ➤

If I were talking to you five or ten years ago I think I would have talked about the world becoming more and more Americanised – this was a speech which used to go down very well in Paris! The French would get very exercised about American cultural imperialism, McDonald's, Coca-Cola and the like. But I am not really talking about that, and neither am I talking about what Theodore Levitt said in that seminal article in the Harvard business review in 1983. I am not talking about consumers consuming things in the same way everywhere in the world.

What I am talking about is economic power – and economic power is shifting very dramatically, as many of you know and you will have seen in the operation of your businesses, from the west to the east. This is something that we find very uncomfortable to get our minds round.

In the longer term the critical differentiator between corporations will be in the way in which they find, the way they recruit, the way they incentivise, the way they motivate and the way they keep their talent.

It's a very long-term swing and therefore I don't want to be gloomy but I think it is irreversible. We are starting to see the full development of a cyclical swing which will take in Asia, Latin America maybe to a lesser degree because of the protectionism that we see there, Central and Eastern Europe and Africa and the Middle East. You may think that I am overstating the case but 2010 the World Cup in Africa will be a seminal event for the sub-continent of Africa. This shift to the east is something which I think we all have to get our minds around.

So what is one of the biggest issues that our clients face? It is over capacity. In most of the industries in which we operate, if not all, there is significant overcapacity. Our biggest client is Ford Motor Company and you see at the moment what is happening in Detroit – not just to Ford but to GM and Daimler Chrysler and that's emblematic of the over capacity that we see in many major industries.

Given that situation what is important? There are two things - innovation and branding. You can have innovation without branding but you can't have branding without innovation. The key to this is product service, both tangible and intangible, and that is where we come in – because our business is about branding, that differentiation, that innovation.

Whilst we have overcapacity, the paradox is that there are still shortages. In the 19th and 20th centuries the difficulty was to get products and services to the consumer. That's no longer the problem. You can produce it in surplus, you can service it in surplus. The shortage is in human capital.

If you look at every demographic statistic, the ageing of the population, lowering of birth rates, all the demographics are against you if you are trying to recruit good people, retain good people, incentivise and motivate them. Our view is that in the longer term the critical differentiator between corporations will be in the way in which they find, the way they recruit, the way they incentivise, the way they motivate and the way they keep their talent.

My next point is the web. In 2000/2001 when we had the compression in the web I think a lot of us breathed a sigh of relief. We thought the shift in new technology was over but now we are going through Internet 2.0 as we would call it – some call it Internet 3.0, and it is much more embedded than it ever was.

The three issues that we all have to think about, particularly in our business, are the following – first that we continue to be disintermediated by new technology companies, by new companies that don't have the legacy systems.

Is Google for example, in our case, friend or foe?, Probably the answer is, friend and foe. We are their third largest customer. We want to be their largest customer. But at the same time they are looking to put together online media planning and buying systems, they are looking at providing free research and they are looking at doing creative in terms of online capacity themselves.

You not only get disintermediated but you get disintermediated by a lower cost business model. These companies, Google, Yahoo, Amazon, eBay, MySpace, YouTube are evaluated by institutional investors and analysts in a totally different way – usually in terms of volume, in terms of revenue and not in terms of profitability or cash flow.

The final point relates to the talent issue. Young people – despite the problems they had in that crunch of the Internet in 2000/2001 when they lost the values of their options, when they lost their jobs – are attracted to these new companies.

They are attracted to the responsibilities they get in these fast moving, less bureaucratic companies than in the more established ones. The web is a big challenge to all of us.

The next point is about internal communications. WPP is a multi-branded company that grew by acquisition. I think that is probably the most difficult type of company to manage. A uni-branded company that grew organically, such as a McKinsey or Goldman Sachs is a much easier company to manage. It is interesting that those two companies, when they have made acquisitions have had problems.

When you are running a multi branded company – and you are trying to keep brand names separate and retain them because that's part of the reason for acquiring them in the first place – it's very much more difficult to manage. The silos that you have to deal with, the geographical silos and the functional silos are very difficult to coordinate.

What CEOs have to face is the dissonance and the lack of clarity, the geographical rivalries and functional rivalries that we see as being critical in the growth of companies. The critical issue for CEOs and indeed CMOs inside companies, is to get organisation alignment, to be able to articulate simply and effectively where we are trying to get to and how we are going to try and get there.

My final point is about distribution. The biggest issue in distribution is the increasing concentration of distribution. If I look at the two best examples of that would be Wal-Mart and Tesco. The statistics are shattering, Tesco's accounts for 31% of the grocery market here in the UK, Walmart is 30% of the US grocery market and it is 8% of the US retail market.

Tesco is 12% of retail sales here, Wal-Mart would rank on its own as the seventh largest nation in the world just on retail sales, and only marginally behind China. More people go to Wal-Mart in a week than go to church on a Sunday in the United States. It is actually the new religion.

This retail concentration has put immense pressure on manufacturers. One of the reasons you can argue why Proctor paid $57 billion dollars for Gillette was in part to deal with the retail concentration issue.

How do you deal with this? In fact how do you deal with all of the issues? The over capacity issue? The web issue? The internal communications issue? The distribution issue? I think it comes down to two things – innovation and branding.

The only way that you will win in the world where the east will be increasingly competitive and increasingly challenging, the only way you will win as technology challenges you, the only way you will win in an over-capacity world, is that you innovate very strongly and effectively and you brand very efficiently.

You have to develop new products with tangible and intangible benefits. There is nothing immoral in giving consumers emotional benefits as well as tangible benefits. But you have to brand those things very effectively, So we remain very bullish in our industry at WPP because of the importance of differentiation and effectiveness. □