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Half of the marketing budget is wasted

By Jan Nyholm

According to a study from VisionEdge, 86% of marketing executives are dissatisfied with their marketing performance management. Even worse, many executives still agree with the famous, old statement 'I know that half of my advertising is wasted, I just do not know which half'. How can this be? In the age of scorecards, reengineering and performance measurement systems, why are there still such deficits in managing marketing efficiency?

The answer is very simple. Most managers still believe that the financial efficiency of marketing activities cannot be measured. This leads to a disturbing lack of financial accountability and a missed opportunity for optimisation. We observe that CEOs still get involved in conversations about the size of a new logo and the use of colours in a campaign rather than dealing with the facts and financials of marketing. When it comes to judging the effect, most firms focus on measurements like awareness, recall, likes and dislikes, page impressions and clicks. These measures might well indicate the reactions to a certain campaign, but for most businesses they say nothing about the efficiency of the respective activities; i.e. whether they generate additional revenue at acceptable costs.

This situation is not sustainable. As shareholders are exercising more and more power, the financial performance increasingly stands in the focus. And marketing now has to prove its contribution to it. The issues to be addressed are clearly defined. We argue that there are techniques and methodologies in place, which make them solvable and enable any firm to look at marketing as an investment like any other investment in order to maximise growth. To do so, we apply a 'Customer Investment Management©' approach that allows fact-based decision-making on key marketing questions. A large financial service provider that applied our approach cut the total marketing investment by 20% and achieved 30% better results.

Be blunt about marketing's role

In a tough competitive market, any firm must ensure that it allocates its resources in a way that enables it to compete successfully and grow profitably. This means, that all funds allocated to marketing must help the firm to 'sell more products to more people for more money more often', as former Coca-Cola CMO Sergio Zyman formulated it. This implies that any marketing investment must in its final effect attract a new customer, sell an extra product to an existing customer, up-sell a customer or ensure that a customer becomes loyal. Only by impacting these business drivers can marketing generate value. Therefore all marketing activities should be measured in these terms.

We observe that most firms do not do that, because they lack the specific knowledge of how to do it. And for good reasons. It is not taught at schools nor are there readily available and easy to apply methodologies at hand. This leads to the fact that most firms do not even set clear business-oriented goals for their marketing investments in the first place. When a European bank entered a major sport sponsorship costing $200 million, no sensible business objectives were set. They accepted the religion telling them to 'build the brand' to the degree that they lost sight of the business purpose.

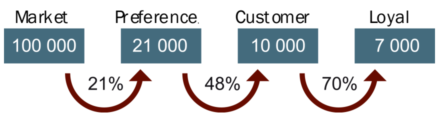
So what does it take for companies to regard marketing as a true business driver and to act accordingly? It requires the mastering of two key disciplines: Firstly, creating a deep understanding of customers and prospects and, secondly, being able to measure marketing effects in financial terms. Let's look at these two competences subsequently.

1. Using a deep customer understanding to drive the business

We have not come across a firm that did not have a lot of information about its customers. Neither have we met a sales person who would admit that he does not really know enough about his customers. However, we observe that often companies do not have the relevant set of information or that they lack the competence to combine the available pieces of data in a way that supports actionable decision-making. In particular, there is a lack of under-standing of customers' behaviour and of the real drivers behind the customers' decisions.

In order to excel in marketing and to set clear marketing priorities, companies have to understand and model the buying process (the 'Customer Decision Path') their customers are going through as well as the company's performance in every single step of this path. The 'Customer Decision Path' needs to reflect the nature of the business. Each firm must find out the relative importance of the parts of the process and determine which ones it will strive to influence in order to create value. An example of a 'Customer Decision Path' from the automobile sector is shown below.

'Customer Decision Path', Car industry



(Source: WATC Consulting AG, simplified illustration)

Measuring conversion rates between the different steps of the 'Customer Decision Path' delivers an indication of how well the firm performs in moving people through the buying process. Adding benchmarking against key competitors will allow a sensible discussion of opportunities and obstacles to growth. Judging the company's performance from an internal perspective only is likely to lead to wrong conclusions. E.g., the loyalty ratio of the car company shown above looks quite convincing. This might lead the company to focus its efforts on attracting new buyers. However, with competitive benchmarking they found out that key competitors actually had a much higher loyalty ratio. And sure enough, further analysis showed that they unnecessarily lost loyal customers to competitors.

So how can a firm ensure that it optimally exploits its full potential? It is necessary to understand what drives the customers' choice and thereby to answer questions such as: Why do people buy a certain car? What drives them to buy the same car again? And, probably even more importantly, why do some people end up not buying a car they have a preference for? Answering these questions is not trivial as it requires uncovering both – the conscious and the unconscious choice drivers. As traditional market research methodologies usually cannot capture that, we recommend a combination of qualitative methods (some of which come from psychology) with quantitative techniques to get reliable results that go beyond the obvious and expected.

This approach produces two superior in-sights. Firstly, it identifies the reasons why people move forward on their decision path. Secondly, it reveals where a company can best differentiate itself from its competitors.

This enhanced customer understanding allows a company to define its real market potential, to define actionable segments, to prioritise segments and to tailor messages. This results in an improvement of conversion rates and therefore in increased revenues. There is no substitute for knowing one's customers.

2. Measuring marketing effects in financial terms

Managing marketing budgets as investment portfolios and measuring their effects in financial terms is not very common. Instead some companies use competitive benchmarking, a percentage of revenues or historical data (e.g., last year's spend) as a basis for sizing their marketing budgets. But this approach does not focus on the firm's business objectives and is therefore not very sensible.

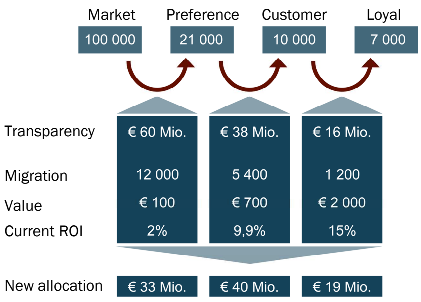
So how should a company really determine the right size of its marketing investments? How should it allocate these investments to various activities? And how can it optimise the financial impact?

To answer these questions, it is helpful to start by creating full marketing investment trans-parency. This can be achieved by allocating all marketing investments to specific business drivers. In practice, this means that each marketing activity is attributed to the specific steps in the 'Customer Decision Path' which it was meant to influence.

Going through this process, marketing is forced to define clear objectives for each single marketing activity. For the company, this process has two main benefits. Firstly, the company is forced to define objectives that have direct relevance for value creation and secondly it determines what needs to be measured for performance management. The result is full transparency on marketing goals and on the current budget allocation to achieve these goals.

To facilitate the process, we have developed an approach which consists of three basic steps. Step one uses a multitude of sources and tools to establish the sales impact of each marketing acti-vity along the 'Customer Decision Path'. With regard to the car example, this means establishing how many individuals have created a preference for the brand, how many have bought one of its models and how many have become loyal customers. Step two determines the life-time value of individuals along the 'Customer Decision Path'. Step three calculates the value creation of the marketing investment portfolio sets it into perspective with the invested capital and computes the return on investment of the major marketing activities.

Investment sizing and allocation



(Source: WATC Consulting AG, simplified illustration)

Understanding marketing's effect and calculating customer values allow for an optimal marketing investment sizing and allocation resulting in significant value creation.

When the efficiency of individual activities has been determined in financial terms, any company will be able to size its marketing budget and to allocate the marketing investments in the most efficient way. This delivers a strong basis for developing a new marketing plan where each euro is invested with clear visibility on the expected return.

It is time for change

The times in which decisions on huge sponsorships were taken based on personal preferences of some top executives or large advertising campaigns were launched merely to 'build the brand' have gone. Marketing can be a tremendous value contributor to any company if a few basic rules are followed:

– The CEO must drive the marketing agenda and ensure that marketing in-vestments are treated like any other investment within the company.
– The head of marketing should act like a business head with the bottom-line in mind. This should earn him a seat on the board.
– Marketing planning and the CFO's budgeting process must be closer aligned. The CFO and CMO must speak the same language. This will enable a factual discussion about budget setting
– The effectiveness of all marketing activities must be measured. It is important to have a solid and consistent methodology in place which pro-vides a financial link to the relevant business drivers.

Companies will find that by undertaking a reorientation of marketing based on the ideas described here, the organisation will become more customer-centric, all the way down to execution. The improved understanding of customers will increase success rates in acquiring and retaining customers, which will result in increased revenue. The efficiency measurement enables fact- based decision- making and will lead to potential cost savings and certainly a substantial improvement in ROI of up to 30%.

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