ADVERTISING, MEDIA, ANALYSIS, OPINIONS

Darren Woolley | Apr 7, 2021

How agencies are increasingly profiting from missing people

Agency retainer models fail to incentivise a reduction in staff churn with consequences for both employees and advertisers, says one industry consultant.

Each year, 600,000 people are reported missing in the USA. Of these, approximately 90% are found either alive or deceased. Missing people have a devastating impact on families, friends, workplaces, communities and society as a whole. But there is one place where the concept of missing people is a financial boon for the organisation involved. That appears to be advertising agencies.

The concept of missing people, leading to agency profitability, is not often talked about. Yet, increasingly, and particularly during the past 12 months, where many markets saw people furloughed or working from home, some of the larger agencies have been able to use their agency churn to reduce costs and improve their bottom line significantly.

How?

The issue is the continued reliance of many advertisers on the retainer fee model to engage their agency. The retainer means that the agency undertakes to provide an agreed number of resources to the advertisers for a pre-agreed fee based on the direct salary costs, multiplied by an agreed overhead and profit margin.

This agency fee model is incredibly convenient for advertisers in that the agreed resources are in no way linked to the agency's workload. The retainer is also convenient for the agency because it guarantees cost recovery for the agency staff covered by the retainer. But in recent years, the efficiency of the retainer has been questioned by advertisers and their procurement teams. Because while the retainer is convenient for agency and advertiser, determining the actual value of these retainer arrangements is often problematic.

Combine this with the churn rate of agency employees which, depending on the market and the agency, is between 20% and 40% of staff. There are often significant gaps in the number of staff members working on retainer. By way of example, using nice round numbers for clarity, assume there are 100 agency staff members retained on the account. Assuming an average churn rate of 30%, this means that over a year, 30 roles or 30 people will go missing. They could have left for other jobs, been promoted into other accounts in the agency or made redundant due to poor financial performance for the agency group as a cost-cutting exercise.

But if a person leaves, usually under the retainer contract, there will be an acceptable period to find a replacement. Let's choose four weeks. That means that 30 roles will be unfilled in a year for four weeks each, or 120 weeks in total, which is effectively 2.3 full-time people missing from the account across the year. The retainer allocation for those people would most likely go some way to pay for recruitment cost to replace those roles. However, this cost is typically built into the agreed overhead.
What if the average time to replace a role is not four weeks? What if, due to a pandemic and working remotely, or simply because there is a good shortage of qualified staff, it now takes 8 or 12 weeks to replace a role? The exact number is now doubled or tripled, with 4.6 people missing or 6.9 people missing under the annual retainer for the year, respectively.

Before we go further with the financial implications, let's consider the human cost. With 30 people missing for between 4 – 12 weeks throughout the year, on top of usual annual leave and sick leave, how does the work get done? The people left working on the account need to lift their workload to make up the shortfall. Therefore, within any particular agency function, e.g. account management, strategy, creative etc., the remaining staff take on extra unpaid overtime to make up for the shortfall.

The fact that advertising agency salaries are mainly exempt from overtime means there is no additional cost implication to the agency for this situation. It is a boon for the agency as the retainer for those roles, where the staff member is missing, including overhead and profit margin, goes straight to the bottom line. Depending on the seniority and fees charged, this could effectively add better than 20% to the bottom line. So, managing the missing people across an agency retainer can effectively drive agency profits. But at what cost to the agency staff. With stress, burnout and mental and physical health issues a growing problem for agencies, it is obvious this is not sustainable.

The problem for advertisers is this can be incredibly difficult to monitor. It is not as if they are all missing at the one time. Also, beyond the account management, many advertisers have little or no visibility into the state of the agency team retained. But a missing retainer resource here and there quickly adds up, and agency justifications for the missing people will often sound perfectly reasonable. But there is a solution.

Rather than insisting on paying an agency retainer, one solution for advertisers is to embrace an output-based pricing model that connects fees with agency workload. This places the responsibility on the agency to manage their resources better and rewards the agency for the quality and quantity of the outputs delivered, rather than paying them for the people they do, or do not deliver.

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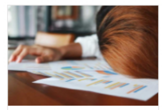

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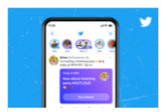

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