Industry outlook: Shifts, rifts and dislocation

By Sir Martin Sorrell

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During the last two years the shifting tectonic plates underpinning economic and political activity around the globe came together to release a series of powerful disruptive forces that have thrown the world into a heightened level of uncertainty for the near to medium future.

The world turns

In the Middle East, a political earthquake was triggered by the clash of ambition between regional players in the form of a new conflict focused on Israel and Gaza; the war in Ukraine ground on and the standoff between China and the US showed no signs of easing; artificial intelligence underwent a step change in evolution and public consciousness; and catastrophic climate change moved a step nearer as 2023 became the hottest year on record.

The aftershocks of the pandemic continued to rumble on in the form of new working practices, unprecedented reliance on technology, and an epic overhang of debt which combined with supply chain disruption to sustain damaging inflation and growth-sapping interest rates around the world. And as the population of India overtook that of China for the first time, emerging powers competed for influence in the race for leadership within a new multi-polar world.

So what does all this mean for the year ahead? Much will hinge on the outcome of major elections around the world. 2024 is set to be a milestone year for democracy with almost half the world's population choosing new leaders, including those in India, Indonesia, Mexico, Pakistan, Russia, the UK and the US. Whether Donald Trump or Joe Biden returns as President in the US is a question that will have a key impact on global politics as well as the outlook for business.

Otherwise, there are big questions to be asked about whether the embracing of AI will race ahead unchecked, what impact that will have in our industry, how China emerges from its growing pains and just how quickly interest rates are brought down by major central banks. But all the signs are that while economic uncertainty is reducing, political uncertainty is going to be greater than ever.

Here's what we know so far.

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We're in the midst of a poly-crisis

War in Ukraine, the conflict between Israel and the Palestinians in Gaza, the malevolent ambitions of Iran, the looming threat to Taiwan's independence, question marks over democracy itself in the US and elsewhere... all these are evidence of a crisis that has many heads surfacing around the world and casting a pall of uncertainty for business leaders wanting to plan for the months and years ahead.

The poly-crisis extends far beyond the geopolitical arena: climate change; loss of biodiversity; pandemic; and widening economic disparities all add to the sense of emergency on multiple fronts.

These are overlapping and interconnected challenges that can't be solved by any country in isolation and make a call on international collaboration that is itself struggling to provide a coherent response as the traditional level of consensus breaks down.

We have entered a period of intense competition between nations, where the 'easy' economic gains of the past are no longer readily available, and it seems so often that growth can only be clawed at the expense of other rival countries. That is leading to assertion of a new multi-polar world order no longer dominated by the US, in which new partnerships are being forged and ambitions pursued while the global outlook that has prevailed for recent generations is replaced by increasing fragmentation.

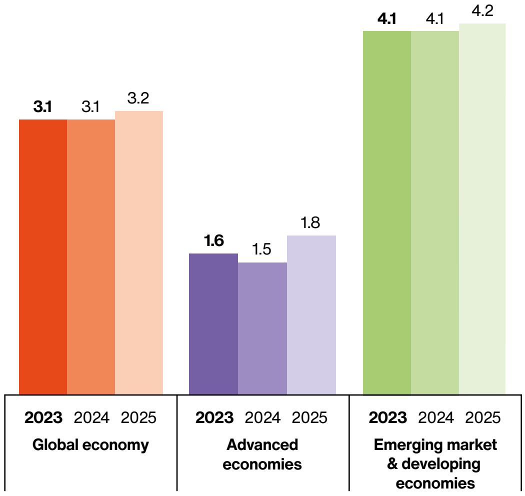
10 things to think about

1. The world is now changing from the 40 years since Professor Ted Levitt's 'Globalization of Markets' was published in the *Harvard Business Review* in May/June 1983.
2. GDP growth will be slower, inflation higher and interest rates higher than before.
3. US/China relations, Russia's ambitions in Ukraine and beyond, Iran's aspirations in the Middle East, along with North Korea's volatility, all mean increased instability.
4. In this new world, two trends are particularly important for our clients and us. First, pick your geographic markets more carefully, mainly in the Americas, the Middle East and Asia Pacific. Second, efficiency becomes more important. AI, the metaverse, blockchain and quantum computing will drive this efficiency gain everywhere, but particularly in lower-growth Europe.
5. In this new world, clients have to focus on three things: agility; taking back control of their marketing; and first-party data.
6. Digital will continue to dominate media spend from 65% now to more than 70% by 2025.
7. The six major platforms – Alphabet, Meta, Amazon, Alibaba, Tencent and ByteDance plus Apple, Microsoft, Nvidia, Adobe, Oracle, Salesforce and Musk – will continue to dominate digital media.
8. Clients and private equity will continue to focus on short-term results, so activation, performance and measurement have become ever more important.
9. Connected TV: retail advertising will become more and more important as linear TV remains under pressure.
10. AI will drive major changes in visualisation and copywriting, in hyper-personalisation, in media planning and buying, in client and agency efficiency and in the democratisation of knowledge. As a result, companies will have flatter organisational structures and become more efficient – just as Nvidia does driven by AI.

In 2023 China used the BRICS forum directly to challenge western hegemony as six emerging market countries – Argentina, Egypt, Ethiopia, Iran, Saudi Arabia and the United Arab Emirates – were invited to join the bloc. The E7 group of seven leading emerging markets – Brazil, China, India, Indonesia, Mexico, Russia and Turkey – now has a higher combined GDP than its established counterpart the G7, composed of Canada, France, Germany, Italy, Japan, the UK and the US. Even the E6, excluding China, would be larger than a G6 excluding the US. Saudi Arabia exemplifies the new-found ambition among emerging states. Its leader, Mohammed bin Salman, is attempting to position the country as a world political and economic power as well as masterminding a transformation of the company's image. Alongside well-versed investments in golf, cricket, football and cultural activities he has forged a close relationship with China, restored relations with Iran and was on the verge of normalising relations with Israel before the attack on 7 October last year.

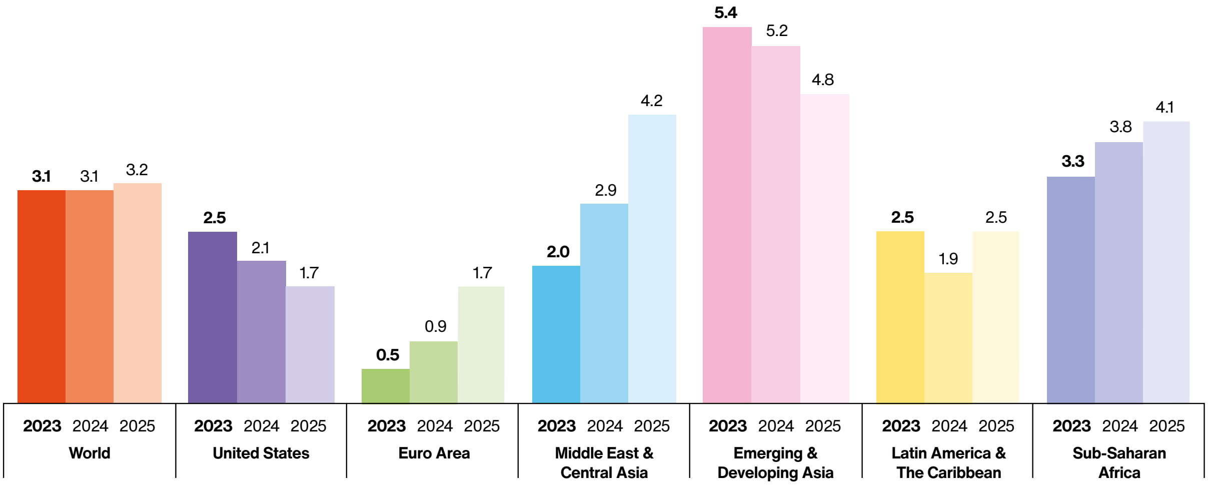
With this challenge to the old-world order, the philosophy of globalisation is in retreat. Geopolitical tensions exacerbate shortages and disrupt the supply chain, and the requirement to facilitate just-in-time manufacturing is becoming overtaken by the overwhelming need for security and de-risking.

World economic outlook growth projections (%)



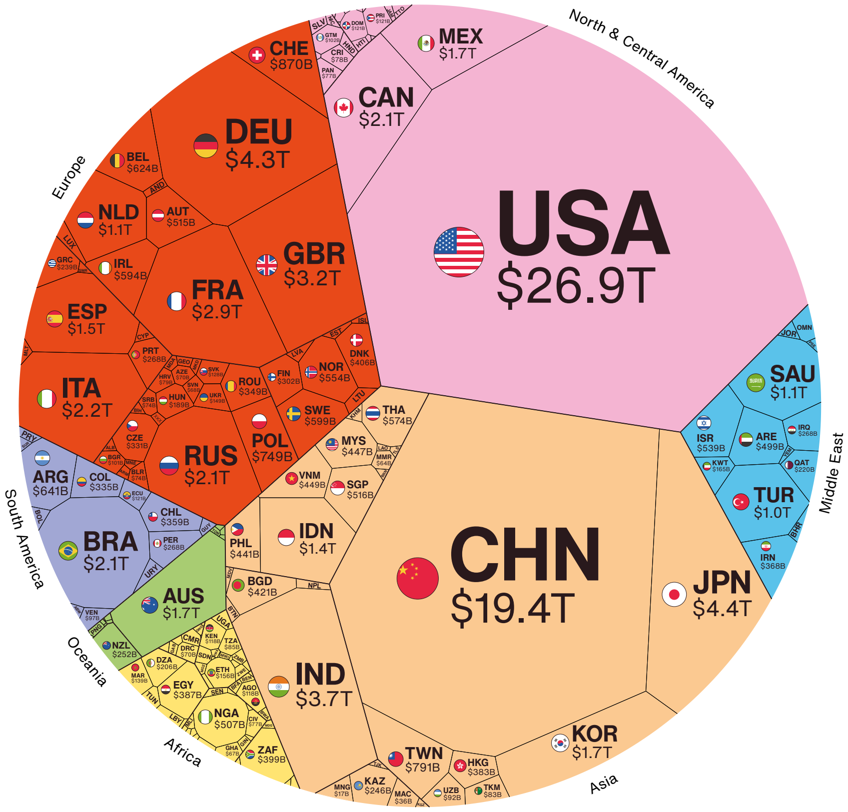
Source: IMF World Economic Outlook Update, January 2024

Growth projections by region (% change)



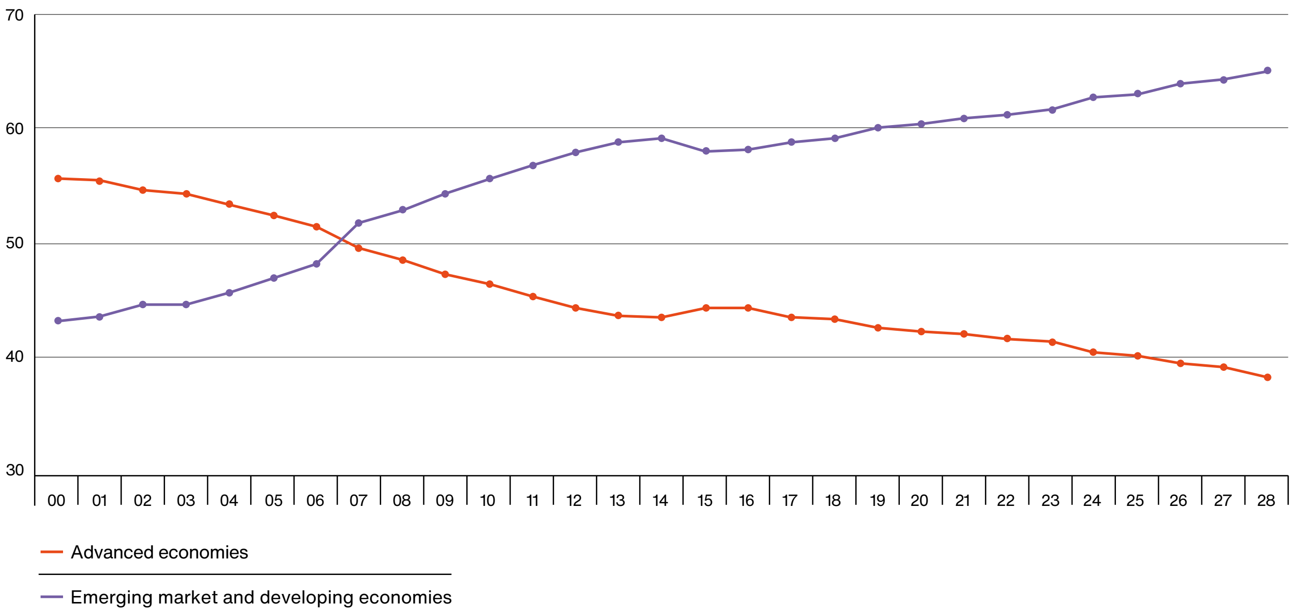
Source: IMF World Economic Outlook Update, January 2024

The $105 trillion world economy (global GDP 2023F)



F: Forecast
Source: IMF World Economic Outlook 2023

GDP based on PPP (% share of market)



Source: IMF, 2023

Companies that are over-exposed to supply from China are urgently looking to diversify as far afield as southeast Asia or north Africa; there's an urgent effort to build semiconductor manufacturing outside Taiwan; and the US is looking increasingly to South America to meet its sourcing needs.

Goldman Sachs reckons that global tensions will exacerbate supply shortages and lead to a commodities boom in 2024. But it's not just about politics: one major client told me their biggest problem last year was factories affected by flooding.

Growth is elusive

World economic growth in 2023 is panning out to be 3.1%. The IMF forecasts the same again for 2024. That masks a widespread variation from country to country and region to region. India has been a shining star with GDP growth forecast by the IMF at 6.7% in 2023 and 6.5% in 2024. India is a winner because of Prime Minister Modi's success – although he's controversial for some – and because it's the alternative to China. India's people are also really good technologically. For example, it's significant that a huge proportion of faculty at Harvard Business School, including two Deans, are from India. Indonesia is set to be a top five economy by 2050, and Vietnam is going great guns.

China still has good growth at around 5% in 2023 but many problems – from youth unemployment to the debt bubble in real estate to over-indebted State-Owned Industries. And the uncertainties around China, given the Taiwan risk, mean that there is an unwillingness to invest from overseas and assets are around 40% undervalued right now. There's also a long-term issue of population, with forecasts that by the end of this century, the Chinese population will have reduced from 1.4 billion to 770 million. President Xi was recently urging Chinese women to have more babies. (President Putin has been encouraging Russian women to do the same.) Every big company must decide whether they want to be bigger or smaller in China. Those with more than 20% of their production concentrated there will certainly have to think whether they want to go further. On the other hand, if you're Unilever or Reckitt Benckiser, with only a relatively small single-digit market share there, you almost certainly want to get bigger.

> The speed at which inflation and interest rates come down in the coming year is going to be the key determinant of economic prospects in the year ahead"

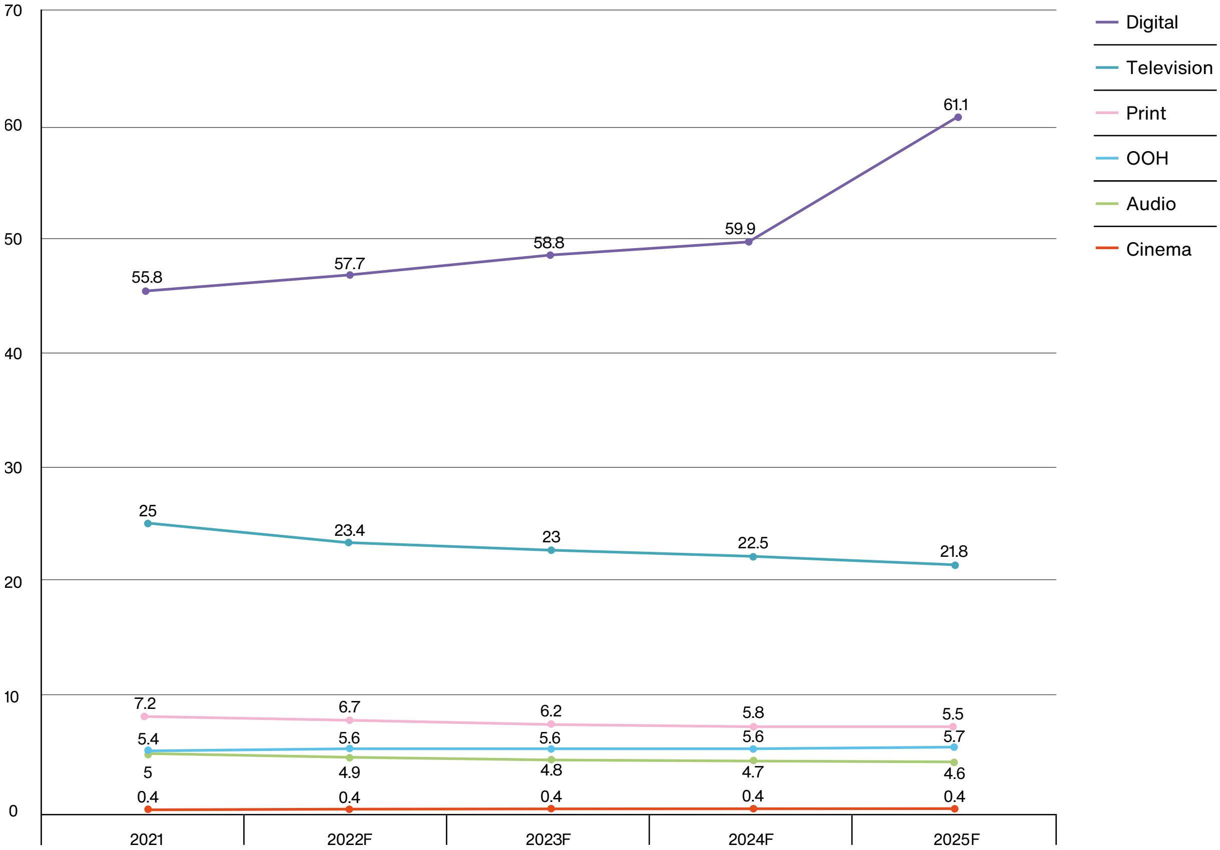
The US is doing better than most of the 'advanced' countries with 2.5% GDP growth in 2023, according to the IMF, although the direction will become clearer after the election. As someone pointed out to me recently, 10 years ago America was 25% of the world's economy – and it's still 25%. The US is vibrant and progressive, and technologically advanced and it still manages to punch above its weight with $27 trillion out of the $105 trillion global economy compared to China's $19 trillion.

Europe is in a deeper hole and is suffering from a dearth of good leadership. The UK is forecast by the IMF to grow at 0.6% next year, Germany at 0.5%. Europe has become a question of cost efficiency in a world where there's slower growth – and that's why digital transformation is so important, particularly driven by AI.

Inflation is deflating, but slowly

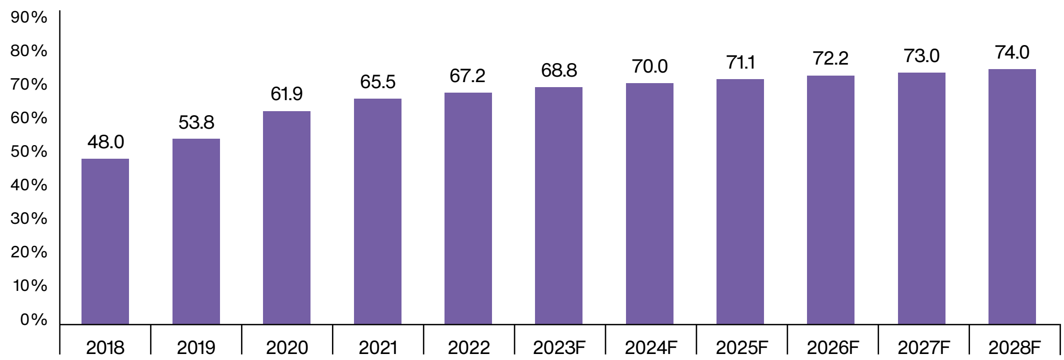
The speed at which inflation and interest rates come down in the coming year is going to be the key determinant of economic prospects in the year ahead. During 2023, inflation proved stickier than many people had expected and that meant central banks had to keep up interest rates to suppress demand. Inflation has proved more resilient in Europe and the UK than in the US, and although there was some positive news at the end of 2023, Europe's inflation saw a modest increase in December. Governments in many countries have to fund big deficits, in some cases well over 100% of GDP, and to sell bonds they have to offer an attractive return. The US is a case in point, and China is not buying bonds like it used to. If you offer a real return of 2% and inflation is still at 3% that indicates a bond yield of 5%.

Share of global ad spend by channel ($bn)



F: Forecast
Source: Dentsu 2023 Global Ad Spend Forecast

Share of digital in advertising revenue worldwide 2018-2028



F: Forecast
Source: Statista.com, 2024

Our market

7.7%

Digital media spend is projected to grow at 7.7% in 2024[1]

0.7%

Digital transformation services is expected to grow at 0.7% in 2024[2]

$305bn

AI is already a $305 billion market in 2024[3]

+26%

Top 25 agency groups had 2022 revenues of $130 billion, S4Capital Group has 0.92% market share, up 26%[4]

Sources:
1. GroupM, Dentsu, MAGNA, December 2023
2. epan, endava, Thoughtworks, CI&T, Globant, Accenture
3. Statista.com
4. AdAge, 2023

Clients have already become less cautious: little more than a year ago they were worried about interest rates going up; now they are focused on rates coming down. Lower interest rates will have a number of implications for our sector. Obviously, they will help stimulate investment and improve valuations of growth stocks; but reduced inflation will curb the ability to increase consumer prices and to use that to increase funding for advertising as a share of net revenue. Incidentally it will also eliminate opportunities for price gouging. In early 2024, Carrefour de-listed PepsiCo products in France because the retailer deemed they were priced too highly.

The US election will likely have a significant impact on the economy there. If the contest comes down to Biden vs Trump, it is the latter that business generally prefers. President Biden is seen as a big spender. Many CEOs rank regulation as their number one issue. President Trump represents low tax and low regulation.

Digital marches on

During 2023 the digitalisation of the media economy continued apace and the standout trend was the decline of linear TV. Revenues for linear TV were down something like 10% over the year and in some cases even more. Bob Iger, who's back at Disney, has had to do a *volte face* on selling ABC, although they are buttressed with live sports through owning ESPN. Disney now says it will focus on making ABC work with its streaming services. What's happening is a kind of repeat of what we saw with the decline of local newspapers though it has taken much longer and is a less dramatic decline. But it is the death knell of cable and broadcast TV in America, as linear sank below 50% for the first time according to Nielsen, and viewers progressively switch to streaming. And that is a reflection of what is happening, or has already happened, in other regions. PepsiCo was recently reported to be dropping linear TV media in some parts of the world.

Two areas of innovation are connected TV and retail media. Connected or addressable TV is traditional media's attempt to target people using IP addresses to personalise content on linear TV with more digitised executions. Retail media is the attempt by retailers to build their own ecosystem complete with advertising. Walmart and Walgreens are both doing this.

The share of advertising spend accounted for by digital is now around 65% worldwide, and is set to grow to 71% by 2025. What that means is that digital – which is where S4Capital is exclusively focused – continues to be the only growing segment of the advertising cake and that legacy advertising is set for continued decline.

Digital advertising is dominated ever more by the major platforms[1]. In 2023, of the nearly $630 billion digital advertising market worldwide, Google was 39%, Facebook was 18% and Amazon 7%. So that's almost

Note:
1. Statista.com

two-thirds of digital spend in the hands of three big players. TikTok broke through to 3%; Microsoft at 2%; and Apple at around 1%. Snap and X (formerly Twitter) at 0.8%; and Pinterest around 0.5%.

AI goes mainstream

If 2023 was generative AI's breakthrough year – to quote McKinsey – then it would be foolish to bet on the pace slowing down in 2024. Key milestones in 2023 included the launches of ChatGPT-4 by OpenAI, and Bard by Google – both taking natural language processing to a new level and bringing these capabilities within the range of millions of workers and even students. ChatGPT became the fastest-growing app ever, while a debate was ignited about the economic and social impact of AI.

That led to a flurry of investment in AI alongside growing focus on the ethics and governance – a topic on which the UK government convened an international conference. The Beatles released a single in which AI was used to recreate the vocals of John Lennon, and the year ended with OpenAI firing its CEO Sam Altman – apparently for his eagerness to commercialise the technology – and then reinstating him.

What does 2024 have in store? This could be the year when AI becomes truly monetised, with ChatGPT launching an app store, and Bard releasing a paid-for version. If CES in Las Vegas is anything to go by we will see AI integrated into every kind of consumer device, from refrigerators to smart TVs, cars – led by VW's range of EVs – and computer keyboards.

The winners from AI are going to be largely those who are already dominant in other technologies. These will include the big six platforms: Alphabet, Meta, Amazon, Alibaba, Tencent and Bytedance, as well as Nvidia, Apple, Microsoft, Musk and OpenAI, Adobe, Oracle and Salesforce. The big, in other words, are set to get bigger.

Advertising gets smarter

S^{4}Capital has been at the forefront of understanding how AI will change our industry for several years now, and that was recognized when *AdWeek* named Media.Monks as its AI Agency of the Year in November 2023. We've identified five key ways in which AI is set to transform our industry.

The first is **visualisation and copywriting**. Content, in the form of copy, images and video, can now be produced far faster. Something that took three weeks can now be done in three hours. Clients are going to want to share that benefit, because we are selling time – albeit we should be selling outputs.

Second is **hyper-personalisation**. When we produce a campaign for Rebel Moon for Narcos on Netflix, for example, we produce around one and a half million pieces of content. And the process is automated with the help of AI. The Netflix model is still the best: you use the first-party data to create the content: "You started this movie, why didn't you finish it?"

Third is **media planning and buying**. Out of the total $950 billion advertising expenditure, around $650 billion can be bought with algorithms. The great thing about that is we'll have better information to make better decisions. However, there are 200,000-250,000 people doing semi-automated manual media planning and buying worldwide whose future is in question.

Fourth, use of AI is **general efficiency**. In every department AI can be harnessed to improve efficiency and deliver solutions faster and at lower cost. An example is Media.Monks' collaboration with AWS, Adobe and Nvidia to deliver software-defined outside broadcasting in place of capital- and carbon-intensive physical infrastructure.

Fifth is **democratisation of knowledge**. Knowing what we know, within the organisation, being able to instantly tap the knowledge of every individual is a kind of Holy Grail that is becoming a reality thanks to AI. As an example, we now have over 800 people globally working on Google. If we can get everybody in that team to know what everyone else is doing, then you flatten the organisation, and you increase efficiency.

It's time to own your data

Google started 2024 by announcing that it will deprecate third-party cookies, initially on 1% of searches and with the objective of eliminating them altogether in the second half of the year. This is a step that was originally planned before the pandemic and was delayed because of covid-19. What it means is that, for clients, the imperative to harvest first-party data in order to understand your customers and to achieve personalisation becomes all the more pressing and is likely to be a key focus this year.

The second key priority for clients right now is the need for agility – a key corporate attribute that is really difficult for companies to attain. It is a cultural factor; people like to be in control of their own swim lane and not have interference, but one consequence of that is that politics becomes a huge distraction. Agility means being able to respond quickly and effectively in a world where the future is very uncertain and the situation is changing rapidly. The democratisation of knowledge that AI will facilitate will help to achieve that.

Taking back control is the third key priority for clients. After the financial crisis, zero-based budgeting came in and the trend to outsource went too far. But in a digital world where you have a vital need for first-party data, maybe in-housing is better than outsourcing. That may sound strange coming from an agency, but we are not trying to do ourselves out of a job. We have embedded models where we put our people inside a company, and other models where we support them to in-house it and then provide continuing services around technology. One is the subject of the business school case study around Sprint and T-Mobile. We won an award for Manufacturers Life, where we in-housed their media. We are continuing services around technology.

Short-termism also continues to be an important perspective for clients. Advertisers such as packaged goods companies whose budgets rose last year because they were set on net revenue, didn't put the money into linear TV – they put it into the platforms, because it is easier to measure and you can see the impact on sales. So the focus of spending has been moving down the funnel from branding towards activation performance, and that's largely because of the short-term focus from investors. Purpose is still there in the corporate boardroom – especially because of the threat from climate change – but because of economic pressures it has moved down the agenda.

The road ahead

2023 was a period of adjustment and some retrenchment in our industry, as we evaluated our own response to this changing and uncertain world. For the big tech companies – Apple, Google, Meta, Microsoft to name a few – it was the year of efficiency and everyone reduced their headcount significantly. At S4Capital we grew from 1,000 to 9,000 people very quickly and we have now reduced to around 7,700 in line with the changing demand. The tech companies reduced their

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spending on advertising, even while their revenues were going up, and so we are overdue for that ratio to be revisited.

Our business model remains as valid today as when S4Capital started in 2018 – 'digital only, data driven, and faster, better, cheaper or more efficient'. We've added those last words because of the impact of AI which means we are now able to produce so much more within the same budget.

In terms of our breakdown of revenues by practice, Content is currently around 60%, Data&Digital Media 25%, and Technology Services 15%. I'd like that to evolve towards 50/25/25. And, geographically, we are about 80% in America, 15% in EMEA and 5% APAC. I'd like it to be 60/20/20 – keeping EMEA at the same portion but doubling our revenues from APAC.

We are still working out our new way of working since the pandemic. Undoubtedly some things have changed forever. I was watching CNBC and they had on an interviewee from Phoenix, Arizona. It's seven o'clock in the morning, so in Phoenix, it would be midnight. This guy is sitting in his office talking about the markets and it seems pretty obvious that he's decamped to Arizona because there's less state tax. On average, our people are in the office three days a week. I'd like it to be more, but there is academic research which suggests the key step is to ensure you have social gatherings – whether that's once a week or once a month – that provide the glue in your organisation.

It's going to be another tough year. CEOs are bullish, but the CMOs often less so. There is less caution around the economy looking forward, but threats, disruptions and uncertainties, particularly in the political sphere, are very real. The outlook may improve after the US election but, for now, the byword in every boardroom is going to be risk.