Quality Adjustment Paper on:

ISIC 7310 Advertising

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Introduction

• ONS-CSO questionnaire (2009) showed that around half of countries with advertising SPPI account for size of audience in some way

• But...is audience size a suitable quality adjustment?
Advertising services

- Creative services
- Media placement services
  - Media (advertising) agency
    Buys media space on behalf of their client. May charge as a broker or a wholesaler.
  - Media marketer
    Buys media space from the broadcaster/publisher and re-sells this space to their client.
The Voorburg Group

• “The objective of the VG is to establish an internationally comparable methodology for measuring the constant dollar outputs of the service industries”

• Need to assess the issue of quality adjustment from the perspective of treatment of Advertising placement in the national accounts
How might we view industry output

• As a broker

• As a reseller

• Is audience size related to industry output?
Industry output

- Media space of different audience sizes are different products
  - *Everyone* agrees on this!

- Advertising that reaches more of the target audience is seen as more desirable

- Is the service of *placing* advertising different for different sized audiences?
  - 2008 SNA suggests it is,
    - at least for some markets

- Looking at different industry practice might help us
Different billing methods

• Net basis
  – Broker

• Gross basis
  – Reseller
  – Broker
    • Cost of media space included
Different pricing mechanisms

• Commission, contract fee, methods based on working time
  – Usually for net billing methods, and brokers

• Expected audience size
  – Explicitly
  – Often implicitly
    • “30 second slot during match of the day”
  – Gross or net billing, brokers and resellers

• Achieved audience size
  – “1.5 million viewers”
  – Gross or net billing, brokers and resellers
Output: turnover and deflation

- Advertising SPPI used to deflate Advertising Turnover to get Advertising output

- Important that price index concept aligns with turnover so that output is the correct measure

- So what do we see in Advertising turnover?
Turnover practices vary

- Some markets have a net basis
  - eg, USA

- Some markets have a gross basis
  - eg, UK

- Some markets have a mix
How do we perceive the industry output?

• Where a net billing approach is used, we can clearly see the service separated from the media space

• Where the gross billing approach is applied, the value of the media space is included in turnover
  – The current price output of the advertising placement industry has some component where different audience size is an indicator of different products
How to proceed?

• For the net approach, this should be fairly straightforward
  – A change in service delivered must flow through to output

• For the gross approach, this depends on how the activity of the industry is viewed
  – And different viewpoints call for different solutions with respect to quality adjustment
1. The industry is a broker

- Advertising brokers are like stockbrokers etc.
- Bring buyer and seller together without taking ownership
  - And not including media in the billing method
- Audience size is not a consideration
2. The industry is like a wholesaler

- Buys and resells media space
  - Or at least includes media space in the billing method

- Service is the same for a broad range of products
  - 1.45 million audience is the same as 1.5 million
  - 10,000 audience is not the same as 1.5 million
    - Compare the approach of trade margins
  - This is implicitly an “expected audience size” type pricing mechanism

- A change in the size of the achieved audience is not a function of the industry
3. The industry adds value by achieving an outcome from a portfolio

- This is for resellers only

- A reseller buys a range of different media slots
  - Different channels, different times, terrestrial, cable and satellite TV etc.

- The service is managing the portfolio so that client achieves a certain outcome
  - The client buys “1.5 million audience achieved”

- A drop in achieved audience figures reflects on poor portfolio management
  - A change in the output of the industry
### Example 1: Broker type, no quality change

<table>
<thead>
<tr>
<th></th>
<th>Price</th>
<th>Quantity</th>
<th>Turnover</th>
<th>Price Index</th>
<th>Output (constant prices)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Q1</td>
<td>1000</td>
<td>10</td>
<td>10,000</td>
<td>100</td>
<td>100</td>
</tr>
<tr>
<td>Q2</td>
<td>1500</td>
<td>10</td>
<td>15,000</td>
<td>150</td>
<td>100</td>
</tr>
</tbody>
</table>
Example 2: Reseller, expected audience size (wholesaler view)

<table>
<thead>
<tr>
<th></th>
<th>Price</th>
<th>Quantity</th>
<th>Turnover</th>
<th>Expected Audience</th>
<th>Achieved Audience</th>
<th>Price per expected viewer</th>
<th>Price index</th>
<th>Output (constant prices)</th>
</tr>
</thead>
<tbody>
<tr>
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<td>1 million</td>
<td>1 million</td>
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<tr>
<td>Q2</td>
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<td>1 million</td>
<td>1.5 million</td>
<td>0.0015</td>
<td>150</td>
<td>100</td>
</tr>
</tbody>
</table>

- Expected audience size remains the same
- Product remains the same
- No quality adjustment
- Output remains the same
Example 3: Reseller, achieved audience size (portfolio manager)

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<tr>
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<th>Price</th>
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</tr>
</tbody>
</table>

- Achieved audience size changes (better portfolio management)
- Product has improved
- Quality adjustment applied (price per achieved viewer used)
- Output increases (as desired)
Issues

- Discounting occurs in addition to changes due to audience size

- Caution needed
  - Need to allow discount to pass through as price change
  - But need to remove that part of observed price change that is due to change in audience size
    - Where we believe that this is a change in output
Example 4: Reseller, achieved audience size (portfolio manager) in the presence of discounts

- Achieved audience size changes (better portfolio management)
- Product has improved
- Quality adjustment applied (price per achieved viewer used)
- Output increases (as desired)
So which is right?

- For those billing methods that don’t use any audience size, audience size is not an issue.

- For those methods that use expected audience size (implicitly or explicitly), the service only changes when the expected audience size changes.

- For those billing methods that use achieved audience size,
  - a change in audience size is *not* a quality change if we consider the service like a wholesaler.
  - a change in audience size is a quality change if we consider the service as some sort of intermediary / portfolio manager.
So which is right?

• Different circumstances apply in different markets

• Different national statistical offices may view the market output differently
  – And sometimes, even within the office!

• It is clear that turnover is effected

• “It depends”
Summary

• Achieved audience size is not a function of the activities of Advertising Placement

**BUT ...**

• Audience size can appear in some billing methods and flow into turnover

• Whether this is a change in output depends on how the output of the industry is viewed
  – If we believe that the output is like a wholesaler, variations due to audience size should be seen as price effects
  – If we believe that the industry adds value beyond the wholesale activity, it is appropriate to remove the effect of change in audience size
Questions?

• Thank you