How to Add Value with In-house Digital Capabilities

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If you're the CEO of a small-to-medium sized public relations firm, it's very possible that a good part of your thinking about the future growth of your agency focuses on formulating a strategy for the sale of your firm someday. That day may not come this year, or in the next five years, or even in the next decade. But you're likely thinking about it. And, the fact is it's never too early to begin laying the foundation for a successful, and lucrative, transition in ownership.

For the hundreds of agency CEOs we at The Stevens Group know, their primary concerns– those that keep most of them up some nights – are retaining top talent, generating strong cash flow, and building a loyal, diversified client base. If you neglect any of these essential management concerns, you do so at your peril. They are responsibilities CEOs do by rote or you wouldn't have made it this far. But when your thoughts turn to building equity to one day attract a buyer, you should be paying particular attention to the way in which you provide your clients with the digital and social media marketing services they are undoubtedly demanding from you. From an agency valuation standpoint, for those CEOs whose growth strategy includes a possible acquisition, if you're continuing to outsource your firm's digital media offerings, bringing those capabilities in-house now is one of the smartest things you can do in order to build value for your firm in anticipation of an eventual sale, regardless of the current size of your firm.

Here, we'll examine why making digital capabilities a core part of your in-house service offerings is an absolute imperative when planning for future growth and increasing agency value.

Keeping Up With the Times

By any measure, the pervasiveness of digital media today cannot be underestimated. Pew Research Center reports that as of August 2017, two-thirds of Americans are using social media channels as an ever-increasing source of the news they read and watch. McKinsey & Company's year-end Global Media Report 2016 predicts that by 2018, digital media spending will actually exceed traditional media spending. Even traditional media outlets now devote a significant amount of time and space to covering content borne via social media channels.

Therefore, it should come as no surprise that the public relations industry is endeavoring to stay one step ahead of this trend. Clients are increasingly shifting the bulk of their marketing dollars to digital media. And in our company's recent 2017 online survey of 800 PR firm CEOs — the majority of which head up firms earning $4 million and under in annual net revenue – more than half cited digital marketing capabilities as their single greatest priority in remaining competitive.

What did surprise us, however, is the proportion of PR firms in this segment that presently lack the requisite in-house digital marketing capabilities: One-third of the respondents to TSG's survey are outsourcing this critical function to external companies or freelance personnel. That's tantamount to an auto-repair business admitting to its customers: "Sure, we do all kinds of work here, but we outsource brake jobs, powertrain problems and electrical issues. We send that stuff down the street, add a markup, and you're none the wiser." Is that really the message you want your firm sending to clients, prospects and one day to a buyer?

The Façade of Strategic Alliances

For sure, using vendors makes sense for certain routine tasks at your firm, such as servicing the photocopiers, emptying the wastebaskets and recycling bins, and administering the company's 401k plan. Your clients don't really care how you tend to most operational tasks. However, with the role of digital media only increasing in importance within the public relations industry, it makes little sense to rest your firm's long-term success and reputation on subcontractors that provide the digital/social services your firm should really be allocating its resources to be able to provide in-house.

You may not personally know the first thing about building a smartphone app, what a wireframe is, how hashtags work, or what MySQL does – and that's okay. But your clients expect you to have professionals on staff who do. Putting digital capabilities under your own roof helps to ensure maximum efficiency and integration. It also can become a real profit center for your firm, rather than just a dreaded monthly ordeal of cutting checks to subcontractors. And from the standpoint of virtually every buyer agency we work with at

TSG, it will put much more money in a your pocket if/when the time is right to sell your firm.

If you're pitching digital media capabilities to potential clients as a core competency of your firm, and you don't actually employ people to provide those services, any so-called "strategic alliance" is merely a thin veneer on your firm's brand. That window dressing will become painfully evident once a potential suitor begins conducting due diligence on your company's overall financial health.

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SOME PEARLS OF WISDOM FROM ART STEVENS FOR PR AGENCY BUYERS & SELLERS

> *The time to sell your PR agency is when you've had at least two good years in a row –higher revenues and profits. If you encounter an off year after two or three solid growth years in a row, as Desi said to Lucy, "You've got a lot of 'splaining to do" to a buyer if you try and sell your firm. Avoid the explanations and the excuses. Sell when you're hot. Don't sell when you're not.*
>
> *Sellers need to consider a menu of options so they can make the wisest decisions on their future.*
>
> *Do you remember the famous song Judy Garland sang in the movie "A Star is Born?" The song was "The PR Firm That Got Away." If you as a buyer have identified a PR firm you're genuinely interested in, don't let it get away.*
> *You may not sing as well as Judy Garland but you have other means at your disposal to demonstrate to the acquisition candidate that your interest is deep and sincere.*
>
> *What many would be sellers don't understand is that if they can't get their businesses running like a business then an*

eventual interested buyer will pass.

Hey, PR agency owners: do you really need to hire that $100,000 a year account manager? I'll bet your present staff could handle the new business that just came in. See? I just saved you $100,000 which will go directly into your pocket.

To negotiate the best deal for your agency make sure that there aren't any individual accounts that are more than 20% of your total revenue.

A common fault among many PR agency owners is that they have too many account people for the business they have. This reduces profitability and the amount of money agency owners can take out. The rationale? Account people are needed for the next wave of new business. Lesson to be learned: tomorrow may not come that quickly. Plan for today and thrive.

Selling your PR agency for the highest price is no longer the number one reason to sell. The number one reason is jump starting your career and the opportunity to work with an exciting buyer.

PR agency owners: beware burning your account people out. If they routinely work twelve hours a day you're heading for trouble. There's enough stress in the agency world as it is. Do yourself and your people a favor. Send them home at a decent hour.

Go the accrual route for a more accurate reading of your financial statements, particularly if you plan to sell your PR agency.

PR agency buyers and sellers: do not allow email communications to replace good old-fashioned phone conversations and in-person get togethers. Emails provide great opportunities for *miscommunications, incorrect interpretations, and negative outcomes.*

PR agency sellers beware. Don't make the mistake of signing a letter of intent with a prospective buyer and then attempt to change terms already agreed to when presented with a purchase agreement. Big mistake. Your deal could implode.

Don't fret if the first two buyers that have expressed interest in acquiring your PR agency decide the fit isn't right. Some may simply be lactose intolerant. There will be a glut of buyers out there for whom the fit is indeed right. The key is to widen the net and find them.

If you sell your PR agency to exit altogether in less than two years you're leaving a lot of money on the table. Commit to at least two years and increase your purchase price by almost 30 percent.

PR agency owners often tell me they want to sell their firms when they reach a certain milestone – $1 million, $5 million or $10 million in revenues. I then ask them what their thinking would be if their revenues went down and not up. That's when there's a long pause. Lesson to be learned – take nothing for granted. Business takes funny bounces. Sell while you're ahead.

PR agency buyers beware. Don't construct an offer that is so complicated it would take a rocket scientist to unravel.

PR agency owners walk a fine line. Running a business properly and making a profit is vital. But there's such a thing as making too much profit. That could mean working your staff to the bone and under servicing clients. The result can be churning clients and staff in and out.

A PR agency CEO wears two hats: one of a competent PR pro who *is valued by clients. And one of a business owner who wants to make money in the process.*