DIGITAL ADVERTISING'S NEXT LEG OF GROWTH?

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Key takeaways:

- If small businesses have shifted most of their spend online and digital-first companies are beginning to mature, double digit digital advertising growth will depend on sustained expansion in digital business transformation from "traditional" marketers - brands whose businesses have historically existed offline primarily.
- Traditional marketers who anticipate that business transformation will meaningfully impact their category will benefit from investments in long-term relationships with media owners whom they expect will be important in years ahead
- All marketers should continually assess the optimal balance between investing in brand-building activities which provide long-term benefits and shorter-term transactions

Some observers have claimed that the driver of digital advertising's rapid pace of growth in recent years is small businesses, although this is doubtful. While it may be true that some companies have benefitted from small business spending, it is not likely true for all of digital media. For example, in the United States data from the IRS indicates that small businesses – which we define here as the nearly 6 million companies with less than $5 million in annual revenue – only spends around $30bn on advertising every year. If digital advertising in its broadest definition is likely to be around $130bn in the US during 2019 vs. $107bn during 2018, even if small businesses increased spending from, say, $20bn to $30bn (an unlikely escalation in any one year) it wouldn't even amount to half of the industry's growth.

Instead, as we have previously written, the more likely factor responsible for most of the growth in digital advertising is ad spending by the world's largest digital companies, although this spending will slow. Many companies whose histories began on the internet now among the world's largest marketers with at least ten spending more than $1bn on advertising annually, dozens spending in the hundreds of millions and all of them collectively increasing their spending at a pace that is significantly faster than total industry-wide spending on digital advertising. However, it would seem inevitable that as their businesses mature and begin to eventually grow in line with the industries in which they operate, these marketers' growth rates will eventually decelerate and converge with industry averages. Further, as these marketers mature, their media mixes shift to include other media (to point, at least some of the resilience of television and outdoor advertising is due to such shifts of spending).

Will traditional large brands help digital advertising sustain its recent growth rates? This leads to an interesting question regarding whether or not a third segment of marketers can pick up the potential "slack" and sustain rapid growth for digital advertising for years to come: traditional, large brands who are the incumbents in their industries. Already we can see that the typical marketer of this nature is allocating around 40% of their advertising into digital media, with many well in excess of that figure. If their spending on digital is less than half today, on average, a digital media optimist could argue spending directed to digital media still has a significant amount of room to expand. But is that realistic?

The first consideration on further meaningful shifts of spending into digital media by traditional brands is whether or not digital media can better demonstrate its brand-building capabilities. While a powerful brand idea executed well can always work in any given medium, so long as the marketer works to optimize a campaign for a given medium, on balance premium video (mostly still television) is likely going to be the environment that continues to support brand-building efforts for most marketers. (A related consideration is the idea that traditional media owners are increasingly the beneficiaries of digital media spending, especially as their media brands are distributed via digital platforms. Is this spending digital or non-digital? Budgeting will be in the eye of the beholder.)

As well, there are ongoing challenges to brands around digital media, including the increasingly "toxic" environments with platforms who do not curate content or other advertisers, with the widespread availability of inauthentic content (including fake ads) and other polarizing or extreme content. Measurement remains as another problematic issue, as fragmented, incomplete and often low-quality sources of data make it difficult to assess the metrics that brand-focused marketers want to rely upon in order to manage their budgets well in digital environments. Digital media's brand-building capabilities are limited by these trends. The big question is whether or not brand-building is the focus of brand owners into the future? It may not be.

Business transformation efforts from traditional brands will orient those companies' media plans towards digital media. As these companies increasingly invest in digital business strategies – business transformation for lack of a better term – including direct-to-consumer concepts, sales via third party e-commerce channels and focus on driving consumers to digital experiences (including marketers' websites or branded content) more growth in spending on digital media will occur. As of this point in time, most brands generate only a small percentage of their revenues e-commerce, but there are some brands pushing towards half or more of their revenues or consumer relationship activities from non-traditional environments, demonstrating possibilities yet to emerge. Of course, some categories will never be meaningfully digital (gasoline for automobiles is one example), and growth trends will not be evenly distributed around the world, as some countries will widely adopt new business models sooner than others.

What are the implications for marketers? One's view on the pace and potential scale of business transformation in a given country should inform one's view on the future growth rate of digital advertising. If business transformation will be slow – whether because of friction in a country's labor laws, a lack of competition among companies in key sectors or limited broadband access – digital advertising growth will be relatively slower. If business transformation is more rapid, growth in digital advertising will be more rapid. Arguably, business models which might emerge because of faster and cheaper mobile broadband services will contribute to rapid digital advertising growth. Where this is true, marketers will benefit from identifying preferred long-term media owner partners likely to have high quality digital media inventory over a multi-year time horizon, as the most premium inventory will become more scarce as time progresses. On the other hand, in markets where business transformation is only going to move gradually – and where digital advertising growth is slower – securing long-term access to high quality inventory will be less important.

More generally, given the nature of business transformation and the likelihood that marketing resource allocations will need to evolve at the same time, important questions should be studied to inform those allocations. Towards those ends, marketers should continually assess the optimal balance between investing in brand-building activities (whether via media or without the use of media, and whether online or offline) which provide long-term benefits and shorter-term transactions.