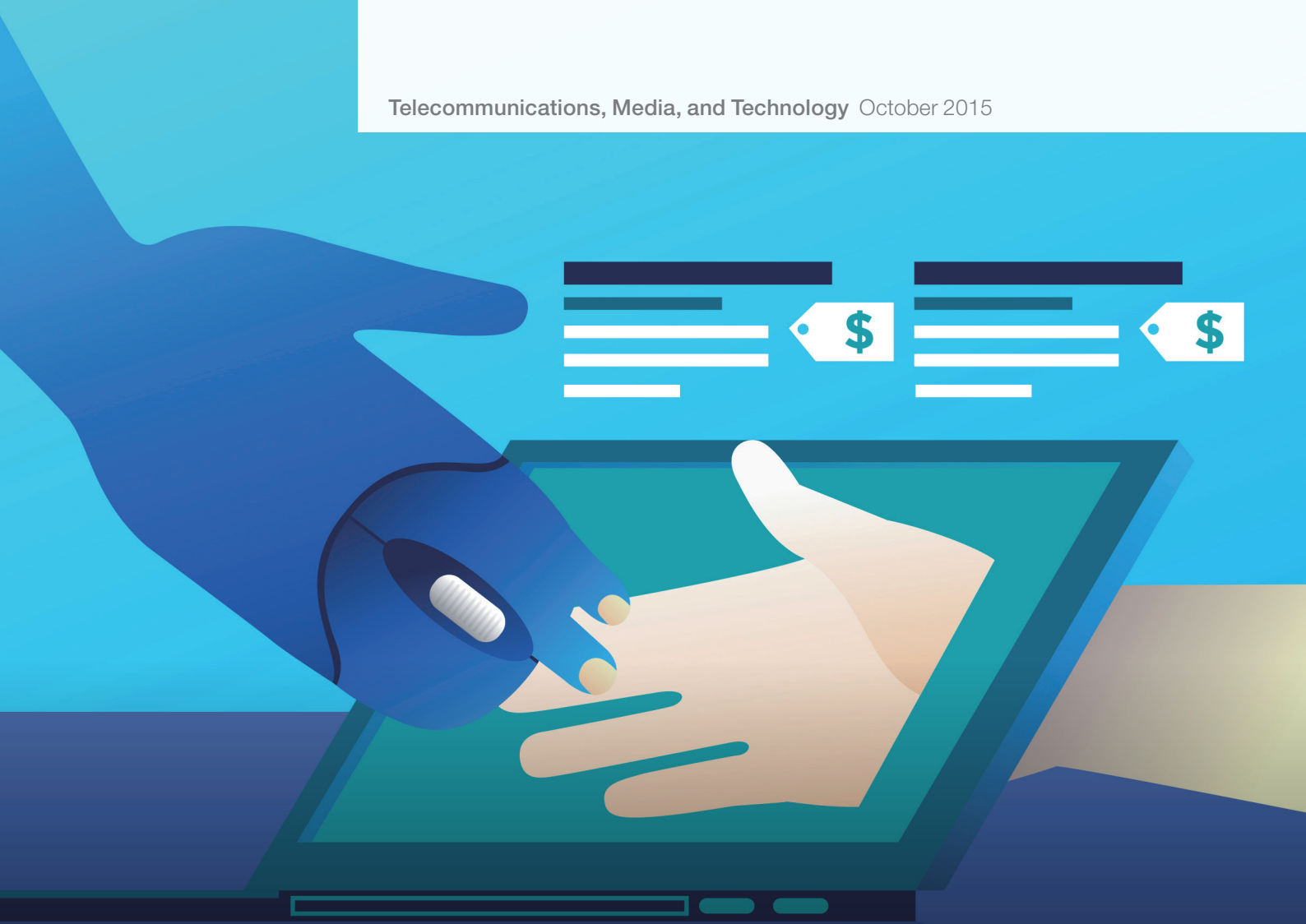


Online classified ads: Digital, dynamic, and still evolving

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Online classified ads: Digital, dynamic, and still evolving

The marketplace for online classified ads is rapidly gaining ground. In some markets, players and platform models have emerged as dominant, but market-shaping opportunities exist for players across the board.

Looking for a used car in Germany? Almost half of German buyers start their search with online classified ads. How about second-hand goods in Norway? Almost three-quarters of Norwegian buyers start by browsing online ads. The Internet has quickly become the virtual flea market of choice in many places, and a McKinsey survey detailed how differently national markets have evolved.

For decades, classified ads were the domain of newspapers, which offered advertisers cheap, small-type notices sorted under specific categories. The ads gave shoppers an easy way to browse various local offers, usually from private sellers. The jump from print to digital was inevitable and has proven itself to be quite lucrative for digital players. In emerging markets, online advertising has enjoyed double-digit annual revenue growth rates, while in more mature markets, annual revenue growth rates are not far behind at almost 10 percent.

The stakes in online classified advertising are high. Market leaders often capture profit margins of 40 to 50 percent and clearly dominate their markets. Understanding how the industry is developing and the differences among national markets can be crucial to success.

The evolution of online classified ad models

McKinsey research into this industry detailed two primary online classified ad business models that have evolved. The first one, the horizontal model, offers ads across a wide range of categories, from bicycles to hair styling. Among the best known horizontal sites is craigslist in the United States. Another is Norway's FINN. In the second one—the vertical model—a site focuses on a single category, such as cars with AutoScout24, the European automotive leader in the category, or real estate with Rightmove in the United Kingdom. To better understand how the online classified ad market has evolved and identify underlying trends, McKinsey surveyed around 11,000 classified ad consumers online in Brazil, France, Germany, India, Italy, Norway, Russia, Spain, Turkey, the United Kingdom, and the United States.

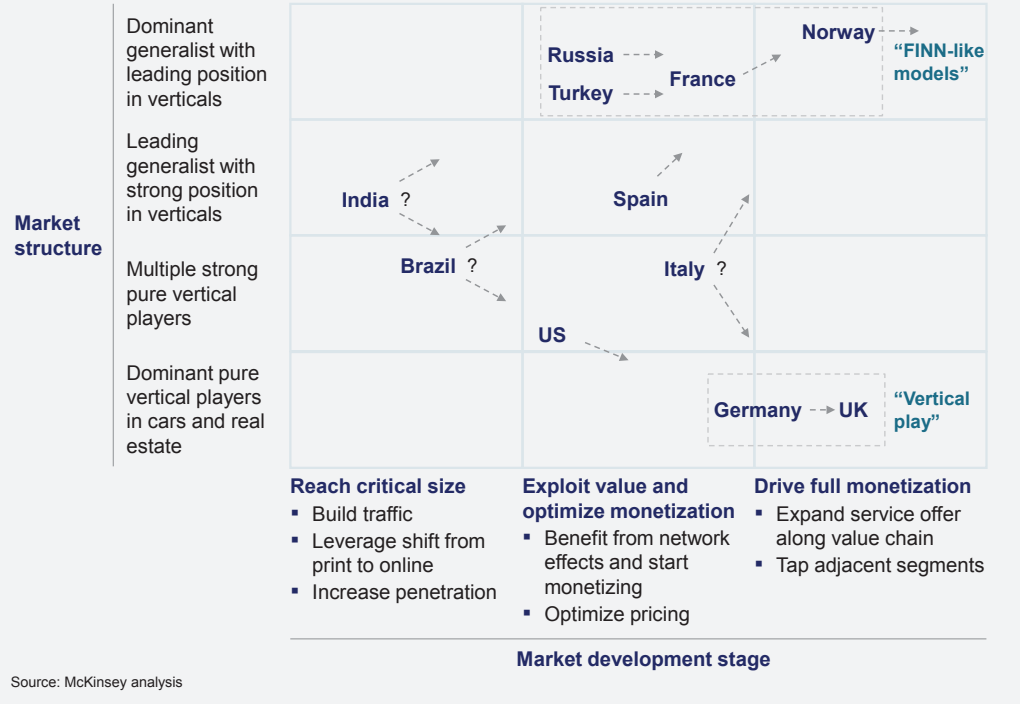
McKinsey research indicates that while both models are evolving, each model's speed of penetration and level of dominance vary by market (Exhibit 1). Countries like France and Norway, for instance, are moving faster under the horizontal model, with about 75 percent of the consumers surveyed turning first to online advertising when searching for second-hand merchandise across a range of categories. Others, such as Germany and the United Kingdom, feature a strong mix of print and online classifieds, with the vertical model dominating. And finally, in Brazil and the United States, consumers still embrace print classifieds. In the United States, for example, only 28 percent of consumers surveyed turned to online ads first when searching for a used car, compared with an average of 43 percent in other developed markets.

Markets where horizontal online models dominate

In advanced markets with dominant horizontal models, consumers have embraced online classified advertising across all categories. France and Norway are examples of strong online markets that offer a wide range of goods and services. The respective leaders

Exhibit 1

Online classified ad model type and penetration vary widely by region



in each of these markets show very high first-choice values—up to 90 percent across the various categories surveyed. For example, 48 percent of survey respondents said they turned first to French market leader Leboncoin for used cars and 48 percent for real estate, topping all other players in these categories. Similar figures can be seen for Norwegian leader FINN (Exhibit 2).

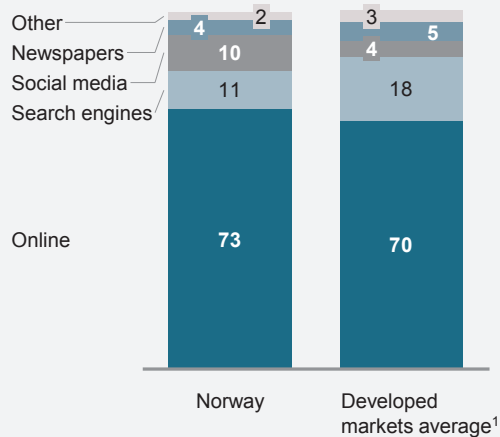
In many markets where the horizontal model is strong, classified ad sites seem to assume the role played elsewhere by established e-commerce sites, especially for consumers seeking hard-to-find items like foreign merchandise or specific branded wares. In Poland, for instance, local classified ad player Allegro—offering used and new merchandise—enjoys a 40 percent market share in e-commerce, a figure on the order of that achieved by Amazon in its dominant markets.

In markets like France and Norway, the current market leadership of horizontal online classified ad models seems clear, but this doesn't mean the game is over for aspiring new entrants. In fact, it is the strength of these sites and their tremendous power to monetize that is also their weakness. Free models—born out of social media communities in particular—can threaten the “incumbents” and disrupt these markets by expanding into services similar to classified advertising. Norway, for example, is one of the world's most advanced online classified ad markets, yet 10 percent of survey respondents there said they go to social media sites when looking for second-hand items, compared with an average 4 percent in other developed markets. In more than 3,500 local Facebook communities, consumers also find used merchandise such as cars. Not only can new platforms challenge the current heavy-hitters, they can do so without sticking to the horizontal model.

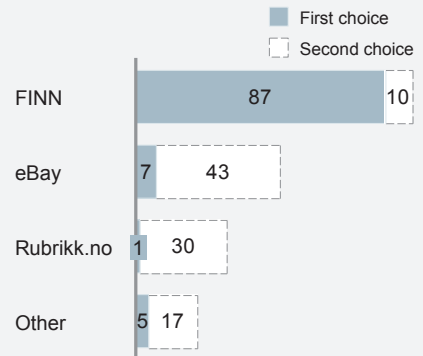
Exhibit 2

In horizontal-dominated Norway, FINN has a near-monopoly in general online classifieds

Starting point when looking for second-hand merchandise
Share of respondents, percent



Preferred websites in Norway
Share of respondents, percent



¹ Includes France, Germany, Italy, Norway, Spain, the UK, and the US
Source: McKinsey survey of around 11,000 classified ad consumers, January 2015

New business models like trade-ins—webuyanycar.com, for example—offer a different consumer value proposition in a vertical model and have the power to attract consumers for different reasons than classical classifieds players.

To successfully disrupt these markets, leaders will need to act in three very specific ways:

Monitoring. Leading horizontal players need to take a closer look at the relevance of their site listings. Understanding if, for example, one website lists more relevant goods or services than another or has a foothold in a specific market, might require a manual listings count or the use of crawlers.

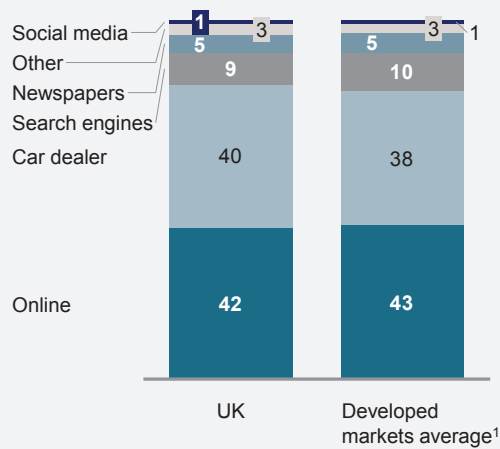
Monetization decision. Successful disruption of a horizontal-dominated market will also require careful consideration of the monetization trade-off. Revenue is ultimately important, but forfeiting monetization potential in certain market segments or verticals by making listings free of charge may attract more listers and thus create a more attractive offering for searchers.

Innovative product play. Horizontal players typically draw a large audience, but they often lack specialized product offerings. Players seeking differentiation in these markets can leverage their broad audience to either develop their own innovative offerings or partner with innovative offerings, making it possible to not only provide customers with the broadest, but also the most tailored offering in a specific category.

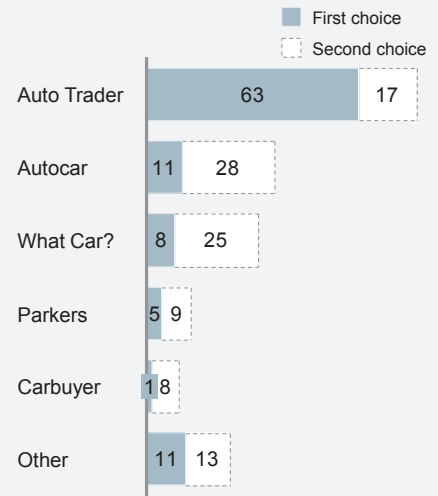
Exhibit 3

Auto Trader is the go-to site for cars in the UK's verticals-leaning online classified ad market

Starting point when looking for used cars
Share of respondents, percent



Preferred websites in the UK
Share of respondents, percent



¹ Includes France, Germany, Italy, Norway, Spain, the UK, and the US
Source: McKinsey survey of around 11,000 classified ad consumers, January 2015

Markets where vertical online models dominate

In contrast to the horizontal model's broad generalist play, some markets, like Germany and the United Kingdom, are dominated by vertical online classified ad business models, with no strong horizontal offering. McKinsey's survey shows that online classified businesses focused on a specific category, particularly in cars and real estate (Exhibit 3), are stronger in these markets. Although several specialized horizontal classified ad sites like Gumtree in the United Kingdom and eBay Kleinanzeigen in Germany have staked claims, none have achieved significant traction across all categories so far.

Gumtree, owned by eBay, was recognized, for instance, by 86 percent of the UK respondents in McKinsey's survey, but was only visited by 34 percent of those familiar with the brand in the previous three months. By comparison, Amazon had been visited by 90 percent of the UK respondents and eBay by 73 percent. Instead, these markets are dominated by highly specialized vertical players. In real estate, Rightmove was the first or second choice for 88 percent of the respondents in the UK and in Germany, ImmobilienScout24 was the first or second choice for 84 percent of German respondents.

Also, in contrast to France and Norway, consumers in markets without a dominant horizontal offering turned to generalist e-commerce sites like Amazon and eBay when looking for hard-to-find items. Without competition from a strong horizontal classified ad site, Amazon, for instance, has captured an estimated 25 percent of the German e-commerce market.

And, just as markets with strong horizontal players can still be shaken up, these vertical-leaning markets can be disrupted by new models. They are by no means secure and set for further monetization. New models with different consumer offerings can find success by entering the market with a different edge. One example is the startup RightHome, which takes parts of the value chain from real estate agents. These digital business models address the consumers who are currently looking on classified ad markets, but they also offer other services beyond content display.

Decision makers hoping to enter this space will also have to closely monitor the market and either integrate the most successful offerings or innovate the marketplace by providing more tailored, more user-friendly offerings in the category they serve. Providing a smartphone-based offering, for example, offering new services in the value chain, or even totally changing the value proposition are ways a player might build on its brand strength and sustain its attractiveness to its audience.

Opportunities in markets with no online leader or dominant digital model yet

The McKinsey survey identified very clear trends in some markets—either horizontal- or vertical-heavy models and clear classifieds leaders. However, a third category exists, and it is comprised of markets with no single player that has definitively pulled users from print to digital. Thus, these markets are not dominated by any particular online classifieds model.

Russia, Turkey, Brazil, and India are among the markets with relatively little overall online classifieds penetration. The survey results reflecting first choice and brand strength, for example, showed that Avito in Russia or Sahibinden in Turkey—both horizontal models—could become the leading online classified ad sites for those markets, taking positions similar to those held by FINN or Leboncoin. The US is also in this category and stands out from the others because it is one of few developed markets where the online classified ad model is off to a slow start. McKinsey's research indicates that only 36 percent of US consumers turn first to online markets for real estate, compared with an average 52 percent in other developed markets, and only 28 percent for used cars, compared with an average of 43 percent in developed markets. Print classified ads remain the clear favorite in the US, and this sluggishness stands in stark contrast to the country's powerhouses in other online categories, such as e-commerce, search engines, and social networks.

The brand awareness of online classifieds site craigslist is on par with Amazon and eBay in the US, but it has yet to convert awareness into site visits. McKinsey research suggests that only 46 percent of US consumers familiar with craigslist have visited it in the previous three months, compared with 82 percent for Amazon and 56 percent for eBay. But craigslist is probably also the reason why the market is still in its nascent stage of development. The site's strength of content has led it to a strong market position and the most relevant place for many consumers. On the other side, the company has barely invested in innovative product offerings or usability such that it has not gained a monopoly position in the consumers' minds. This is surprising, since most other leading global digital models like Amazon—the largest e-commerce site of the Western hemisphere—or the big social media giants all have their roots in their strong US market position. In classifieds, European sites are in the lead.

Without a clearly leading player, the fragmented specialty markets suggest there is scope for consolidation in the US market and, perhaps, still room for strong new entrants that offer innovative business models or enticing consumer interfaces. One potential attacker in this field certainly is eBay. In late 2014, eBay announced that it will make a new and very different kind of classified ad offering in the San Diego area. They launched a pilot of a new service from eBay, called Close5, which offers local, peer-to-peer sales. Another contender is Shpock, a company that offers a mobile-native marketplace and in which Norwegian classifieds giant Schibsted has invested. The massive penetration of smartphones in the United States—and also globally—leaves ample space for an inventive market entrant to battle for a share of the classified ad market.



Online classifieds as an industry is developing dynamically with “the archetypical digital business” operating at margins of more than 60 percent. Some markets are defined by generalist services, others are dominated by specialist platforms, and yet others struggle to establish a digital model that competes with traditional print ads. In each of these market categories, however, there is room for current players and new entrants. Just like Amazon’s Jeff Bezos put it, “Your margin is my opportunity.” Key to success to defend this—regardless of horizontal or vertical model—will be the careful monitoring of markets and making data-savvy decisions regarding monetization and innovation.

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