2005 Agency Business Report: Right in the middle

Craig McGuire - 18 Apr 2005 00:00

Midsize firms are displaying strength ahead of the industry curve.

Sometimes, being stuck in the middle may not be so bad. This is the case if you are one of the many midsize agencies enjoying increasing interest from clients that are eschewing the services of a global PR powerhouse in favor of such benefits as simply being able to direct dial into your AOR's top dogs.

According to *PRWeek*'s 2005 Agency Rankings, agencies with annual revenues between $5 million and $65 million reported an average growth of 19.4% in 2004, as compared to the 13% growth overall across all submissions. Of course, this does not take into account the financial performance of the majority of large agencies that are owned by holding companies. "The problem is that midsize agencies cannot accurately compare our growth to the larger firms, which currently are almost all subsidiaries of diversified organizations and are not publicly reporting revenues because of Sarbanes-Oxley," points out Ken Makovsky, president of Makovsky & Co. which reported a 16% increase on 2004 revenues of $5.9 million.

An argument can be made that a gain of just a few percentage points for a major PR agency like a large firm can surpass the total annual revenues of others, but the story within the story that the numbers do not show comes when you examine agencies leading the charge.

Like any other sector in the professional services industry, PR lives and dies on the back of the US economy. To get an idea of just how far the midsize segment has rebounded, consider that during the economic downturn of recent memory, nowhere was the pain felt greater than in the technology sector, and many midsize firms had much of their resources devoted to that area. This free fall siphoned off millions of dollars in fees, suffocating agencies.

"There's no question, between consolidation and the dot-com meltdown, we've seen the number of midsize agencies focused on the tech sector greatly reduced," says Lou Hoffman, president of The Hoffman Agency. "But we're back in a cycle where new agencies are being launched and inevitably, a percentage of these will have success and grow into midsize firms."

In a year when the tech sector was sluggish (Hoffman slid 2% to $5.2 million in revenue for 2004), the agency managed impressive wins like Amazon.com's technology platform business.

Not surprisingly, some industry insiders are still holding their breath waiting for the growth to maintain consistency.

"For [the $5 million to $20 million agencies], I think 2005 is a mixed bag," says Elliot Sloane, president of Sloane & Co., which had a13% gain to $7.3 million. "Contrary to what you may read in the papers, the economy is still in a slow recovery and there is a lot of competition for new business out there. I think those midsize firms - like ours in the financial space - who are focused on a specific type of service are doing better than generalist firms, who offer everything to everyone."

Appealing times

Despite the prevailing conservative winds permeating PR these days, you would be hard pressed to find anyone in the segment, or in the overall industry for that matter, that says the gains of 2004 will be given back this year.

That's because attributes that make midsize firms so appealing are attractive in a conservative economic climate.

"We have a cost [overhead] structure that does not prevent us from working with the smaller companies at smaller budget levels," says Bob Angus, president of A&R Partners, which had a 26% increase in 2004 to $12.5 million. "At the same time we have a strong mix of staff and resources that enable us to address the broad needs of our clients resulting in more comprehensive programs and ultimately better results."

Simply put, midsize is just the right size these days because it can mold to the client's needs, says David Close, EVP at Schwartz Communications, which grew 12% to $18.1 million.

"A midsize agency can have deep resources and financial stability, but still provide highly flexible and customized services to clients," Close says. "And of course, we're better able to work within a client's budget."

To Marina Maher, CEO of Marina Maher Communications, considering how competitive the scene is today and how demanding clients have become, the midsize space is an ideal place to be.

"There's plenty of space for growth without having to change the agency's DNA," Maher says. "Midsize offers great advantages - enough resources to compete with big firms; greater resources and business strategy than smaller firms; and no red tape or committees regarding investments in people and the agency. We can define our ideal clients and pursue new business as we see best. We are not enslaved by profit-margin targets and we keep our eye on the numbers, but we don't measure by the month."

Nimbleness and low overhead are great advantages, but from the client's perspective, nothing beats attention from founders and senior management.

"Midsize agencies with the founder still serving as a principal are driven by a vision that assures a high standard of customer service throughout the firm," Makovsky says. "Also, it appears that founder-headed firms are less likely to be subject to the ethical problems facing the big firms ... when your name's on the door, the unassailable integrity of your firm is of paramount concern."

Meanwhile, luring top talent from the big boys is not as difficult as it once was.

"Midsize agencies that are owned independently have more flexibility in the areas of compensation to keep good people, and investment spending to address specific needs," says Jerry Epstein, CEO of Zeno Group, which recorded 31% growth to $16.5 million.

"As a result, staffing is more stable, experienced counselors spend more time on client business, and clients benefit," Epstein adds. "And clients are increasingly following the talent, and more willing to take a chance with a midsize agency that has attracted top performers with great reputations."

Still, some midsize firms believe bigger is better - bigger clients, that is.

"We believe that a roster of fewer, larger clients managed by the most senior agency leaders and supported by dedicated teams allows us to develop and execute the most successful programs," says Michael Sullivan, president of IPG's DeVries Public Relations.

For instance, Sullivan says such attention has enabled his shop to maintain a 22-year collaboration with corporate powerhouse Procter & Gamble.

Market familiarity

One limitation for many midsize agencies is global business. Many don't have the staff and resources to accommodate international clients. On the other hand, with no global agenda, they have a firm grasp on the local scene.

Raleigh, NC-based Capstrat grew its revenue stream by 15% to $6.3 million last year, focusing exclusively on the Southeastern US.

"Familiarity with the market is a big advantage and we know this region," Capstrat CEO Ken Eudy says. "The head of a major agency recently told me, 'We can always parachute in on a PR problem, but with public affairs, we don't necessarily know the players or the politics.'"

Concentrating on a specific vertical is a strategy for carving out a secure niche in the midsize space. And few did it better last year than Dorland Public Relations, which reported a 70% increase to $10.6 million in revenue with its penetration in the healthcare vertical.

"We are seeing resurgence in clients' appreciation of the value of a midsize firm," says Dorland president Nancy Bacher Long. "Clients look for top-tier talent dedicated to their business. They look for focus on their business - not on the holding company or Wall Street."

Many major companies are extricating themselves from major agencies to sign with midsize shops.

"The clients who hired us after an experience with a large-agency tended to have two or three common complaints," says Sean Cassidy, president of Dan Klores Communications, which recorded revenues of $17.4 million for 2004. "One is that the large agencies were great when it came to developing comprehensive communications plans, but tended to fall short on the execution of the programmatic elements, in particular, media," Cassidy explains. "A second big concern was that they felt lost in the bureaucracy of the agency or, in a couple of cases, felt the agency was constantly trying to sell in additional media services offered by an assortment of affiliated companies."

Large agencies will always have compelling advantages over their smaller counterparts, such as global networks, considerable resources, and manpower.

"Most midsize agencies don't have the marketing advantage of saying they have a global network of people and offices, which closes them out of opportunities with some of the world's largest companies," says Rick French, president & CEO of French/West/Vaughan, which had 10% growth to $8.7 million. "Although, we see that trend shifting as many marketers themselves realize that seldom do they really need that level of agency support."

Midsize firms predict more large US and global companies that previously may have opted for a multinational agency will tap them for work. Many expect the space will continue to grow at between 7% and 15% annually before the next round of consolidations.

"We believe there will be a divergence among small firm owners along two separate paths," Epstein says. "Those that position their agencies to be acquired, and those that position their agencies to serve clients. In the former case the emphasis will be on delivering maximum EBIT, and in the later the emphasis will be on creating a culture in which benefits to both employees and clients are paramount."

M&A activity in PR has been minimal in recent years, but it's possible it will pick up. What the rankings tables will look like in the future is anyone's guess, but there will always be a strong cadre of midsize agencies at its backbone.

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