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THE HARDER HARD SELL

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More people are rejecting traditional sales messages, presenting the ad industry with big challenges

IT MAY have been Lord Leverhulme, the British soap pioneer, Frank Woolworth, America's first discount-retailer, or John Wanamaker, the father of the department store; all are said to have complained that they knew half of their advertising budget was wasted, but didn't know which half. As advertising starts to climb out of its recent slump, the answer to their problem is easier to find as the real effects of advertising become more measurable. But that is exposing another, potentially more horrible truth, for the $1 trillion advertising and marketing industry: in some cases, it can be a lot more than half of the client's budget that is going down the drain.

The advertising industry is passing through one of the most disorienting periods in its history. This is due to a combination of long-term changes, such as the growing diversity of media, and the arrival of new technologies, notably the internet. Consumers have become better informed than ever before, with the result that some of the traditional methods of advertising and marketing simply no longer work.

Ad spending grew rapidly in the late 1990s, but in 2000--just as the technology bubble was about to burst--it soared by more than 8% in America, which represents about half the world market. The following year it plunged by 8%. Spending is up again, according to ZenithOptimedia, which has long tracked the industry. It forecasts that worldwide expenditure in 2004 on major media (newspapers, magazines, television, radio, cinema, outdoor and the internet) will grow by 4.7% to $343 billion. It will be helped by a collection of big events, including the European football championship, the Olympic Games and an election in America. Historically, when there is an upturn in advertising expenditure, it tends to rise faster than the wider economy. So, provided economic growth can be sustained, ad spending may continue to pick up.

How will the money be spent? There are plenty of alternatives to straightforward advertising, including a myriad of marketing and communications services, some of which are called "below-the-line" advertising. They range from public relations to direct mail, consumer promotions (such as coupons), in-store displays, business-to-business promotions (like paying a retailer for shelf-space), telemarketing, exhibitions, sponsoring events, product placements and more.

These have become such an inseparable part of the industry that big agencies now provide most of them. Although some are less than glamorous, marketing services have grown more quickly than advertising. Add in the cost of market research, and this part of the industry was worth some $750 billion worldwide last year, estimates WPP, one of the world's biggest advertising and marketing groups.

As ever, the debate in the industry centres on the best way to achieve results. Is it more cost-effective, for instance, to employ a PR agency to invite a journalist out to lunch and persuade him to write about a product than to pay for a display ad in that journalist's newspaper? Should you launch a new car with glossy magazine ads, or--as some carmakers now do--simply park demonstration models in shopping malls and motorway service stations? And is it better to buy a series of ads on a specialist cable-TV channel or splurge $2.2m on a single 30-second commercial during this year's Super Bowl?

Such decisions are ever harder to make. Although a Super Bowl ad is still cheaper than in 2000, in general network-TV pricing has risen faster than inflation--even though fewer people tune in. Changes in TV-viewing habits, however, are only part of a much wider shift in the way media is consumed, not least because it has become more fragmented and diverse.

For a start, people are spending less time reading newspapers and magazines, but are going to the cinema more, listening to more radio and turning in ever-increasing numbers to a new medium, the internet (see chart 1).

After the technology bust it was easy to dismiss the internet. But the phenomenal success of many e-commerce firms, such as Amazon and eBay, shows that millions of people are becoming comfortable buying goods and services online. Many more are using the internet to research products, services and prices for purchases made offline. Some 70% of new-car buyers in America, for instance, use websites to determine which vehicle to buy--and often to obtain competing quotes from dealers.

GOOGLE THAT

Such consumers can be targeted by internet advertisers and, in some cases, their responses accurately measured. A surge in online advertising is being led by paid-for text-links dished up by search engines such as Google and Yahoo! The response rate from people clicking on paid links can be as low as 1%--about the same as direct mail, which remains one of the biggest forms of advertising. But there is an important difference: internet advertisers usually pay only if someone clicks on their link. This is the equivalent of paying for the delivery of junk mail only to households that read it.

How are companies and the advertising industry responding to these trends in media consumption? Some people do not believe they amount to a sea-change, while others are simply hoping it will not come to pass on their watch, reckons Sir Martin Sorrell, WPP's chief executive.

Nor is it the only significant force he sees at work. New markets, such as China, are becoming increasingly important for advertisers, especially multinationals. But these markets can have very different characteristics. Clients are also more concerned than ever about getting value for money. What will increasingly matter, says Sir Martin, is not what it costs to put an ad in front of 1,000 people (a traditional industry measure), but "how effective is that cost-per-thousand?"

At the same time, negotiating advertising deals is becoming tougher because of consolidation, both among clients and among media owners. This could favour the big, integrated agencies. In May, WPP won a contract to handle all the advertising and marketing for HSBC, after the international banking group decided that parent companies and not their individual agencies should bid for the $600m it spends on such services every year. Samsung, a big South Korean electronics firm, is also expected to appoint a single group.

Nevertheless, the smaller agencies believe they can still compete by being more nimble. "There is definitely a change in the landscape," says Jane Asscher, chairman of 23red, a London-based agency that describes itself as "media-neutral" in its choice of outlets for campaigns. Ms Asscher believes that consumers are becoming far more sophisticated in their reaction to all forms of advertising and marketing, so smarter ways have to be used to reach them.

During the slump, some companies tried different forms of advertising and liked the response they got. "There's lots of ways to skin a cat today," says Scott Goodson, founder of StrawberryFrog, an agency based in Amsterdam that specialises in international campaigns. While his firm still uses traditional media, such as TV and print, it is often in conjunction with other techniques, such as "viral" marketing. This means trying to spread the message by word of mouth--still considered the most-powerful form of advertising. Sometimes that involves using the internet for e-mail messages containing jokes, film clips and games, which recipients are encouraged to pass along to friends.

No one knows just how important the internet will eventually be as an advertising medium. Some advertisers think it will be a highly cost-effective way of reaching certain groups of consumers--especially for small companies operating in niche businesses. But not everyone uses the internet, and nor is it seen as particularly good at brand building. Barry Diller, the head of InterActiveCorp, believes network TV is a great place to promote his company's websites, such as Expedia, his online travel agency, and LendingTree, a consumer lender. Unlike bricks-and-mortar businesses, web-based firms do not worry if their ad is being seen by lots of people in towns where they have no shops. They just want people to remember their website address--or at least enough of their name to be Googled.

So far, the internet accounts for only a tiny slice of the overall advertising pie (see chart 2), although it has been growing rapidly. A joint study by the Interactive Advertising Bureau and PricewaterhouseCoopers found that internet advertising revenue in America grew by 39% to $2.3 billion in the first quarter of 2004, compared with the same period a year earlier. Internet ad revenues are now back above what they were at the height of the tech boom.

And Google and Yahoo! have yet to unleash the full potential of their technology. Google, which already places text ads on other people's websites and splits the revenue with them, recently began testing a system to distribute display ads as well, in effect increasing its role as a sort of online ad agency.

Others are honing new techniques. As part of a recent campaign for American Airlines, the online edition of the WALL STREET JOURNAL used "behavioural targeting" to estimate how likely readers were to be frequent-flyers based on how much interest they paid to travel-related stories and columns. The targeted readers were presented with American Airline ads, and not just when they were reading travel stories. According to Revenue Science, a New York company that developed the targeting system, the results were dramatic: the number of business travellers who saw the ads more than doubled.

The potential for advertising on the internet is tempting more firms to join the fray. For instance, Microsoft is working on a search system with the intention of leapfrogging Google. Microsoft and others see that as more types of media, including music and films, start to be distributed over the internet, there will be more opportunities for online operators to put advertising messages in front of consumers.

Indeed, the makers of personal video recorders (PVRs) recently announced that their new machines will be capable of downloading music and films from the internet, as well as from TV. Many advertisers dread PVRs because they can be used to "time shift" viewing, allowing viewers to record their own schedules with greater ease than existing video recorders. Several studies have shown that users think one of the machine's most-appealing features is the ability to skip past ads. The providers of internet-based content might be able to slip in those ads in other ways than traditional 30-second commercials, perhaps through sponsorship deals or as display ads on the websites which PVR owners will use to select their programming.

BOMBARDED

People are tiring of ads in all their forms. A recent study by Yankelovich Partners, an American marketing-services consultancy, says that consumer resistance to the growing intrusiveness of marketing and advertising has been pushed to an all-time high. Its study found 65% of people now feel "constantly bombarded" by ad messages and that 59% feel that ads have very little relevance to them. Almost 70% said they would be interested in products or services that would help them avoid marketing pitches.

It has been calculated that the average American is subjected to some 3,000 advertising messages every day. If you add in everything from the badges on cars to slogans on sweatshirts, the ads in newspapers, on taxis, in subways and even playing on TVs in lifts, then some people could be exposed to more than that number just getting to the office. No wonder many consumers seem to be developing the knack of tuning-out adverts.

"Consumers are getting harder to influence as commercial clutter invades their lives," says a recent report by Deutsche Bank. It examined the effectiveness of TV advertising on 23 new and mature brands of packaged goods and concluded that in some cases it was a waste of time. Although in the short-term TV advertising would lead to an incremental increase in volume sales in almost every case, there was only a positive cash return on that investment in 18% of cases. Over a longer term the picture improved, with 45% of cases showing a return on investment. Not surprisingly, new products did better than older ones. The study concluded that "increased levels of marketing spending were less important than having new items on the shelf and increasing distribution."

The effectiveness of advertising is a hugely controversial area. Conventional wisdom in the industry is that sales may well increase for a certain period even after the advertising of a product ends. But there comes a point when sales start to decline and it then becomes extremely expensive to rebuild the brand.

This supports the idea of continuous advertising. But some people in the industry believe the conventional wisdom is no longer true. When America's big TV networks reached prime-time audiences of 90% of households, they were a powerful way to build a brand. Now that those audiences might be as low as one-third of households, other ways of promoting a brand have become more competitive. Moreover, many clients never really embraced continuous advertising: when times get tough, just as they did after 2000, one of the first things many companies cut is their ad budget.

Robert Shaw, a visiting professor at the Cranfield School of Management in Britain, runs a forum in which a number of big companies try to monitor the "marketing payback" from advertising. The return from traditional media was, he says, "never terribly good". Generally under half of ads provide a return on their investment. And there can be various reasons why ads influence sales, other than their direct effect on consumers. For instance, if a producer announces a multi-million dollar ad-campaign, then retailers are often persuaded to increase deliveries. This can result in a "distribution effect" that leads to additional sales.

Some companies have profited from re-allocating their spending across different media, adds Mr Shaw. But it is a tricky business to determine what works best. For many companies, and especially the media-buyers who purchase space and slots for ads, greater media diversity and the arrival of the internet has made a difficult job much tougher.

SOAP STARS

Some big spenders have already made clear choices. With an annual budget of more than $4 billion, America's Procter & Gamble (P&G) is the biggest advertiser in the world. Ten years ago about 90% of its global ad spend was on TV. Now the figure is much smaller. Last year the company launched a non-prescription version of Prilosec, an anti-heartburn medicine. It was one of the most successful brand launches in the company's history, according to Jim Stengel, P&G's global marketing officer. But only about one-quarter of the marketing spend on Prilosec went to TV. The rest was spent on other forms of marketing, such as in-store promotions.

P&G, which helped to launch TV soap operas as a new way to market goods, is now looking once again for novel ways to reach consumers. Three years ago it set up an operation called Tremor to recruit an army of several hundred thousand American teenagers. It uses them to discuss ideas about new products and to help spread marketing messages. In return, the teenagers get to hear about and use new things before many of their peers.

Getting trendsetters to buy (or be given) new products in order to influence a broader market is hardly a new idea. So-called "early adopters" are a similar group, much sought-after by consumer-electronics companies in order to give their new products a good start. But there is a wider group which marketers sometimes call "prosumers"; short for proactive consumers. Some people in the industry believe this group is the most powerful of all.

Euro RSCG, a big international agency, is completing a nine-country study of prosumers, which it says can represent 20% or so of any particular group. They can be found everywhere, are at the vanguard of consumerism, and what they say to their friends and colleagues about brands and products tends to become mainstream six to 18 months later. They also vary by category, says Marc Lepere, Euro RSCG's chief marketing officer: a wine prosumer, for instance, will not necessarily be a prosumer of cars.

Such people often reject traditional ads and invariably use the internet to research what they are going to buy and how much they are going to pay for it. Half of prosumers distrust companies and products they cannot find on the internet. If they want to influence prosumers, says Mr Lepere, companies have to be extremely open about providing information.

Despite all of these complications, many in the advertising business remain sanguine. For Rupert Howell, chairman of the London arm of McCann Erickson, which is part of the giant Interpublic group, the industry's latest downturn was the third he has experienced. As it did from the others, he says, the industry is emerging a little wiser. But, he insists, "the underlying principles haven't changed." Even the arrival of new media, like the internet, does not spell the demise of the old. Indeed, as he points out, TV never killed radio, which in turn never killed newspapers. They did pose huge creative challenges, but that's OK, he maintains: "The advertising industry is relentlessly inventive; that's what we do."