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This piece is a lightly edited version of a speech given by Sir Martin Sorrell on the occasion of the IDM's Patrons' Lunch for 2007. It contains the reflections of one of Britain's premier business executives on what he sees as the important trends and challenges in business today.

Opinion Piece

The challenges facing today's business leaders

Sir Martin Sorrell

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Background

WPP companies provide clients with advertising; media investment management; information; insight and consultancy; public relations and public affairs; branding and identity; healthcare and specialist communications. Collectively, WPP employs 98,000 people in more than 2,000 offices in 106 countries.

WPP's major brands include advertising agencies JWT, Ogilvy & Mather Worldwide, Y&R, Grey Worldwide and The Voluntarily United Group of Creative Agencies; global media investment management companies MindShare, Mediaedge:cia and MediaCom; market research companies Millward Brown, Research International, KMR Group and proprietary diagnostic tools for managing brands, BrandAsset® Valuator and BRANDZ; the direct, customer relationship and interactive marketing networks OgilvyOne Worldwide, Wunderman, 141 Worldwide and Grey Direct; public relations and public affairs firms Hill & Knowlton, Ogilvy Public Relations Worldwide, Burson-Marsteller, Cohn & Wolfe and GCI; global healthcare companies CommonHealth, Sudler & Hennessey, Ogilvy Healthworld and Grey Healthcare Group; and global branding and identity firms Landor, Enterprise IG, Fitch and G2 Worldwide. WPP's specialist communications group includes firms that provide sales promotions, web communications and hi-tech marketing.

Clients include more than 330 of the Fortune Global 500, over half of the NASDAQ 100 and over 30 of the Fortune e-50.

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Preamble

I thought I would start by explaining about how we at WPP see the industry and by giving you some key statistics.

WPP company overview

Billings

WPP has \$50bn of billings. That amounts to 20–25 per cent of total media billings around the world. In the UK, through one buying point, Group M, we are responsible for 25 per cent of television and a third of print. We have 15 per cent in China and 50 per cent in India. In Italy we have 45 per cent, in Germany 40 per cent and in Spain 27 per cent.

Market capitalisation and revenue

WPP

WPP has about \$11bn of revenue and a market capitalisation of about \$18bn, making us slightly bigger than Omnicom currently. Adding together WPP's and Omnicom's market capitalisations of \$18bn each, Publicis's \$8bn and IPG's \$6–7bn, you reach about \$50bn. Adding together the revenues of all four, the total is about \$33bn. Google has the same revenues as WPP and Omnicom, and is growing much faster; its margins are also much bigger, at about 40 per cent. Its market capitalisation, however, is \$150bn — three times bigger than the top four agencies put together.

WPP is a medium-size company. We are ranked, in terms of value, at about 550 in the world, having started 21 years back with two people in a room. We now have about 97,000 people, or 75,000–77,000 excluding associates, that is companies of which we own 20–50 per cent. We operate in 106 countries.

Clients

Our top five clients are Ford, Unilever, Procter & Gamble, IBM and Pfizer. We have 300 clients in Fortune 500, representing about half of our business. We also have clients who are the multinationals of the future: local and regional companies growing at great speed.

WPP's objectives

Geographical

Objectives

From 40:40:20...

Our first objective is geographic. Today, 40 per cent of our work is in US and 40 per cent in Europe, including eastern and western Europe, which are growing at two totally different rates. The remaining 20 per cent is in by far the most important and interesting parts of the world: Asia-Pacific, Latin America, Africa & Middle East.

...to 33:33:33

In the next 5–10 years, our objective is to be one-third, one-third, one-third because, by 2014 two-thirds of the world's population will be in Asia-Pacific alone; today, it is about half.

Incidentally, people talk about there being 1.3 billion people in China, which is four times as many as in the US. There are, actually,

about 1.5 billion people. I sat next to the former Communist Party Secretary in Beijing a few weeks ago and, through his interpreter, we had a fascinating dinner. He kept saying '1.3–1.5 billion people in China'. The third time he said it, I could not resist asking him why he used the phrase '1.3–1.5 billion', when everyone thinks that there are only 1.3 billion. In response, he said: 'We honestly do not know. We think there are, actually, 1.5 billion people in China'.

If there are 1.5 billion people, that is 200 million more than we knew of — it amounts to two-thirds the size of the US, 3.5 times the size of the UK or equal to the size of Indonesia. India has another 1.1–1.2 billion, where birth rates are higher. Over time, perhaps, the birth rate may rise in China, too, but a colossal population shift is taking place.

Market channels: Information, insight and consultancy

From 50 per cent...

Information, insight and consultancy

If people really want to upset me, they should call WPP an 'advertising conglomerate'. In fact, it is no longer an advertising agency as a whole, since 54 per cent of our revenues come from outside traditional advertising, in areas such as media investment management and media planning and buying. This 54 per cent comes from what we call 'information, insight and consultancy', which is a posh phrase for market research, public relations and public affairs, branding and identity, healthcare, and what we call 'specialist communications', which embraces direct, interactive and internet agencies. Some \$2bn of our revenues are indirect, from brands like OgilvyOne, Wunderman, RMG Connect, G2 and others.

... to two-thirds

Instead of being half our business, I want this to be two-thirds of our business in the next 5–10 years for two reasons. First, the fragmentation of media and the growth of new technologies; secondly, the cost of television advertising continues to escalate at a rate faster than the general price inflation.

Inflation

The fact is that people pay \$2.6m for a 30-s Super Bowl ad and continue to be willing to do so. Before he left Viacom, I was telling Mel Karmazin that our clients were worried that they had to pay \$2.5m for 30s. He said: 'In five years' time, it will be \$5m.' That tells you something about how network owners feel about clients and cost escalation.

I think it is likely to continue. There is a pool of money looking for the reach of events like the Baftas, the Academy Awards, the World Cup or the Olympics. That has the habit of driving prices up faster than inflation. If you are a manufacturer and the cost of an input escalates faster than the general price inflation, either you use less of it or you find an alternative, which is what is happening to television in the long

run. That is why I would like to see two-thirds of our business outside traditional advertising.

Measurability

From a third...

About a third of our business is in the direct area and in market research. Kantar is the parent company for Millward Brown, Research International and AGB Nielsen. We measure television audiences in virtually every country outside the US through our joint company with VNU, now called the Nielsen company, with IBOPE in Latin America and others. Those two businesses together account for about \$4bn out of \$11bn.

... to a half

I want this proportion to increase to about a half, because I think measurability is going to become more important. Clients do not want to make decisions without statistical justifications. Of course, creative directors in advertising agencies hate the fact that their ads have to make Millward Brown '8' scores. They loathe the idea that you can reduce creativity to a number. I probably agree with them, in my heart of hearts, but it is unrealistic to believe clients are going to make decisions about media budgets unless they have a statistical justification for doing so. Our third objective, therefore, is to have half of our business coming from quantitative, measurable areas. Direct, interactive and internet fits right into that space.

Summary

In 5–10 years, in terms of what WPP is going to look like:

- It will be more Asian, Latin American, African and Middle Eastern, and central and eastern European.
- It will have more non-traditional advertising, particularly in areas such as direct, interactive and internet, given the technological change.
- It will be more measurable, adding to market research.

Key concepts

Geography

Major shift in economic power to the East

There are six things we think are currently important in the world. The first relates to geography. It is difficult, standing in London, New York or Paris, to get this point across and there is an inbuilt resistance to accepting it. But there has been a power shift in the past 5–10 years that we in the West still have not woken up to.

**Measurability to
become important**

Six important things

Achieving premium positions in 'developing/emerging' markets

I mentioned the population statistics, but we see companies like Vodafone, in the context of its acquisition of a controlling stake in Hutchison Essar, driving to achieve a premium position in what people call 'developing' or 'emerging' markets. This is condescending: these are the faster growing markets. The Indian government said recently that its economy was predicted to grow by 9–9.5 per cent. The ex-Communist Party Secretary told me that China consistently underestimates the growth of gross national product (GNP) in China. If they say it is growing by 9–10 per cent, it is probably growing at 10–12 per cent.

True globalisation, not Americanisation

The shift that is taking place is considerable — the first time that we have seen true globalisation rather than Americanisation. And this is globalisation in the sense of a power shift, rather than as imagined in Theodore Levitt's vision, who once predicted that we would all buy the same things regardless of where we were in the world.

Rise of Chinese companies

We are seeing the rise of companies, not just from the US, the UK, France, Germany, Italy, Spain or Japan, or *chaebol* like LG, Samsung, Hyundai or SK in South Korea, but the rise of corporations in China such as Sinopec, TCL, Lenovo, Konka, Bright Dairy or Mongolian Cow. Mongolian Cow is the company that bought the National Basketball Association (NBA) and sponsors the television talent show Supergirl in China.

Rise of Indian companies

In India, who would have thought that Tata would buy British Steel? It may have been renamed Corus when it got together with the Dutch company Hoogovens, but it is basically still British Steel. In addition, there are the Reliance companies, run by Mukesh and Anil Ambani, Wipro, and Infosys. Infosys is a software company that will grow from 60,000 to 120,000 people in two years. This Bangalore-based company receives 1.4–1.5 million applications for jobs every year.

Back to the future

If anyone thinks that such change is new, think again: this is *Back to the Future* stuff. If you return to 1825, it was the same process, but in reverse: the rise of Meissen and Wedgwood, and of high-quality china at low prices, completely destroyed the porcelain industry in China in the way we are seeing now in reverse. If you plot Indian and Chinese GNP over 200 years, it is a perfect U-curve, starting at 14 per cent 200 years ago and returning to 14 per cent, according to Goldman Sachs, in 2025.

Rise of Chinese and Indian companies

**Differentiating factor
is behaviour of people
within companies,
internally and
externally**

Overcapacity

Greater reliance on agencies for differentiation

In all the industries we operate in with our clients, we see significant overcapacity, with one or two exceptions. Our largest client, Ford, is in an industry that can produce 80 million units, although consumers consume only 60 million. In that environment, we become more important; clients are reliant on agencies for differentiation in a world of overcapacity. Tangible and intangible differentiation becomes critically more important, particularly given the pressure of new technology.

Shortage of human capital

At the same time as overcapacity grows, there is a shortage of human capital. In the 21st century, the biggest issue is going to be the supply of people. In the 19th and 20th centuries, it was about getting goods to the consumer, but that is over. The problem now is how we locate, identify, recruit, motivate, incentivise and keep good people, because all the demographics are against us, even in the faster growing markets. Mexico, Brazil, India and China all have problems of ageing populations and declining birth rates, making the supply of people much more difficult. We believe, then, that the differentiating factor between companies over the coming years is how people behave within companies, both internally and externally.

Internet

Disintermediation by lower cost business models

There is still disintermediation by lower cost internet business models and they still steal your people. In Internet 1.0, we lost a fair number of people to the new internet start-ups. After they collapsed in 2000–2002, a number of people who left us came back. I remember conducting ‘re-entry’ interviews, rubbing my hands with glee at the thought that these people would be grovelling for their jobs again. But far from it: every one of them said that, if they had the opportunity again to go to smaller, less bureaucratic, more flexible and responsive companies they would take it. We see the same in Internet 2.0.

Profitability of traditional companies permanently impaired by new technology

The internet and the role of technology companies is far more embedded now than it was even in 1999–2000, which is a crucial issue we have to face. It is difficult for us in the agencies, for our clients and for media owners to get our minds around the fact that the profitability of traditional companies has probably been permanently impaired by new technology.

Consumer power has become considerable

The ability of consumers to receive knowledge and information virtually for free enables consumers to exert a power they never

previously had. We see this with user-generated content, which happened with Dove and its 30-s, \$2.6m spot on the Super Bowl. The power of the consumer has become considerable and companies have to understand that the future will be less profitable than the past. That is certainly the case in network television, national newspapers and magazines.

What do I want as a consumer of business information? I want the story now and I want it analysed now. I am more aggressively looking at *breakingviews* on my BlackBerry and am not prepared to sit and wait for a week or two for *Fortune*, *Business Week* or *The Economist* to give me their analysis, no matter how brilliant it is.

Far more competition; relatively low inflation; limited pricing power

We were talking about the insurance industry and somebody said the company they worked for had invested a lot in the internet, but were facing a lot of competition from switch sites. I do not think this is much different from what we encountered with sales promotions 10 or 20 years ago, but this is the reality of life. It is going to be far more competitive and, in a world of overcapacity where there is relatively low inflation and limited pricing power, this is going to become more of an issue.

Internal communications

Explaining strategic and structural changes in direction

If you link some of these things, the critical issue for most chairmen and chief executives we deal with is how they explain, internally, the strategic and structural changes in the direction they are taking. This is a matter of getting everyone to work together and to face in the same direction, at the same point in time. For WPP, I have to confess it is a nightmare: it is the worst possible model. It is a company that is growing by acquisition and one that is multi-branded. Companies that grow organically, such as McKinsey or Goldman Sachs, tend to have greater difficulty when they do make acquisitions than when they grow organically.

Organic growth is stronger than growth by acquisition

You may find this extraordinary coming from me, but organic growth is the strongest way to grow: it is the way that you build the strongest cultures. Acquisitions are a weaker way of growing, but if you want to build a big international services company in your lifetime, this is the way you have to do it. If I was writing a *Harvard Business Review* article, I would say the easiest model is the uni-branded company, organically grown; the most difficult is the multi-branded model that has grown by acquisition.

Facing the same direction, at the same point in time

Whatever the model is, explaining strategic and structural change internally is vital: if I could get the 100,000 people in WPP to face the

How to explain strategic and structural changes

same direction at the same point in time, it would be a powerful and unstoppable army. I am sure everyone in this room works seamlessly with one another, with no divisions, responding instantly to one another and helping one another effortlessly. Outside this room, however, that is not the situation.

Coordination problem

Inability of people to work together

The biggest problem our clients face — and that we face internally within WPP — is the inability of people to work together. You have a coordination problem when you have two people in an organisation; when you have 97,000, you can imagine what a nightmare it is, particularly given the structure. This is the critical issue. I often look at WPP and our clients and say: ‘If we spent 15–20 per cent of the time that we spend on internal bickering thinking about clients, or about the issues that we have to deal with, we would be much more effective.’ If you asked me to identify the most important of these concepts, it would be this one.

Distribution

Shares of revenue

Tesco represents 12 per cent of retail sales and 30 per cent of grocery sales. Wal-Mart represents 8 per cent of US retail sales and 30 per cent of grocery sales. Procter & Gamble achieves 16–17 per cent of its sales, and 30 per cent of its US sales, through Wal-Mart. Our biggest client represents about 5 per cent of our revenues; if the figure was 20–30 per cent, I would feel distinctly uncomfortable.

Portfolio games

Tesco and Wal-Mart are both expanding internationally. One half of Tesco’s footage is now outside the UK, but I doubt whether the same is true for one half of its profits. As it grows internationally, it will be a much different game to play than when you have a homogeneous, domestic market in which you are dominant; you have to play much more of a portfolio game.

Increased retail power

More people go to Wal-Mart in a week than they go to church on a Sunday in the US: it is the new religion. How does a manufacturer deal with that increased power at the retail level? It is simply down to innovation and branding. The balance of power between retailer and producer has shifted, particularly when retailers are developing private label products at varying price points. It used to be that private label was the cheapest, but this is no longer the case.

Corporate social responsibility (CSR)

At the front and centre of the agenda

If I was talking here 6–9 months ago, I probably would not have included this on the agenda. A recent *FT* article by Carlos Grande

CSR

Environmental and social issues are at the top of the agenda

quotes three of our agencies and two others on the importance of CSR. Three things have happened recently, which have put this at the front and centre of the agenda: First, Warren Buffett's deal with Bill Gates on transferring Microsoft stock into Berkshire Hathaway — a nifty way for Bill Gates to diversify his portfolio, as well as to invest more aggressively in big-scale, corporate philanthropy projects.

Secondly, Sir Richard Branson's brilliant PR coup a few months ago at the Global Clinton Initiative in New York — he did not say he was going to invest \$3bn of profit, but that, if he made the \$3bn, he would invest it in altruistic, charitable projects.

Thirdly, James Murdoch's initiative at BSkyB, which his father then picked up in the context of News Corporation, on the back of Al Gore and his film 'An Inconvenient Truth' on carbon neutrality.

Long-term business sense

Those three things have pushed environmental and social issues to the forefront in a way not seen before, and they are at the top of everyone's agenda now. I am somewhat incredulous about this. If you are interested in the short term, you will rape the environment, pillage society and make the quickest buck that you can. But if you are interested in building long-term brands, you will not do that. We know that younger, middle-aged and older people are concerned about these issues. We know that environmental, social and political issues are critically important: consumers will buy products if they think they are environmentally friendly and will not buy them if they think they are doing bad things. Being a good corporate citizen, then, has nothing to do with charity and altruism, but is about long-term business sense.

WPP's conversion to CSR

The reason why I was converted to this was simple and I remember it clearly. It was the HSBC pitch about four years ago. The request for a proposal was put out and the third question was: 'What is your corporate philanthropy policy?'

We were the only parent company to have a document that we produced and gave to HSBC, which is somewhat of an indictment of the industry. We are going through our fourth iteration of the CR Report, which I am proud of.

Training matters

In terms of training, we started a WPP Fellowship programme ten years ago, with a special three-year programme for graduates. We are still the only company in our industry to do this. My biggest fear, when we started the programme, was that we would be copied. Omnicom comes about halfway to doing this, but nobody else. What does that tell you about our industry? It tells you that they cannot be bothered, believing instead that if you need somebody, you steal them — you do not train them. The IDM's Trainer of the Year award is, therefore, critically important.

What distinguishes McKinsey and Goldman Sachs is that, every year, they go to universities and recruit people intensively. It does not matter where we are in the economic cycle, they just keep on doing it. It is a big indictment of our industry that we do not do that, so I applaud any efforts in that area.

We do not do enough at WPP; we should do more. The proof of the pudding is that, if we asked Ogilvy whether WPP fulfils any useful function, they would say that the only one is training — everything else is nonsense. We do ourselves a disservice, particularly in this digital era, when finding people is even more difficult.

Conclusion

Important issues

Key issues

- The shift from Americanisation to globalisation.
- The shift in power to the East.
- Overcapacity and the shortage of human capital.
- The internet.
- Internal communications and getting everyone aligned internally.
- Wrestling with the distribution issue.
- CSR.

In terms of what you do about it, the issue is innovation and branding. I am interested in branding, for obvious reasons, because our business is about how we get clients to differentiate their products and services, either tangibly or intangibly. There is nothing unethical about trying to create a difference on psychological, social or emotional grounds. In the UK, people used to object to the idea that you would encourage consumers to buy things or have marketing platforms on an emotional or intangible basis, but this has become critically important, as you all know.

Innovation

Branding is important, but at the heart of it is innovation. If you look at the big changes that have taken place in the past couple of years, Apple is probably the most interesting, with the iPhone. It is probably difficult for most consumers to get their minds around the difference in technology and approach. It is groundbreaking stuff, as was the iPod. WPP invested in Big Ideas Group (BIG), which has 10,000 online inventors. It was started by a Harvard Business School graduate in Boston who gets briefs from clients on new products, new product introductions and ideas, and posts the briefs via the internet to his 10,000 inventors. In the event that the inventors come up with a successful programme or idea, there is a fee and royalty system. This is an interesting and important example of how we are using technology.

In answering questions from the floor, Sir Martin made the following points:

On whether the growth model adopted by WPP has been to the benefit of its clients as well as to WPP

It has been to the benefit of our clients. Clients are interested in solutions. Ogilvy's first campaign for IBM was 'solutions for a small

planet', a line I always thought appropriate to our business. Clients want solutions. I will probably offend colleagues and people in competitive organisations by saying that clients are not interested in our agency brands. They are interested in getting the best group of people to work on their opportunities, challenges and problems.

If I look at WPP, it is a matter of how we can pull together the best set of people to deal with a specific brief. It is not about whether they reside in JWT, Y&R, Ogilvy, Grey or Millward Brown. That is what I would say if I were a client. What Omnicom, IPG, Publicis and we have done is to re-create the full service agency model that used to exist. In the 1960s if you visited, for example, JWT in Berkeley Square, London, you would find a creative department, a marketing department, an account-handling department, a media department, a public relations department. There would be a merchandising department, a direct mail department, a packaging department, a production department, an experimental film department, a market research department, a conference department. Even a home economics department with two fully equipped kitchens — plus an operations research department designing a factory for Mr Kipling's cakes. Long before the phrase 'integrated communications' came into common use, integrated communications were exactly what such full-service agencies provided.

Organic growth takes time

What has happened is that everything has become much more specialised, the biggest example being media planning and buying, and clients have a better functional offer as a result. The issue is how you unite it again in an integrated way. Organic growth takes time; acquisitions are quicker, but there are different objectives.

If you are running a listed company, there is an inbuilt advantage, because of accounting conventions, to acquiring in goodwill, rather than investing and building cost on to the profit and loss account.

In terms of the internet, Publicis paid three to four times revenue for Digitas; General Atlantic bought a majority stake in AKQA, again probably three to four times the revenue. This is nosebleed territory. The clear answer is to build from scratch: it is a much better way in economic terms and one that delivers much better quality. Given the size we are now, our organic growth plays a much bigger role than it used to.

On which brands have best been able to embrace the shift and effectively harness Internet 2.0

Resistance to change

Business-to-business (B2B) brands have been more successful, which is understandable. I am 62, an age when I do not like change. Let us take the average chief executive in a client, agency or media owner. They have spent 20 to 25 years of their life picking and clawing their way to the top. They get to be chief executive for 4–5 years. The last thing they want is change: they want to come into the office and for everything to carry on as it is. They want to travel around the world and enjoy themselves — they do not want trouble. So there is an inbuilt resistance to change.

What is happening to some extent is that people are shifting money because they are worried. If they shift £10m out of television or national press, they do not put it to work elsewhere: they keep a bit back. People are so worried when they look at circulation statistics — as they should be, frankly. When a Craigslist is providing classified advertising at a local or regional level for nothing, the competitive response is to provide it for nothing. It is the cannibal argument: 'If I do not eat my children, someone else will.'

People underestimate how tough it is. I studied economics, and supply and demand models had two very interesting conditions: one was free trade, without barriers; the other was free flow of information. We have both at the moment. I pray that it lasts on the first; on the second, technology has meant that the barriers to knowledge and the tyranny of geography have been all but broken.

Politicisation

On the politicisation of the advertising industry

Politicisation can mean many things. I think we have to be proactive if there are issues around advertising to children, for example. These are just variations of the events around alcohol and tobacco that we have seen over the years. In the direct industry, we have always had issues about privacy. It is one of the biggest issues that Google faces. Last week, in India, it blacked out sensitive military sites and the homes of important political people on its mapping. There have always been these issues; how we deal with them is important. We have to anticipate these changes, rather than being driven into them.

The power of what we have technologically far outweighs that. David Ogilvy founded Ogilvy in 1948 as a direct agency, as well as an advertising agency. Just like the media people, the direct people had the last five minutes of the presentation, the offices at the back of the building and the second-hand cars and may have been included in the bonuses as 'also-rans'. Life has changed.

The interesting thing will be the extent to which the industry becomes integrated with the traditional advertising industry to deliver the best solutions to clients. The traditional advertising business is under pressure, particularly in western markets. The growth in western markets is in direct, interactive and internet advertising. Profitability is under pressure in the traditional business. In Murdoch's results last week, the pressure is on network television — Fox, \$70m down — and national press. The growth is in the internet — MySpace, the Google deal etc. The interesting factor will be how those organisations coalesce within the big holding companies.

In my experience, direct businesses are bolstering the traditional advertising businesses, particularly in the US and in western markets, and how that resolves itself will be interesting. Direct is subsidising traditional advertising, which is wrong in my view. When an industry is under pressure, you have to take out cost — rather than keeping the

cost there, putting it with a growth part of the business and saying everything is fantastic. You look at them as two separate businesses, take cost out of the slow-growing business and invest it in the growth business. There are really interesting changes taking place in the industry, which will make life uncomfortable for people in the traditional businesses.

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