MARKETING ACCOUNTABILITY

How to measure marketing effectiveness

Malcolm McDonald
and Peter Mouncey

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London and Philadelphia

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Introduction

This book is a major breakthrough for marketing and is a must-read for all marketers who are depressed by the very low regard in which marketing is held. The 2007 Deloitte report, *Marketing in 3D*, placed the discipline at the very bottom of the pile in terms of corporate reputation. Here are just three quotations from the report:

> The historic rift between marketers and the finance department, caused by marketing's reluctance to be accountable for what they do, is as marked as ever.
>
> Tense relations between CFOs and Marketers are dividing boardrooms over the value of marketing. One in three CFOs said they did not believe marketing to be crucial in determining strategy.
>
> Marketers have constantly hidden behind a fog of measures that are based purely on tactical marketing activity, rather than solid financial metrics that are relevant to the City.
>
> *(Deloitte, 2007)*

Yes, the principal reason that marketing as a discipline is at an all-time low is because of its lack of accountability to the directors for the often enormous amounts of money invested by marketers. One US academic, David Stewart (2008), estimates that companies devote no less than 20–25 per cent of their expenditure to marketing. However, despite the high proportion of funds dedicated to marketing, McGovern *et al* reported in the *Harvard Business Review* in November 2004 that: 'In a survey of large US companies, more than one-third reported that their boards spent less than 10 per cent of their time discussing marketing or customer related

activities.' The authors argue that 'in too many companies marketing is poorly linked to strategy' and 'marketing managers are rarely held accountable for ROI or expected to explain how what they do supports corporate strategy'. They claim that: 'Misguided marketing strategies have destroyed more shareholder value – and probably more careers – than shoddy accounting or shady fiscal practices have.'

Way back in 2004, research at Cranfield University School of Management found that marketers were considered 'unaccountable, expensive and slippery' by their senior non-marketing colleagues.

In the United States, both the Marketing Science Institute (MSI) and the Association of National Advertisers (ANA) have given marketing accountability top billing. As the ANA task force on accountability observed: 'The view from the corner office sees the marketing function as the last grape with any juice left unsqueezed.' The extent to which marketers have the skills to respond to this pressure is underlined by a leading British CEO: 'Marketers must be more than functional specialists to win over Chief Executives. Marketers fail to reach Board level because they are not fluent in the language of finance. Success requires a new set of skills' (Sir Roy Gardner, CEO, Centrica, 2004). As part of their crusade on this issue, the MSI sponsored a special section of the leading peer-reviewed journal in the field of marketing, the *Journal of Marketing* (October 2004), which was devoted to 'Linking marketing to financial performance and firm value'.

In the UK, Les Binet and Peter Field (2007), in their in-depth analysis covering over 10 years of submissions to the Institute of Practitioners of Advertising (IPA) awards, conclude that marketers have a poor grasp of business finance. The authors state that marketers tend to focus more on intermediate measures, such as awareness and attitudes, rather than on business or behavioural measures. Even when marketers do use business measures, Binet and Field believe they concentrate on the wrong ones – sales rather than market share, volume rather than value, and return on investment rather than profit. The authors state that there are therefore many cases where the payback measurement methods used as evidence to prove the effectiveness of marketing are fundamentally flawed and that there are few entries where this is measured properly. As these are all entries to a prestigious competition, the overall situation may be infinitely worse.

Finally, the findings from a literature review of published papers conducted by one of the authors of this book for the Cranfield University Marketing Measurement and Accountability Forum suggested that many of the models covered were theoretical with little or no practical evidence from real-world case studies as evidence to support their efficacy: 'Overall, there appears to be a dearth of either tested approaches or evidence that suggested models can be applied in the real world.' The author concluded that:

> Marketers need to develop a much better understanding of how shareholder value is created. Without this knowledge, and more effective communications between marketing and finance, traditional low-level, short-term performance measures will continue to prevail and the strategic impact of marketing will

> continue to be understated. The current annual battle endured by many marketers to defend their budgets will continue to be lost and marketing will continue to punch below its weight. This situation perhaps needs to be addressed within postgraduate level marketing education programmes, and developing effective links between professional bodies in the finance and marketing communities.

The reason we undertook, over a seven-year period, a painstaking process of research into global best practice in the domain of marketing accountability was to do something about this major problem, and we are delighted to announce that we have succeeded. This book contains the breakthrough findings of our research, and we have tried – and we think succeeded – to explain these methodologies in a 'how to do it' book, not a dense theoretical treatise.

'I get paid to make the owners of the company increasingly wealthy with each passing day. Everything else is just fluff.' So said Roberto Goizueta, a former chief executive of Coca-Cola. This, however, is becoming increasingly difficult as under-siege CEOs are faced with maturing markets, globalization and growing customer power and, as Sean Silverthorne of Harvard Business School said in 2007: 'The key challenge in aligning marketing activities with corporate strategy is to develop a set of metrics to be used by top executives and the board that measure the impact of marketing activities against the goals of the corporation.'

This book goes some considerable way towards providing a solution to this challenge and will empower marketing executives to justify their actions to both CEOs and chief financial officers.

We have enjoyed enormously working with many of the best companies in the world to produce and test the methodologies set out in this book.

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1

It's tough at the top – CEOs are finally demanding accountability for marketing expenditure

Summary

Intangible assets are accounting for an increasing percentage of corporate value – over 85 per cent in the United States – yet there are few formal processes for treating them as an investment and measuring financial returns on them. Nevertheless, investment communities around the world take account of their value and assess the risks associated with future strategies using those assets.

Meanwhile, profit and loss accounts in the main continue to emphasize costs, whilst failing to expand on sources of revenue. This chapter goes into some considerable detail about why managerial forecasts and budgets are in the main backward-looking, create managerial stress and force managers to focus on the budgets rather than on customers. Evidence is provided of the failure of such pressure. Finally, the chapter emphasizes that a robust strategy for what is sold and to whom and why customers should buy is the prerequisite for long-term commercial success.

1.1 The growing importance of intangible assets

In 2006, Procter & Gamble paid £31 billion for Gillette, of which only £4 billion was accounted for by tangible assets, as Table 1.1 shows.

Table 1.1 Intangibles

Gillette brand	£ 4.0 billion
Duracell brand	£ 2.5 billion
Oral B	£ 2.0 billion
Braun	£ 1.5 billion
Retail and supplier network	£10.0 billion
Gillette innovative capability	£ 7.0 billion
Total	**£27.0 billion**

Source: Haigh (2005)

Recent estimates of companies in the United States and in the UK show that over 80 per cent of the value of companies resides in intangibles. Table 1.2 and Figure 1.1 show some of this research. Figure 1.2 shows a typical breakdown of intangibles, whilst Table 1.1 is an example of the breakdown of intangibles in a recent acquisition. Yet very little is known about intangibles by shareholders and the investment community. Traditional accounting methods are biased towards tangible assets, for this is where the wealth used to reside.

Table 1.2 Invisible business: some research findings

- Brand Finance analysis of top 25 stock markets – $31.6 trillion (99% of global market value)
- 62% of global market value is intangible – $19.5 trillion
- Technology is the most intangible sector (91%)
- The technology sector in the United States is 98% intangible

Source: Brand Finance (2005)

Generalizing from this it can be seen from Figure 1.3 what typically appears in a balance sheet. However, when a predator bids for such a company, it is often forced to pay substantially more than the £100 million shown in this balance sheet.

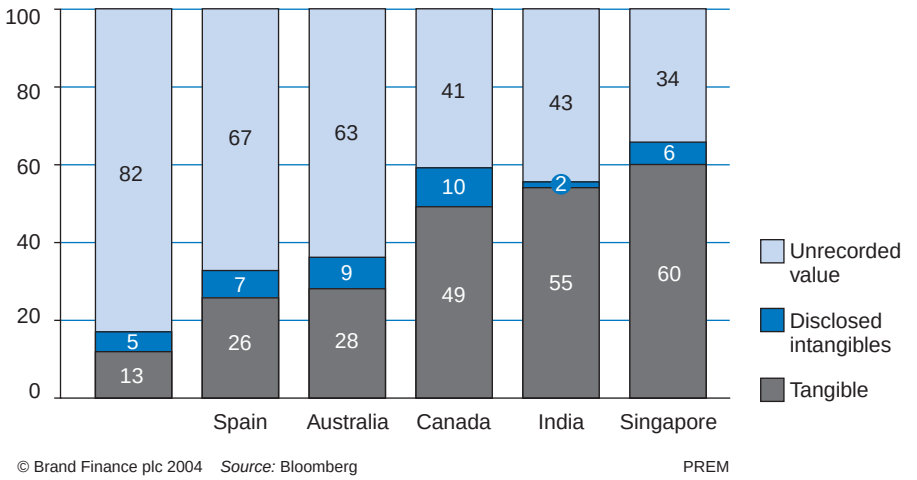

Figure 1.1 Asset split across selected economies

Brands are estimated to represent at least 20% of the intangible value of businesses on the major world stock markets. Brands combine with other tangible and intangible assets to create value

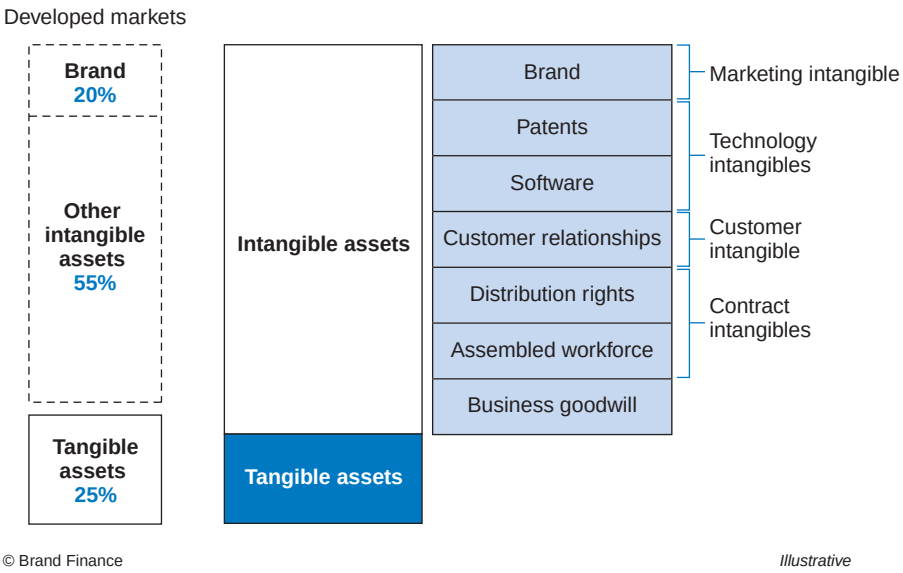

Figure 1.2 Brands are key intangibles in most businesses

In this hypothetical example, it can be seen from Figure 1.4 that in this case it is £900 million – £800 million more than is shown in the balance sheet in Figure 1.3.

The problem is that it leaves a balance sheet that doesn't balance, so this is corrected in Figure 1.5, which shows a balancing figure of £800 million.

This leads on naturally to the next point.

2.8.4 Understand competitors

Guideline 4 is merely an extension of the marketing audit. Suffice it to say that, if any organization, big or small, doesn't know as much about its close competitors as it knows about itself, it should not be surprised if it fails to stay ahead.

Again, if anyone is unsure how to go about this, use a consultant initially, although our advice is to use a modicum of common sense and sweet reasonableness in this process, stopping short, of course, at industrial espionage!

Closely connected with this is a final piece of information (in the box below) in this process we have referred to as a marketing audit.

Understand competitors

- Direct competitors.
- Potential competitors.
- Substitute products.
- Forward integration by suppliers.
- Backward integration by customers.
- Competitors' profitability.
- Competitors' strengths and weaknesses.

Develop a structured competitor monitoring process. Include the results in the marketing audit.

2.8.5 Understand your own strengths and weaknesses

Guideline 5 sets out potential sources of differentiation for your own organization. It represents a fairly comprehensive audit of the asset bases. Along with the other two sections of the marketing audit (the environment and competitors), it is important to make a written summary of your conclusions from all of this.

If you cannot summarize on a couple of sheets of paper the sources of your own competitive advantage, it has not been done properly. If this is the case, the chances are that you are relying on luck. Alas, luck has a habit of being somewhat fickle!

Strengths and weaknesses

Carry out a formal position audit of your own product/market position in each segment in which you compete. In particular, understand by segment:

- what the qualifying features and benefits are;
- what the differential features and benefits are;
- how relatively important each of these is;
- how well your product or service performs against your competitors' products or services on each of these requirements.

2.8.6 Understand market segmentation

Guideline 6 looks somewhat technical and esoteric, at first sight. Nonetheless, market segmentation is one of the key sources of commercial success and needs to be taken seriously by all organizations, as the days of the easy marketability of products and services have long since disappeared for all but a lucky few.

The secret of success, of course, is to change the offer in accordance with changing needs and not to offer exactly the same product or service to everyone – the most frequent, production-oriented mistake of large organizations.

Closely connected with this is the next point.

Market segmentation

- Not all customers in a broadly defined market have the same needs.
- Positioning is easy. Market segmentation is difficult. Positioning problems stem from poor segmentation.
- Select a segment and serve it. Do not straddle segments and sit between them:
  - Understand how your market works (market structure).
  - List what is bought (including where, when, how, applications).
  - List who buys (demographics, psychographics).
  - List why they buy (needs, benefits sought).
  - Search for groups with similar needs.

2.8.7 Understand the dynamics of product/market evolution

Whilst at first sight Guideline 7 looks as if it applies principally to large companies, few will need reminding of the short-lived nature of many retailing concepts, such as the boutiques of the late 1980s. Those who clung doggedly on to a concept that had had its day lived to regret it.

2.8.8 Understand your portfolio of products and markets

Guideline 8 suggests plotting either products/services or markets (or, in some cases, customers) on a vertical axis in order of the potential of each for you to achieve your personal and commercial objectives as, clearly, they can't all be equal. Organizations will obviously have greater or lesser strengths in serving each of these 'markets'. For each location on the four-box matrix in Figure 2.10, put a circle, the size of which represents current sales. This will give a reasonably accurate 'picture' of your business at a glance and will indicate whether or not it is a well-balanced portfolio. Too much in any one box is dangerous.

Understand your portfolio of products and markets

You cannot be all things to all people. A deep understanding of portfolio analysis will enable you to set appropriate objectives and allocate resources effectively. Portfolio logic arrays competitive position against market attractiveness in a matrix form (Figure 2.10):

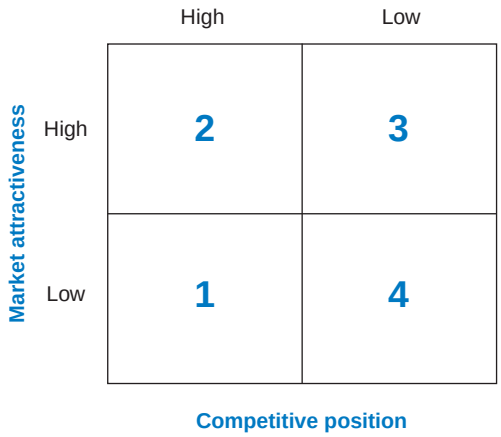

Figure 2.10 The McDonald Portfolio Matrix

- *Box 1:* Maintain and manage for sustained earnings.
- *Box 2:* Invest and build for growth.
- *Box 3:* Selectively invest.
- *Box 4:* Manage for cash.

Follow the guidelines given and there is no reason why any firm should not have a healthy and growing business.

2.8.9 Set clear strategic priorities and stick to them

Guideline 9 suggests writing down the results of your earlier endeavours in summary form (a marketing/business plan).

Set clear strategic priorities

- Focus your best resources on the best opportunities for achieving continuous growth in sales and profits.
- This means having a written strategic marketing plan for three years containing:
  - a mission statement;
  - a financial summary;
  - a market overview;
  - SWOT analyses on key segments;
  - a portfolio summary;
  - assumptions;
  - marketing objectives and strategies;
  - a budget.
- This strategic plan can then be converted into a detailed one-year plan.
- To do this, an agreed marketing planning process will be necessary.
- Focus on key performance indicators with an unrelenting discipline.

Whilst it is not our intention to stifle creativity by suggesting that any firm should get into a bureaucratic form of planning, it remains a fact that those individuals and organizations that can make explicit their intended sources of revenue and profits tend to thrive and prosper in the long term. This implies something more sophisticated than forecasts and budgets. Commercial history has demonstrated that any fool can spell out the financial results they wish to achieve. But it takes intellect to spell out how they are to be achieved. This implies setting clear strategic priorities and sticking to them.

2.8.10 Understand customer orientation

Guideline 10 will be familiar to all successful firms. BS 5750, ISO 9001 and the like, whilst useful for those with operations such as production processes, have little to do with real quality, which, of course, can be seen only through the eyes of the customer. It is obvious that making anything perfectly that no one buys is somewhat of a pointless exercise.

Understand customer orientation

- Develop customer orientation in all functions. Ensure that every function understands that it is there to serve the customer and not its own narrow functional interests.
- This must be driven from the board downwards.
- Where possible, organize in cross-functional teams around customer groups and core processes.
- Make customers the arbiter of quality.

Whilst it is, perhaps, easier for small companies than for large companies to check out customer satisfaction, this should nonetheless be done continuously, for it is clearly the only real arbiter of quality.

2.8.11 Be professional

Guideline 11 sets out some of the marketing skills essential to continuous success. Professional management skills, particularly in marketing, are becoming the hallmark of commercial success in the new millennium. There are countless professional development skills courses available to all firms. Alas, too many directors consider themselves too busy to attend, which is extremely short-sighted. Entrepreneurial skills, combined with hard-edged management skills, will see any firm through in the new world of the twenty-first century.

Be professional

Particularly in marketing, it is essential to have professional marketing skills, which implies formal training in the underlying concepts, tools and techniques of marketing. In particular, the following are core:

- market research;
- gap analysis;
- market segmentation/positioning;
- product life cycle analysis;
- portfolio management;
- the four Ps:
  - product management;
  - pricing;
  - place (customer service, channel management);
  - promotion (selling, sales force management, advertising, sales promotion).

2.8.12 Give leadership

Guideline 12 sets out the final factor for success.

Give leadership

- Do not let doom and gloom pervade your thinking.
- The hostile environment offers many opportunities for companies with toughness and insight.
- Lead your team strongly.
- Do not accept poor performance in the most critical positions.

Charismatic leadership, however, without the 11 other pillars of success will be to no avail. Few will need reminding of the charisma of Maxwell, Halpern, Saunders and countless others. Charisma, however, without something to sell that the market values, will ultimately be pointless. It is, nonetheless, still an important ingredient in success.

2.9 Conclusions

Lest readers should think that the 12 factors for success are a figment of the imagination, there is much recent research to suggest otherwise. The four ingredients listed in Figure 2.11 are common to all commercially successful organizations, irrespective of their national origin:

1. From this it can be seen that the core product or service on offer has to be excellent.
2. Operations have to be efficient and, preferably, state-of-the-art.

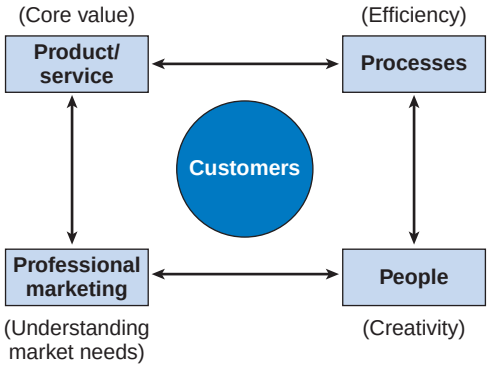

Figure 2.11 The four abiding characteristics of successful organizations

3. The research stresses the need for creativity in leadership and personnel, something frequently discouraged by excessive bureaucracy in large organizations.
4. Excellent companies have professional marketing. This means that the organization continuously monitors the environment, the market, competitors and its own performance against customer-driven standards.

Having taken a quick 'Cook's tour' through strategic and operational marketing planning, it will be made clear later in this book where and how marketing accountability fits in.

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3

A three-level marketing accountability framework

Summary

This chapter examines marketing investment appraised techniques and then introduces a three-level model for marketing accountability.

The first level spells out how to assess whether marketing strategies create or destroy shareholder value using a technique developed by the Cranfield School of Management Marketing Value Added Research Club. The second-level model – also emanating from the Cranfield Research Club – links all expenditure relating to products, markets and customers to corporate revenue and profit objectives and clearly demonstrates what should be measured, why, when, and how frequently. Finally, the third-level accountability framework relates to promotional expenditure.

3.1 Introduction

The ultimate test of marketing investment, and indeed any investment, is whether it creates value for shareholders. But few marketing investments are evaluated from this perspective, and many would argue that it is almost impossible to link financial results to any specific marketing activity.

But increasingly boards of directors and city analysts the world over are dissatisfied with this lack of accountability for what are, very often, huge budgets. Cranfield School of Management has been addressing this problem through its Marketing Value Added Research Club, formed with a number of blue-chip companies. The

club set out to create and test a new framework, which shows how marketing systematically contributes to shareholder value, and how its contribution can be measured in an objective and comparable way.

There is an urgent need for such a framework. Not only does marketing need it, to answer the widespread accusations of poor performance, but corporate and financial strategists need it too, to understand how to link marketing activities to the wider corporate agenda. All too often marketing objectives and strategies are not aligned with the organization's overall plans to increase shareholder value.

The purpose of this chapter is to set out the logic of this framework, which is underpinned by the work of two Cranfield PhDs (H N Wilson, 1996, and B D Smith, 2003).

The chapter starts with a brief justification of the need for a wholly new approach to measuring the effectiveness of marketing. It then proceeds to the second level in the accountability framework developed in the Cranfield Research Club.

3.2 A three-level marketing accountability framework

3.2.1 What counts as marketing expenditure?

Historically, marketing expenditure has tended to escape rigorous performance appraisal for a number of reasons. Firstly, there has been real confusion as to the true scope and nature of marketing investments. Too often, marketing expenditure has been assumed to be only the budgets put together by the marketing function and, as such, a (major) cost to be controlled rather than a potential driver of value. Secondly, the causal relationship between expenditure and results has been regarded as too difficult to pin down to any useful level of precision.

Now, as explained in Chapter 1, because of the demands of increasingly discerning customers and greater competition, marketing investments and marketing processes are under scrutiny as never before. From the process point of view, as a result of insights from management concepts such as the quality movement and re-engineering, marketing is now much more commonly seen as a cross-functional responsibility of the entire organization rather than just the marketing department's problem.

Howard Morganis, past chairman of Procter & Gamble, said, 'There is no such thing as a marketing skill by itself. For a company to be good at marketing, it must be good at everything else from R&D to manufacturing, from quality controls to financial controls.' Hugh Davidson, in *Even More Offensive Marketing* (1997), comments, 'Marketing is an approach to business rather than a specialist discipline. It is no more the exclusive responsibility of the marketing department than profitability is the sole charge of the finance department.'

But there is also a growing awareness that, because of this wider interpretation of marketing, nearly all budgets within the company could be regarded as marketing

investments in one way or another. This is especially the case with IT budgets. The exponential increase in computing power has made it possible to track customer perceptions and behaviours on a far greater scale and with far greater precision than previously. When used correctly, these databases and analytical tools can shed a much greater light on what really happens inside the 'black box'. However, the sums involved in acquiring such technologies are forcing even the most slapdash of companies to apply more rigorous appraisal techniques to their investments in this area.

This wider understanding of what 'marketing' is really all about has had a number of consequences. Firstly, the classic textbook treatment of strategic issues in marketing has finally caught up with reality. Topics such as market and customer segmentation, product and brand development, databases and customer service and support are now regularly discussed at board level, instead of being left to operational managers or obscure research specialists.

CEOs and MDs are increasingly accepting that they must take on the role of chief marketing officer if they want to create truly customer-led organizations. Sir Clive Thompson commented: 'I am convinced that corporate and marketing strategy are more or less the same things. The chief executive has to be the chief marketer. If you delegate that responsibility, you are not doing your job.'

Secondly, because of their 'new' mission-critical status, marketing investments are attracting the serious attention of finance professionals. As part of a wider revolution in thinking about what kind of corporate assets are important in today's business environment, intangibles such as knowledge about customers and markets, or the power of brands, have assumed a new importance. Evidence for this is provided in Chapter 1. The race is on to find robust methods of quantifying and evaluating such assets for the benefit of corporate managements and the wider investment community.

Unfortunately, this new focus on the importance of marketing has not improved the profile of marketing professionals. Instead, the spotlight has merely highlighted their weaknesses and shortcomings. After one 1997 survey on the perceived status of the profession, John Stubbs, CEO of the UK Marketing Council, was forced to comment:

> I was taken aback by just how little reputation marketing actually has among other functions… marketing and marketers are not respected by the people in their organizations for their contributions to business strategy, results or internal communication. We often do not know what or who is good or bad at marketing; our measurements are not seen as credible; our highest qualifications are not seen to have compatible status with other professions.

A survey at Cranfield during a two-year period revealed that marketers are seen as 'slippery, expensive, unreliable and unaccountable'.

A study by Synesis in 2000 confirmed this perception of the marketing function. Synesis found 'a self-confident profession with high self-esteem', which unfortu-

nately had 'some way to go to convince [its colleagues] that marketing is as effective as it could be'.

3.2.2 What does 'value added' really mean?

The term 'value added' is fast becoming the new mantra for the early-21st-century business literature, and is often used quite loosely to indicate a business concept that is intended to exceed either customer or investor expectations, or both. However, from the point of view of this chapter, it is important to realize that the term has its origin in a number of different management ideas, and is used in very specific ways by different sets of authors. Most of the ideas come from the United States, and originated in business school and consultancy research in the mid-1980s.

3.2.3 Value chain analysis

Firstly, there is Michael Porter's well-known concept of value chain analysis. Porter's concept of value added is an incremental one; he focuses on how successive activities change the value of goods and services as they pass through various stages of a value chain:

> Value chain analysis is used to identify potential sources of economic advantage. The analysis disaggregates a firm into its major activities in order to understand the behaviour of costs and the existing and potential sources of differentiation. It determines how the firm's own value chain interacts with the value chains of suppliers, customers and competitors. Companies gain competitive advantage by performing some or all of these activities at lower cost or with greater differentiation than competitors.
>
> *(Porter, 1985)*

3.2.4 Shareholder value added (SVA)

Secondly, there is Alfred Rappaport's equally well-known research on shareholder value added. Rappaport's concept of value added focuses less on processes than Porter's, and acts more as a final gateway in decision making, although it can be used at multiple levels within a firm. SVA is described as:

> The process of analysing how decisions affect the net present value of cash to shareholders. The analysis measures a company's ability to earn more than its total cost of capital… Within business units, SVA measures the value the unit has created by analysing cash flows over time. At the corporate level, SVA provides a framework for evaluating options for improving shareholder value by determining the tradeoffs between reinvesting in existing businesses, investing in new businesses and returning cash to stockholders.
>
> *(Rappaport, [1986] 1998)*

There are a number of different ways of measuring shareholder value added, one of which, market value added (MVA), needs further explanation. Market value added is a measure, first proposed by consultants Stern Stewart in 1991, which compares the total shareholder capital of a company (including retained earnings) with the current market value of the company (capitalization and debt). When one is deducted from the other, a positive result means value has been added, and a negative result means investors have lost out. Within the literature, there is much discussion of the merits of this measure as against those of another approach proposed by Stern Stewart – economic value added (EVA).

However, from the point of view of marketing value added, Walters and Halliday (1997) usefully sum up the discussion thus: 'As aggregate measures and as relative performance indicators they have much to offer… [but] how can the manager responsible for developing and/or implementing growth objectives [use them] to identify and select from alternative [strategic] options?'

Market value added is one of a number of tools that analysts and the capital markets use to assess the value of a company. Marketing value added as a research topic focuses more directly on the processes of creating that value through effective marketing investments.

3.2.5 Customer value

A third way of looking at value added is the customer's perception of value. Unfortunately, despite exhaustive research by academics and practitioners around the world, this elusive concept has proved almost impossible to pin down: 'What constitutes [customer] value – even in a single product category – appears to be highly personal and idiosyncratic', concludes Zeithaml (1988), for instance. Nevertheless, the individual customer's perception of the extra value represented by different products and services cannot be easily dismissed: in the guise of measures such as customer satisfaction and customer loyalty, it is known to be the essence of brand success, and the whole basis of a new movement known as 'relationship marketing'.

3.2.6 Accounting value

Finally, there is the accountant's definition of value added: 'value added = sales revenue − purchases and services'. Effectively, this is a snapshot picture from the annual accounts of how the revenue from a sales period has been distributed, and how much is left over for reinvestment after meeting all costs, including shareholder dividends. Although this figure will say something about the past viability of a business, in itself it does not provide a guide to future prospects.

One reason that the term 'value added' has come to be used rather carelessly is that all these concepts of value, although different, are not mutually exclusive. Porter's value chain analysis is one of several extremely useful techniques for identifying potential new competitive market strategies. Rappaport's SVA approach can

be seen as a powerful tool that enables managers to cost out the long-term financial implications of pursuing one or other of the competitive strategies that have been identified. Customer perceptions are clearly a major driver (or destroyer) of annual audited accounting value in all companies, whatever strategy is pursued.

However, most companies today accept that value added, as defined by their annual accounts, is really only a record of what they achieved in the past, and that financial targets in themselves are insufficient as business objectives. Many companies are now convinced that focusing on more intangible measures of value added such as brand equity, customer loyalty or customer satisfaction is the new route to achieving financial results.

Unfortunately, research has found that there is no neat, causal link between offering additional customer value and achieving value added on a balance sheet, ie good ratings from customers about perceived value do not necessarily lead to financial success. Nor do financially successful companies necessarily offer products and services that customers perceive as offering better value than competitors.

In order to explain the link that does exist between customer-orientated strategies and financial results, a far more rigorous approach to forecasting costs and revenues is required than is usual in marketing planning, coupled with a longer-term perspective on the payback period than is possible on an annual balance sheet. This cash-driven perspective is the basis of the SVA approach, and can be used in conjunction with any marketing-strategy formulation process.

However, despite the SVA approach's apparent compatibility with existing planning systems, it is important to stress that adherents of the approach believe that, after all the calculations have been made about the impact of different strategic choices, the final decision about which strategy to pursue should be in favour of the one that generates the most value (cash) for shareholders. This point of view adds a further dimension to the strategic debate, and is by no means universally accepted: there is a vigorous and ongoing debate in the literature as to whether increasing shareholder value should be the ultimate objective of a corporation.

Despite these arguments, there is no denying that, during the last 15 years, SVA (or variants on the technique) has become the single most dominating corporate valuation perspective in developed Western economies. Its popularity tends to be limited to the boardroom and the stock exchanges, however. Several surveys (eg CSF Consulting in 2000 and KPMG in 1999) have found that less than 30 per cent of companies were pushing SVA-based management techniques down to an operational level, because of difficulties in translating cash targets into practical, day-to-day management objectives. This is a pity because, apart from its widespread use at corporate level, the SVA approach particularly merits extensive attention of researchers interested in putting a value on marketing, as it allows marketing investments (or indeed any investments) to be valued over a much longer period of time than the usual one-year budget cycle.

Although common sense might argue that developing strong product or service offerings and building up a loyal, satisfied customer base will usually require a

series of one- to two-year investment plans in any business, nevertheless such is the universal distrust of marketing strategies and forecasts that it is common practice in most companies to write off marketing as a cost within each year's budget. It is rare for such expenditure to be treated as an investment that will deliver results over a number of years, but research shows that companies that are able to do this create a lasting competitive edge.

Meanwhile, as stated earlier, research into marketing accountability continues apace at Cranfield; a three-level model has been developed and tested, and it is to this model that we now turn.

3.3 Three distinct levels for measuring marketing effectiveness

When one of the authors was marketing director of a fast-moving consumer goods (FMCG) company 30 years ago, there were many well-tried-and-tested models for measuring the effectiveness of marketing promotional expenditure. Indeed, some of these were quite sophisticated and included mathematical models for promotional campaigns, for advertising threshold and wear-out levels, and the like.

Indeed, it would be surprising if marketing as a discipline did not have its own quantitative models for the massive expenditure of FMCG companies. Over time, these models have been transferred to business-to-business and service companies, with the result that, today, any organizations spending substantial sums of shareholders' money on promotion should be ashamed of themselves if those responsible could not account for the effectiveness of such expenditure.

Nonetheless, with the advent of different promotional methods and channels, combined with an empowered and more sophisticated consumer, the problems of measuring promotional effectiveness have increased considerably. Consequently, this remains one of the major challenges facing the marketing community today and, as mentioned above, the research and practice of specialists at Cranfield School of Management continue apace.

But, at this level, accountability can be measured only in terms of the kinds of effects that promotional expenditure can achieve, such as awareness, or attitude change, both of which can be measured quantitatively.

But to assert that such expenditure can be measured directly in terms of sales or profits is intellectually indefensible, when there are so many other variables that affect sales, such as product efficacy, packaging, price, the sales force, competitors and countless other variables that, like advertising, have an intermediate impact on sales and profits. Again, however, there clearly is a cause-and-effect link; otherwise such expenditure would be pointless. This issue is addressed later in this chapter.

So the problem with marketing accountability has never been with how to measure the effectiveness of promotional expenditure, for this we have had for many years. No, the problem occurs because marketing isn't just a promotional activity. As explained in detail in Chapter 2, in world-class organizations where the

customer is at the centre of the business model, marketing as a discipline is responsible for defining and understanding markets, for segmenting these markets, for developing value propositions to meet the researched needs of the customers in the segments, for getting buy-in from all those in the organization responsible for delivering this value, for playing their own part in delivering this value, and for monitoring whether the promised value is being delivered.

Indeed, this definition of marketing as a function for strategy development as well as for tactical sales delivery, when represented as a map (see Figure 3.1), can be used to clarify the whole problem of how to measure marketing effectiveness. From this map, it can be seen that there are three levels of measurement, or metrics.

3.3.1 Level 1: shareholder value added

Level 1 is the most vital of all three, because this is what determines whether or not the marketing strategies for the longer term (usually three to five years) destroy or create shareholder value added. It is justified to use the strategic plan for assessing whether shareholder value is being created or destroyed because, as Sean Kelly (2005) agrees: 'The customer is simply the fulcrum of the business and everything from production to supply chain, to finance, risk management, personnel management and product development, all adapt to and converge on the business value proposition that is projected to the customer.'

Thus, corporate assets and their associated competences are relevant only if customer markets value them sufficiently highly for them to lead to sustainable competitive advantage, or shareholder value added. This is our justification for

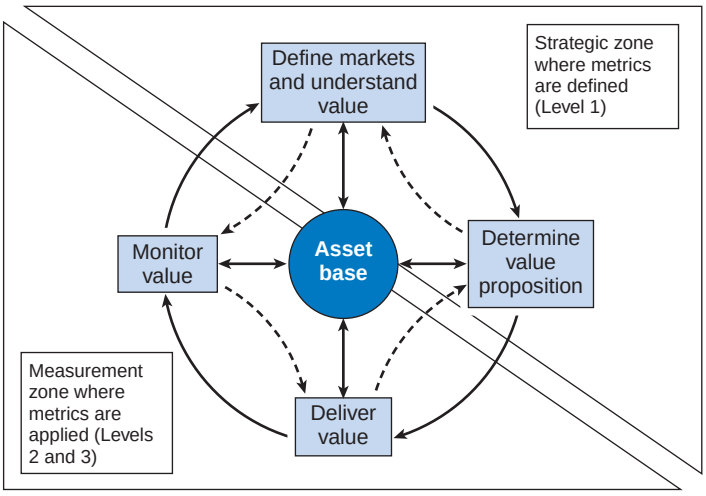


Figure 3.1 Map of the marketing domain and the three-level accountability framework

evaluating the strategic plan for what is to be sold, to whom and with what projected effect on profits as a route to establishing whether shareholder value will be created or destroyed.

A company's share price, the shareholder value created and the cost of capital are all heavily influenced by one factor: risk. Investors constantly seek to estimate the likelihood of a business plan delivering its promises, whilst the boards try to demonstrate the strength of their strategy. Research since 2002 from Cranfield School of Management into Marketing Due Diligence and shareholder value added provides insight and tools to do both.

How much is a company really worth? We spelled out in Chapter 1 the huge discrepancy between the tangible assets and the share price; there are innumerable tools that try to estimate the true value of intangibles and goodwill. However, these mostly come from a cost-accounting perspective. They try to estimate the cost of re-creating the brand, intellectual property or whatever is the basis of intangible assets. Our research into companies that succeed and fail suggests that approach is flawed, because what matters is not the assets owned but how they are used. We need to get back to the basics of what determines company value.

We should never be too simplistic about business, but some things are fundamentally simple. We believe that a company's job is to create shareholder value, and the share price reflects how well the investment community thinks that is being done. Whether or not shareholder value is created depends on creating profits greater than investors might get elsewhere at the same level of risk. The business plan makes promises about profits, which investors then discount against their estimate of the chance a company will deliver it. So it all comes down to that. A company says it will achieve $1 billion; investors and analysts think it is more likely to be $0.8 billion. The capital markets revolve around perceptions of risk. What boards and investors both need therefore is a strategic management process that gives a rigorous assessment of risk and uses that to assess and improve shareholder value creation. Just such a process has emerged from many years of research at Cranfield, a process we have called, appropriately, Marketing Due Diligence.

There is a whole chapter dedicated to explaining this process (Chapter 4), so we will provide only a brief summary here.

3.3.1.1 Where does risk come from?

Marketing Due Diligence begins by looking for the risk associated with a company's strategy. Evaluation of thousands of business plans suggests that the many different ways that companies fail to keep their promises can be grouped into three categories:

1. The market wasn't as big as they thought.
2. They didn't get the market share they hoped for.
3. They didn't get the profit they hoped for.

Of course, a business can fail by any of these routes or a combination of them. The risk inherent in a plan is the aggregate of these three categories, which we have called, respectively, market risk, strategy risk and implementation risk. The challenge is to assess accurately these risks and their implications for shareholder value creation.

Our research found that most estimates of business risk were unreliable because they grouped lots of different sources of risk under one heading. Since each source of risk is influenced by many different factors, this high-level approach to assessing business risk is too simplistic and inherently inaccurate. A better approach is to subdivide business risk into as many sources as practically possible, estimate those separately and then recombine them. This has two advantages. Firstly, each risk factor is 'cleaner', in that its causes can be assessed more accurately. Secondly, minor errors in each of the estimations cancel each other out. The result is a much better estimate of overall risk.

3.3.1.2 How risky is a business?

Marketing Due Diligence makes an initial improvement over high-level risk estimates by assessing market, strategy and implementation risk separately. However, even those three categories are not sufficiently detailed. We need to understand the components of each, which have to be teased out by careful comparison of successful and unsuccessful strategies. Our research indicated that each of the three risk sources could be subdivided further into five risk factors, making 15 in all. These are summarized in Table 3.1.

Armed with this understanding of the components and sub-components of business risk, we are now halfway to a genuine assessment of our value creation potential. The next step is to assess accurately our own business against each of the 15 criteria and use them to evaluate the probability that our plan will deliver its promises.

This gradation of risk level is not straightforward. It is too simplistic to reduce risk assessment to a tick-box exercise. However, a comparison of a strategy against a large sample of a company's other strategies does provide a relative scale. By comparing, for instance, the evidence of market size, or the homogeneity of target markets, or the intended sources of profit, against this scale, a valid, objective assessment of the risk associated with a business plan can be made.

3.3.1.3 What use is this knowledge?

Marketing Due Diligence involves the careful assessment of a business plan and the supporting information behind it. In this assessment, it discounts subjective opinions and sidesteps the spin of investor relations. At the end of the process the output is a number, a tangible measure of the risk associated with a chosen strategy. This number is then applied in the tried-and-trusted calculations that are used to work out shareholder value. Now, in place of a subjective guess, we have a research-

Table 3.1 Factors contributing to risk

Overall risk associated with the business plan		
Market risk	**Strategy risk**	**Implementation risk**
Product category risk, which is lower if the product category is well established and higher for a new product category.	Target market risk, which is lower if the target market is defined in terms of homogeneous segments and higher if it is not.	Profit pool risk, which is lower if the targeted profit pool is high and growing and higher if it is static or shrinking.
Segment existence risk, which is lower if the target segment is well established and higher if it is a new segment.	Proposition risk, which is lower if the proposition delivered to each segment is segment specific and higher if all segments are offered the same thing.	Competitor impact risk, which is lower if the profit impact on competitors is small and distributed and higher if it threatens a competitor's survival.
Sales volumes risk, which is lower if the sales volumes are well supported by evidence and higher if they are guessed.	SWOT risk, which is lower if the strengths and weaknesses of the organization are correctly assessed and leveraged by the strategy and higher if the strategy ignores the firm's strengths and weaknesses.	Internal gross margin risk, which is lower if the internal gross margin assumptions are conservative relative to current products and higher if they are optimistic.
Forecast risk, which is lower if the forecast growth is in line with historical trends and higher if it exceeds them significantly.	Uniqueness risk, which is lower if the target segments and propositions are different from those of the major competitors and higher if the strategy goes 'head on'.	Profit sources risk, which is lower if the source profit is growth in the existing profit pool and higher if the profit is planned to come from the market leader.
Pricing risk, which is lower if the pricing assumptions are conservative relative to current pricing levels and higher if they are optimistic.	Future risk, which is lower if the strategy allows for any trends in the market and higher if it fails to address them.	

Micro-segment	1	2	3	4	5	6	7	8	9	10
What is bought										
Where										
When										
How										
Who										
Why (benefits sought)										

Figure 6.16 Micro-segments

bring together or cluster all those micro-segments that share similar or approximately similar needs (see Figure 6.19).

Once the basic work has been done in describing micro-segments, that is steps 2, 3, 4 and 5, any good statistical computer program can carry out cluster analysis to arrive at a smaller number of segments. The final step consists of checking whether the resulting segments are big enough to justify separate treatment, whether they are indeed sufficiently different from other segments, and whether they have been described sufficiently well to enable the customers in them to be reached by means of the organization's communication methods; the company then has to be prepared to make the necessary changes to meet the needs of the identified segments.

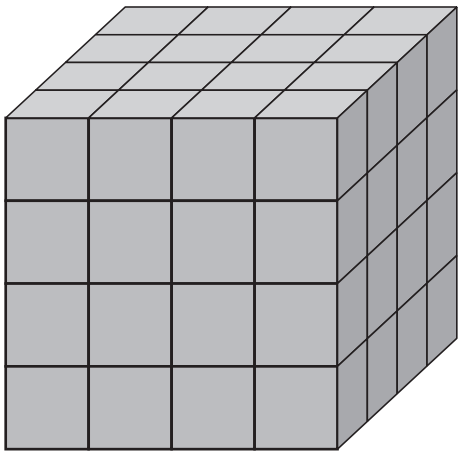


Figure 6.17 An undifferentiated market, but one with many different purchase combinations

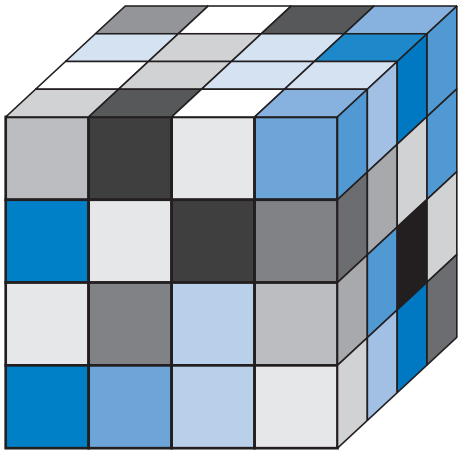


Figure 6.18 Different needs in a market

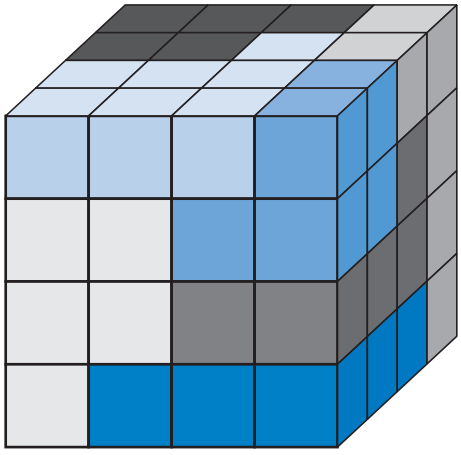


Figure 6.19 Segments in a market

Before the process of market segmentation can be summarized, it will by now be clear that market segmentation is fundamental to corporate strategy. It is also clear that, since market segmentation affects every single corporate activity, it should not be just an exercise that takes place within the marketing department, but has to involve other functions. Finally, the most senior levels of management must lead this initiative if their organization is to be truly market or customer need driven.

Table 6.3 is a summary of what we have discussed so far. It is obvious that there will be very few markets in the world where all customers have the same needs. Also, once market segmentation has been carried out, positioning products and services to meet the different needs of the different segments is comparatively easy. The difficult bit is segmenting markets. It is also vital to focus on serving the needs of the identified segments, whilst it is dangerous to straddle different segments with

the same offer. The photocopier example was only one example of thousands of well-known companies that suffered from this mistake as markets began to break into segments. The computer industry during the 1980s and 1990s was also replete with examples of this mistake.

The process of market segmentation itself consists of five steps: One, understand how your market works. This involves defining the market and drawing a market map. Two, list what is bought, including where, when, how, and the different applications of the product or service. Three, list who buys, using descriptors such as demographics and psychographics. Four, list why they buy, especially the benefits sought. Five, search for groups with similar needs. These will be the final market segments.

Market structure and market segmentation are the heart and soul of marketing. Unless an organization spends time on it, driven from the board downwards, it is virtually impossible for it to be market driven, and in any organization that isn't market driven the marketing function will be ineffective or, at best, will spend its time trying to promote and sell products or services that are inappropriate for the market. Figure 6.20 describes in more detail each of the important steps in the market segmentation process.

To see the details behind each stage, read *Market Segmentation: How to do it, how to profit from it* (McDonald and Dunbar, 2005).

Professional market segmentation is hard work, and is time-consuming. It is worth repeating why market segmentation is so important. Correct market definition is crucial for:

Table 6.3 Understand market segmentation

- Not all customers in a broadly defined market have the same needs.
- Positioning is easy. Market segmentation is difficult. Positioning problems stem from poor segmentation.
- Select a segment and serve it. Do not straddle segments and sit between them.

1. Define the market to be segmented and size it (market scope).
2. Determine how the market works and identify who makes the decisions (market mapping).
3. Develop a representative sample of decision makers based on differences they see as key (including what, where, when and how); note who they are (demographics) and size them.
4. Understand their real needs (why they buy, the benefits sought).
5. Search for groups with similar needs.

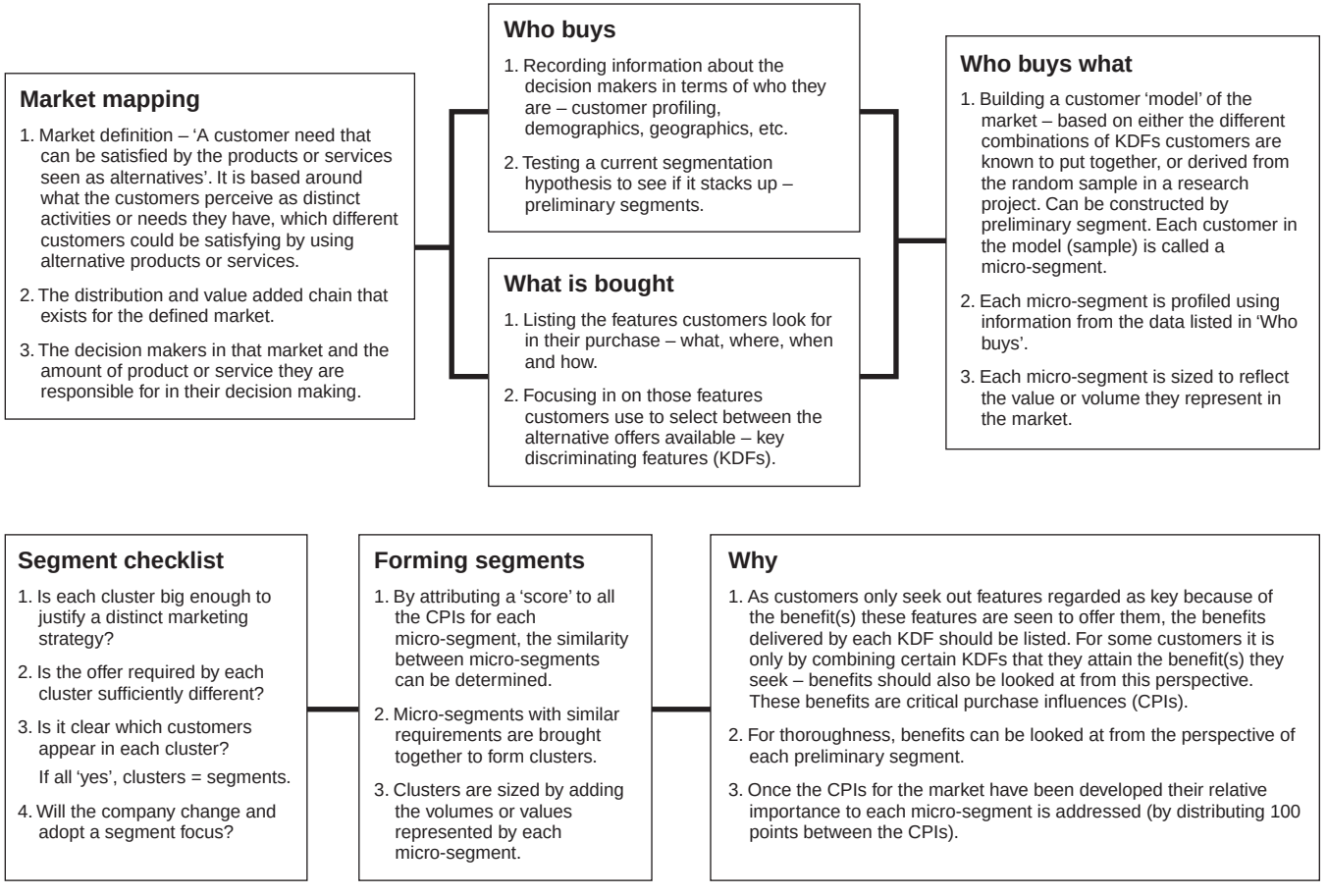


Figure 6.20 The market segmentation process – summary

- share measurement;
- growth measurement;
- the specification of target customers;
- the recognition of relevant competitors;
- the formulation of marketing objectives and strategies.

To summarize, the objectives of market segmentation are:

- to help determine marketing direction through the analysis and understanding of trends and buyer behaviour;
- to help determine realistic and obtainable marketing and sales objectives;
- to help improve decision making by forcing managers to consider in depth the options ahead.

6.5 Case studies

Case study 6.1: A national off-licence chain

In the mid-1980s, a national off-licence chain, with retail units in major shopping centres and local shopping parades, was experiencing both a decline in customer numbers and a decline in average spend. The original formula for success of design, product range and merchandising, meticulously copied in each outlet, no longer appeared to be working. The chain had become a classic example of a business comfortably sitting in the middle ground, attempting to be all things to all people, but managing to satisfy very few of them.

Rather than sit back in the belief that the business was just passing through a difficult patch, and what worked yesterday was bound to work again, the company embarked on a project designed to understand both its actual and its potential customer base.

The first stage of this study turned to one of the more sophisticated geodemographic packages in order to understand the residential profiles of each shop's catchment area. Not unexpectedly, many geodemographic differences were found, and the business quickly accepted that it was unlikely that the same retail formula would appeal to the different target markets found in them.

Rather than looking at each shop separately, the catchment area profiles for each shop were subject to a clustering routine in order to place similar catchment areas together. This resulted in 21 different groupings, each of which was then profiled in terms of its potential to buy different off-licence products using purchasing data from national surveys. (The company's own

in-house retailing data would, of course, reflect only the purchasing pattern of existing customers or, at worst, only a proportion of their requirements if this was limited by the company's current range.)

However, stocking the requisite range of products in their correct geographical location would not necessarily attract their respective target markets. The chain was already associated with one type of offer that, in addition to including a particular range of drinks, also included the basic design of the shops and overall merchandising.

The project, therefore, moved into a second stage, in which the market's attitudes and motivations to drinking were explored and relative values attached to the various dimensions uncovered. This was achieved through an independently commissioned piece of market research, and resulted in the market being categorized into a number of psychographic groups. These included, amongst others, 'happy and impulsive' shoppers, 'anxious and muddled' shoppers, 'reluctant but organized' shoppers, and the 'disorganized, extravagant' shoppers.

By ensuring that this stage of the project linked the attitude and motivational findings to demographic data, the two stages could be brought together. This enabled the original 21 clusters to be reduced to give distinct segments, each of which required a different offer.

The company then had to decide between two alternative strategies: 1) to focus on one segment using one brand and relocate its retail outlets accordingly through a closure and opening programme; or 2) to develop a manageable portfolio of retailing brands, leave the estate relatively intact, and rebrand, refit and restock as necessary. The company decided to pursue the second strategy.

Realizing that the demographic profiles in geographic areas can change over time, and that customer needs and attitudes can also evolve, the company now monitors its market quite carefully and is quite prepared to modify its brand portfolio to suit changing circumstances. In the early 1990s, however, its five retail brands of 'Bottoms Up', 'Wine Rack', 'Threshers Wine Shop', 'Drinks Store from Threshers' and 'Food and Drinks Store' sat comfortably within the five segments. They also sat comfortably together in the same shopping centre, enabling the group to meet effectively different requirements of the segments found within that centre's catchment area.

Perhaps more importantly, this strategy sits comfortably alongside the financial targets for the business.

(Based on Thornton, 1993)

Case study 6.2: Sodium tri-poly phosphate!

Sodium tri-poly phosphate (STPP) was once a simple, unexciting, white chemical-cleaning agent. Today, one of its uses is as the major ingredient of a sophisticated and profitable operation, appearing under many different brand names, all competing for a share of what has become a cleverly segmented market.

Have you ever wondered how the toothpaste marketers classify you in their segmentation of the market? Table 6.4, adapted from Haley (1968), which presents the main segments, may assist you.

Table 6.4 Toothpaste market segmentation

	Segment name	Worrier	Sociable	Sensory	Independent
Profile	Demographic	C1, C2	B, C1, C2	C1, C2, D	A, B
		25–40	Teens	Children	35–40
		Large families	Young smokers		Male
	Psychographic	Conservative: hypochon-driacs	High sociability: active	High self-involvement: hedonists	High autonomy: value-orientated
What is bought, where, when and how	Product examples	Signal, Mentadent P	Macleans, Ultrabrite	Colgate, Aquafresh	Own label
	Product features	Large canisters	Large tubes	Medium tubes	Small tubes
	Health properties	Whitening properties	Flavouring		
	Outlet	Supermarket	Supermarket	Supermarket	Independent
	Purchase frequency	Weekly	Monthly	Monthly	Quarterly
Why it is bought	Benefits sought	Stop decay	Attract attention	Taste	Functionality
	Price paid	Medium	High	Medium	Low
	Percentage of market	50%	30%	15%	5%
Potential for growth		Low	High	Medium	Nil

Note: 'C1', 'C2' and so on appearing in the demographic profiles of each segment represent socio-economic groups that were in use in the UK until 2001, now replaced by eight analytic classes numbered from 1 through to 8. 'Signal' and 'Mentadent P' are trademarks of Lever Fabergé; 'Macleans' and 'Aquafresh' are trademarks of GlaxoSmithKline; 'Ultrabrite' and 'Colgate' are trademarks of Colgate-Palmolive.

Case study 6.3: GlobalTech (service segmentation)

Summary

This case study describes the use of market segmentation to assist in the development of a service product. Customer requirements were captured via qualitative research. The segmentation was completed through the use of quantitative research. The result was a set of segments that enabled the development of a new approach to delivering service while improving customer satisfaction. GlobalTech is the fictitious name of a real company marketing high-tech and service products globally. Customers are counted in hundreds of thousands. The markets are mainly business-to-business, with a very few large customers buying thousands of items. Service is a major revenue stream measured in billions of dollars. The lessons learnt could be of interest to any organization having to care for a large number of customers.

Background

A failed segmentation

An internal GlobalTech team tried to complete a marketing audit early in 2000. This included market definition, market segmentation and quantification. The product divisions conducted their audits separately. They used mainly brainstorming techniques to define their markets and produce the data required.

Lesson 1

Markets transcend your internally defined product divisions. Therefore it is best to understand the markets and monitor your overall performance in those markets. To reshape market information to meet the needs of internal reporting will lead to misinformation.

On completion, the results were compared across the divisions. It rapidly became apparent that each division addressed almost all the markets. However, the market definitions they produced were different, with significant bias towards just the products they offered. Similarly, the segments each division identified were in conflict with the outputs from the other divisions. On reflection, it was agreed that the results were unreliable. They could not be used to help shape future strategies or marketing investments.

GlobalTech was now in the uncomfortable situation of being in a market information vacuum. Any confidence it had had in its understanding of the

market had been destroyed. Consequently, the decision was taken that all future market analysis and understanding tasks would be supported by appropriate investments in market research.

Lesson 2

Do not rely on the internally gathered opinions of your sales and marketing staffs to define markets and identify customer requirements and attitudes. Do invest in the necessary market research to provide a reliable segmentation and support for strategy and product development.

First market segmentation

The following year the segmentation was redone, supported by extensive qualitative and quantitative market research. The objective was to understand and group into segments the product buyers in the overall market.

The qualitative study produced a very clear picture and definition of the markets addressed by GlobalTech. It also provided the customers' view of the benefits they sought from the products and the differences in their attitudes towards their suppliers. The questionnaire for the quantitative study was based on the results of the qualitative study. The result was seven clearly defined product buyer segments.

This enhanced understanding of the market assisted with hardware and software product marketing but did not address service products or customer satisfaction and loyalty issues.

The internal need

At the dawn of the 21st century, the market life cycle had matured. All but the more sophisticated products were perceived as commodities. Consequently, the opportunities for effective product differentiation had diminished. GlobalTech, in common with its competitors, was finding that customers were becoming increasingly disloyal.

For many years, product churns and upgrades from existing customers had accounted for some 70 per cent of GlobalTech's product revenues. Service and exhaust revenues almost equalled total product revenues. (Exhaust revenues are those revenues that follow on, almost automatically, from an initial product sale. These would normally include service plus training, consumables, supplies and add-ons, etc.) Service was perceived to be a key influencer of loyalty, but the costs of delivering service were becoming

unacceptable to customers. Concurrently, service pricing was coming under increasing competitive pressures.

The challenge was to increase loyalty while achieving a step function improvement in margins. Thus it was decided to invest in a better understanding of the service market as an enabler to delivering cost-effective differentiation and loyalty. This case study covers the project from inception to implementation.

The segmentation project

Buy-in

The GlobalTech main board director responsible for customer service sponsored the project. This was a critical prerequisite, as the outcome would have a significant impact on the organization, its processes and behaviours.

Similarly, the project team included key members of service, marketing and finance to ensure buy-in. However, at that time it was deemed inappropriate to include representatives from all but two of the countries, owing to travel implications, cost, and resource impacts. In retrospect, this was not a good decision.

Lesson 3

Try to anticipate the scale of the organizational change that may result from a major segmentation project. Then ensure that the buy-in planned from the start of the project embraces all those who will have a say in the final implementation.

Business objectives

The project team agreed the overall business objectives as:

- to develop strategies for profitable increase in market share and sustainable competitive advantage in the service markets for GlobalTech's products;
- to identify opportunities for new service products and for improving customer satisfaction within the context of a robust customer needs segmentation that can be readily applied in the marketplace;
- to identify the key drivers of loyalty so that GlobalTech may take actions to increase customer loyalty significantly;

- to provide the information required to help develop a new and innovative set of service products designed and tailored to meet differing customer requirements while significantly reducing internal business process costs.

Results from the qualitative study

The output from the qualitative study was a 93-page report documenting the results, in line with the desired research objectives. Some of the more surprising aspects were supported by verbatims. A key output was the polarization of very different attitudes towards service requirements that some buyers had in comparison with others. For example:

- Some wanted a response within a few hours, whereas many others would be equally happy with the next day.
- Some wanted their staff thoroughly trained to take remedial actions supported by a specialist on the phone, while others did not want to know and would just wait for the service provider to fix the problem.
- Some wanted regular proactive communications and being kept up to date, while others wanted to be left alone.
- Some would willingly pay for a premium service, under a regular contract, while others would prefer to take the risk.
- The attitudes of professional buyers, procuring on behalf of user departments, were consistently different from those of the user departments.

Results of the quantitative study

The output from the quantitative study was extensive. Much of the output was detailed demographic data, opportunities information and competitive positioning comparisons. However, the focus was on a fairly extensive executive summary for internal communications within GlobalTech. What follow are summarized extracts from those outputs.

The segments

Six market segments were identified as a result of iterative computer clusterings. Initially the clustering routines had identified more segments, but by careful analysis these were reduced to what was decided to be the most manageable level. Some previously very small segments were merged with very similar larger segments.

Polarizations in attitude

The computer clustering generated the segments by grouping customers with similar attitudes and requirements. This resulted in some marked

differences in attitude between segments. As illustrated in the list below, the Koalas really did not want to know about being trained and having a go, but the Teddies, Yogis and Polars had an almost opposite attitude:

- *Koala Bears:* Preserve their assets (however small) and use, say, an extended warranty to give them cover; won't do anything themselves, but prefer to curl up and wait for someone to come and fix it.
  Small offices (in small and big companies), 28 per cent of market
- *Teddy Bears:* Lots of account management and love required from a single preferred supplier; will pay a premium for training and attention. If multisite, will require the supplier to cover these sites effectively ('Protect me').
  Larger companies, 17 per cent of market
- *Polar Bears:* Like Teddy Bears except colder! Will shop around for the cheapest service supplier, whoever that may be. Full third-party approach. 'Train me but don't expect to be paid.' Will review annually (seriously). If multisite, will require the supplier to cover these sites effectively.
  Larger companies, 29 per cent of market
- *Yogi Bears:* 'Wise' Teddy or Polar Bears working long hours; will use trained staff to fix if possible. Need skilled product specialist at the end of the phone, not a booking clerk. Want different service levels to match the criticality of the product to their business process.
  Large and small companies, 11 per cent of market
- *Grizzly Bears:* Trash them! Cheaper to replace than maintain. Besides, they're so reliable that they are probably obsolete when they break. Expensive items will be fixed on a pay-as-and-when basis – if worth it. Won't pay for training.
  Not small companies, 6 per cent of market
- *Andropov Big Bears:* My business is totally dependent on your products. I know more about your products than you do! You will do as you are told. You will be here now! I will pay for the extra cover but you will…!
  Not small or very large companies, 9 per cent of market

Satisfaction and loyalty

GlobalTech was measuring customer satisfaction for use both locally, as a business process diagnostic tool, and globally, as a management performance metric. These satisfaction metrics were averaged across all customers, both by geographic business unit and by product division to meet internal management reporting requirements.

However, the outputs from the quantitative study clearly showed that these traditionally well-accepted metrics were, in fact, almost meaningless.

What delighted customers in one market segment would annoy customers in another, and vice versa. To make the metrics meaningful, they had to be split by key criteria and the market segments. Loyalty was obviously highest where GlobalTech's 'one size fits all' service deliverable coincidently best matched the segment's requirement, as illustrated in Figures 6.21 and 6.22.

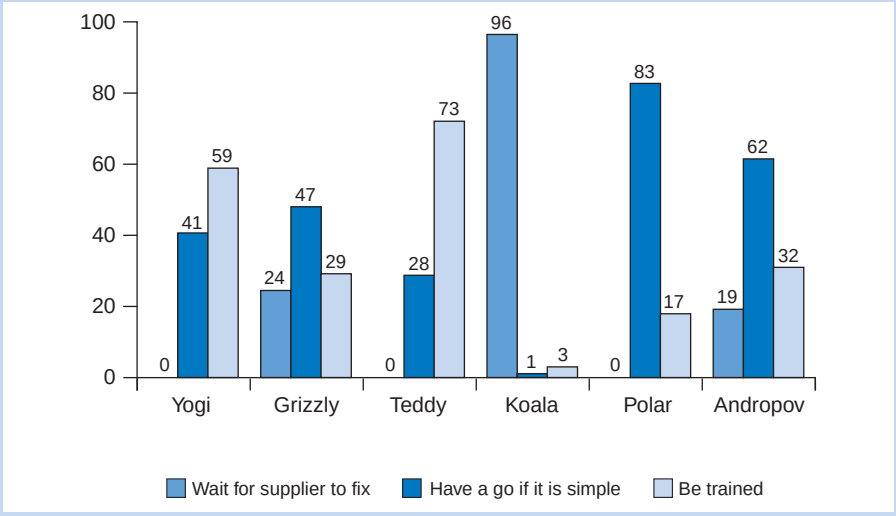


Figure 6.21 Key criteria for the market segments

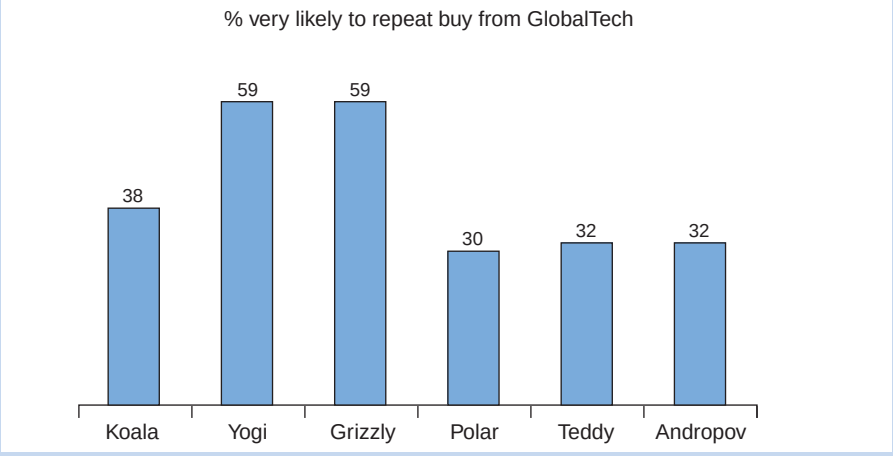


Figure 6.22 Likelihood of repeat buying from GlobalTech

Correlation between loyalty and customer satisfaction

The market life cycle for many of GlobalTech's products was moving into the commodity phase. Therefore, not surprisingly, customers were becoming less loyal.

Each percentage point increase in loyalty translated into almost the same increase in market share. Each percentage point in market share added many millions of dollars of gross revenues. The cost of reselling to a loyal customer was about one-sixth the cost of winning a new customer. Consequently, each percentage point increase in loyalty had a significant impact on the bottom line.

Because of this, the quantitative study included correlating the key drivers of satisfaction and loyalty within each market segment. The qualitative study identified some 28 key customer requirements of their service provider. The quantitative study prioritized these to provide a shorter list of 17 common requirements. The correlation exercise reduced this to only two requirements that drew a significant correlation between satisfaction and loyalty: 1) providing service levels that meet your needs; and 2) providing consistent performance over time. Although GlobalTech was achieving the second, it was delivering the first in only two of the market segments.

Segment attractiveness

As an aid to deciding where best to invest, a chart of segment attractiveness was produced using attractiveness factors determined by GlobalTech (Figure 6.23). Demographic data from the quantitative study were combined with internal GlobalTech financial data. Each factor was weighted to reflect the relative importance to GlobalTech. This highlighted quite a few issues and some opportunities. For instance, the highest margins were coming from some of the least loyal segments.

Competitive positioning

Fortunately for GlobalTech, its competitors did not appear to have an appreciation of the market segments of the differing requirements of their customers. They were also mainly delivering a 'one size fits all' service offering. However, there were some noticeable differences in their offerings. These resulted in each major competitor being significantly stronger in just one or two market segments where their deliverable best matched the segment needs.

The quantitative study provided detailed ranking of the DBCs and CSFs for each market segment. These were to prove invaluable during the phase of designing the service products and developing the strategy to achieve competitive advantage.

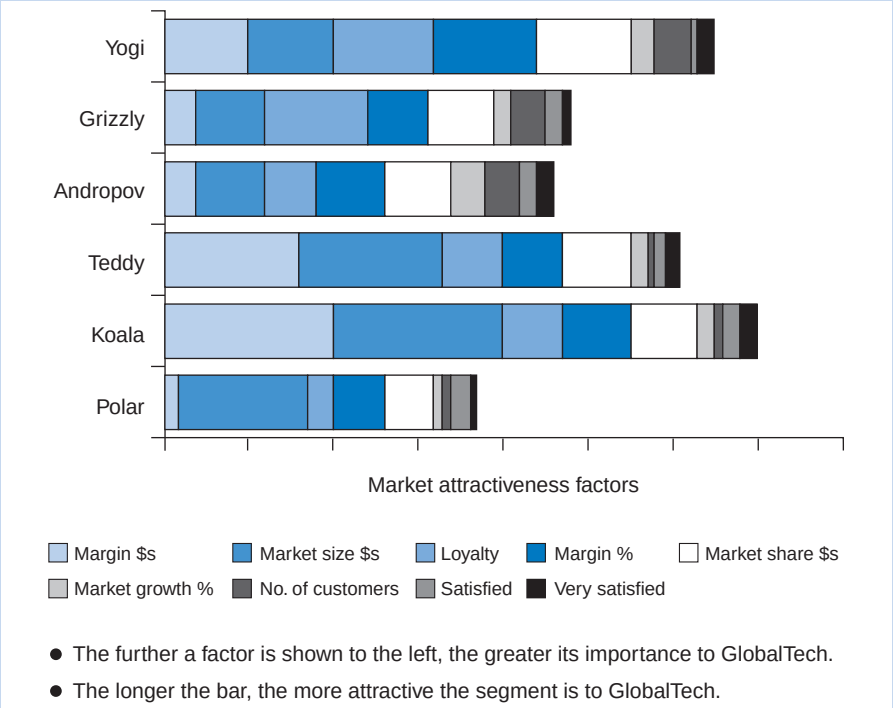


Figure 6.23 Market attractiveness factors

Decision buying criteria (DBCs) are the needs (benefits) buyers are seeking to have satisfied by their choice of product or service.

Critical success factors (CSFs) are the constituents of the factors required to deliver each DBC.

Reachability

Key to GlobalTech successfully implementing any strategies or communications that were to be market segment based would be being able to identify each customer by segment. As part of the quantitative study, two statistical reachability tasks were completed.

A sampling of internal GlobalTech databases showed that there were sufficient relevant data to achieve better than 70 per cent accuracy, using statistical imputation methods, to code each customer record with its market segment. This was considered to be good enough to enhance marketing communications measurably, but might not be sufficiently accurate to ensure always making the most appropriate offer. Statistical analysis identified four

questions that would provide acceptable accuracy in segment identification. These questions could then be used during both inbound and outbound call centre conversations until such time as all customers had been coded.

The recommendation was to use both methods in parallel so that accuracy would improve over time. Also, the coding of larger customers should be given a priority.

Lesson 4

Understanding the different market segments helps in designing the required offers, but do not get too concerned about reachability. It is not essential to code every customer to the right segment from day one. Where you are not really sure, let them see different offers and so position themselves. Similarly, be willing to accept that within a large organization some buyers may fall into different market segments, though the difference will be on only one or perhaps two buying criteria rather than across all the buying criteria.

Strategy development and implementation

Market understanding and strategy development

The challenge now was for the project team to absorb and understand all the findings from the two research studies. The team then had to turn that understanding into realizable strategies. To achieve this, a workshop process covering opportunities, threats and issues (OTIs) was used. Briefly, the process involved an extensive, but controlled, brainstorming session followed by a series of innovative strategy development workshops.

A facilitator took the team systematically through each piece of relevant information available. Using brainstorming, the team tried to identify every conceivable opportunity, threat or internal issue associated with each item of information. The information was also then tested against a predetermined list of business behaviours and processes in an endeavour to entice additional and creative ideas out of the brainstorming. Using the DBCs and CSFs from the market model, strengths and weaknesses were added, thus turning the process into a SWOT. Like ideas were merged and de-duplicated.

Each idea was given two scores in the range of 1–9. The first ranked the probable financial impact; the second ranked the probability of success. The ideas were then grouped by like activity and where they had the same or an overlapping financial impact. This ensured that double-counting was eliminated, and that opportunities and threats were offset as appropriate. Any

one group of ideas would take on the highest single financial impact score and a reassessed probability-of-success score. If the resolution of an internal issue was a prerequisite for capturing an opportunity or overcoming a threat, then the issue plus associated costs and resources was included in the same group as the opportunity or threat. The norm was for a single issue to be attached to many groups. The groups were named and then ranked by both financial impact and probability of success. This provided a prioritized short-list of imperatives that should deliver the maximum realizable benefits to both GlobalTech and its customers. Iterative discussions developed this into an overall strategy with a number of prioritized sub-strategies. Each sub-strategy was supported by a documented description of the opportunity. At this stage, encouragement was given to creating innovative, yet simple, implementation options that would maximize the chances of success. Each implementation option was supported by market, revenue and organizational impact data, associated issues, resources, costs, and required control metrics. Board members were involved in an option selections and investment approvals process. Finally, the implementation programmes and project plans were created.

The strategy

The overall recommendation was to create a set of service deliverables tailored to the individual needs of each segment. These would be complemented by a set of premium add-ons that could be offered to the appropriate segments. By focusing on business process simplification during the design of the offering for each segment, redundancy was eliminated.

The objective of each offering was to increase customer satisfaction significantly, with an emphasis on those items that would most positively impact on loyalty. Some offerings were quite different from others, in terms both of the deliverable and of the internal processes that made it possible. This differentiation was also intended to create a measurable competitive advantage in a number of market segments.

A key to the implementation of the project was a recommended change to the customer satisfaction metrics, so that they became an effective diagnostic tool for tuning the ongoing deliverables for each market segment.

Implementation

Throughout the project, the same core team had been intimately involved with each stage of the project. They guided the work and took on board the results. They delved deeply into the analysis and did their best to understand the markets, their customer requirements and likely competitive impacts. Finally, they worked hard at developing the proposed strategies. They

thought buy-in had been achieved by the project being sponsored by a main board director.

The implementation roll-out across country boundaries became difficult. Each country wanted its say. Each country had different views of its customer needs and how things should be done in the country. The countries did not easily understand or even accept the findings of the research and the meaning of the outputs.

The majority of these internal barriers were eventually overcome. Inevitably, there were compromises. These led the project team into believing that not all the market segments would be fully satisfied with the new offerings in all countries.

6.5.1 Case studies conclusion

These three case studies illustrate the importance of intelligent segmentation in guiding companies towards successful marketing strategies. However, it is easy to understand this success after the event. The problem for most of us is how to arrive at meaningful segments that will enable us to create differential advantage. This is the purpose of this chapter.

6.6 Segmentation and the Metrics model

6.6.1 Summary

The purpose of this section of the chapter is to describe briefly how the necessary segmentation data should be captured in the Metrics model. The stage in the overall model process is shown in Figure 6.24.

6.6.2 The Ansoff Matrix

The Ansoff Matrix (Ansoff, 1957) provides a useful framework for identifying the products/services that might be most appropriate for each selected segment (Figure 6.25). This is a two-dimensional matrix mapping what is sold (products/services) and to whom (segments), divided into four possible strategies:

1. Sell existing products/services to existing segments.
2. Sell existing products/services to new segments.
3. Develop new products/services to sell to existing segments.
4. Develop new products/services to sell to new segments.

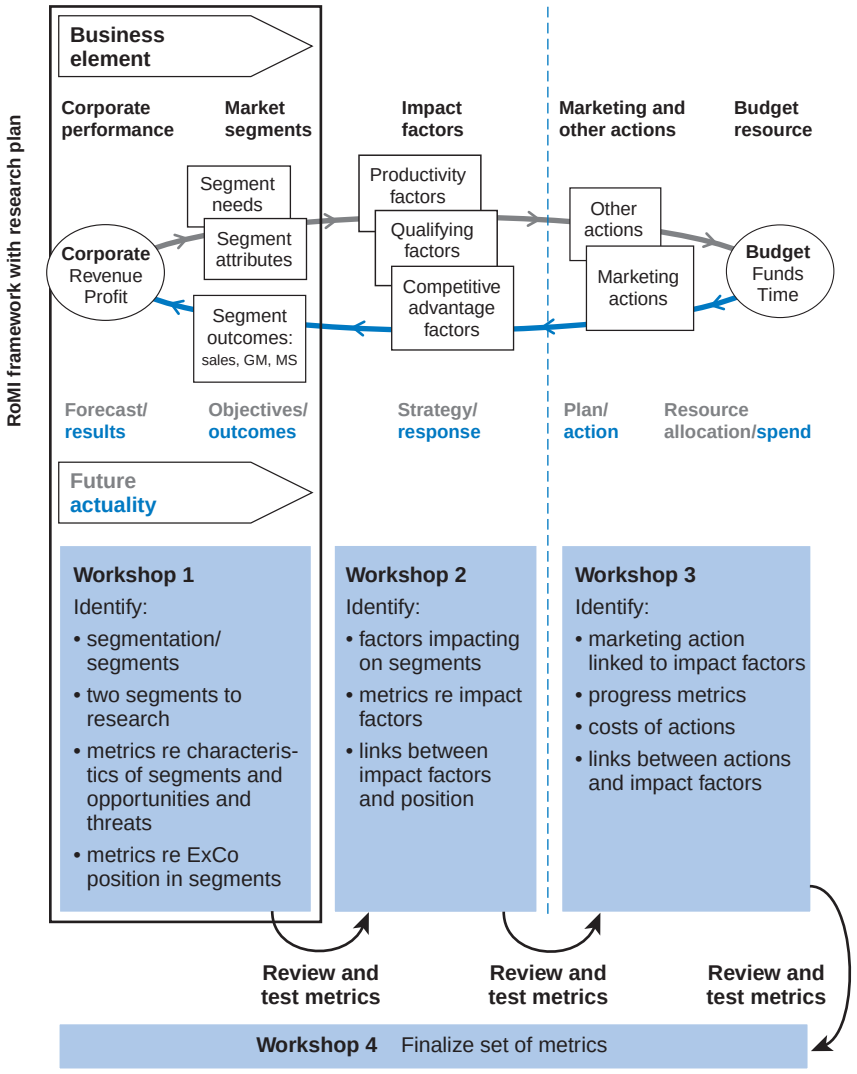


Figure 6.24 Marketing Metrics model process: market segments

'Existing' segments can also be interpreted as those segments in a market that the company is already serving, whilst 'new' segments can also mean segments existing in a market that the company has not served in the past.

6.6.3 Applying the Metrics model

As shown in Figure 6.25, some strategies will be about increasing penetration within an existing segment, whereas others might be about entering new markets, requiring the company to diversify beyond its historical 'comfort zone' and take a higher risk.

Table 7.3 Productivity factors template

Segment title: 'Specialist retailers'

Productivity factor	Metric	Measurement method	Importance weighting %	Our current position	Our target position	Benchmark
Reduce level of missed calls	Missed calls	Call centre stats	40	15%	5% (yr 1)	10%
Minimize obsolete stock	Dumped stock £ & %	Stock stats	40	10%	2%	–
Lower average time to payment collection	Invoice to payment days	Accounts receivable stats	20	60 days	30 days	–
Total			100			

to establish the *qualifying factors* for delivering a telephone-based customer service by studying the needs of consumers and the service provided by competitors (using mystery shopping methods) – what the norm was that was expected in the market. The second step was to identify what would deliver a service level that would clearly create additional benefits in the minds of consumers – the *competitive advantage factors*. The final step was to define the *productivity factors* to ensure that the improved service would be delivered as efficiently as possible. This process would be repeated for each strategy, identifying any common factors that apply across strategies, and across key segments of customers. The revised template to capture the required information and identify the metrics is shown in Table 7.4.

The template records the criteria required for each type of impact factor. These show that the organization does not currently meet the qualifying factors expected by customers in the particular segment 'Wealthy empty-nesters'. However, as shown for the competitive advantage factors, customers would like to see service levels above those currently provided by competitors. Finally, the organization has also identified opportunities to provide service more efficiently, use the opportunity of contacts with customers to update information held about them on the customer database, and increase the level of trade-up sales of additional products by the call centre. The current position, the target levels (and by when in the plan), the metrics that will track performance, how the performance will be measured, and who will be responsible are recorded.

7.6 Impact factors: using 'gap' analysis for creating organizational alignment

A further tool helpful in identifying whether the organization is in tune with the needs of the consumer is a form of gap analysis, such as can be found within the SERVQUAL model for measuring customers' perceptions of service quality. The full model was developed in the 1980s and based on a questionnaire covering 22 criteria most commonly found in the initial qualitative research conducted amongst consumers to identify the factors that participants used in assessing service quality. These were divided into five initial dimensions, with a further one added a few years later:

- *tangibles:* the physical aspects or service, such as the equipment used, the appearance of the service personnel, etc;
- *reliability:* the ability to deliver the promised service dependably and accurately;
- *responsiveness:* the willingness to help customers and provide service promptly;
- *assurance:* the attitude of employees, their knowledge and the extent to which they inspire trust and confidence;

Table 7.4 Impact factors: analysis by strategy

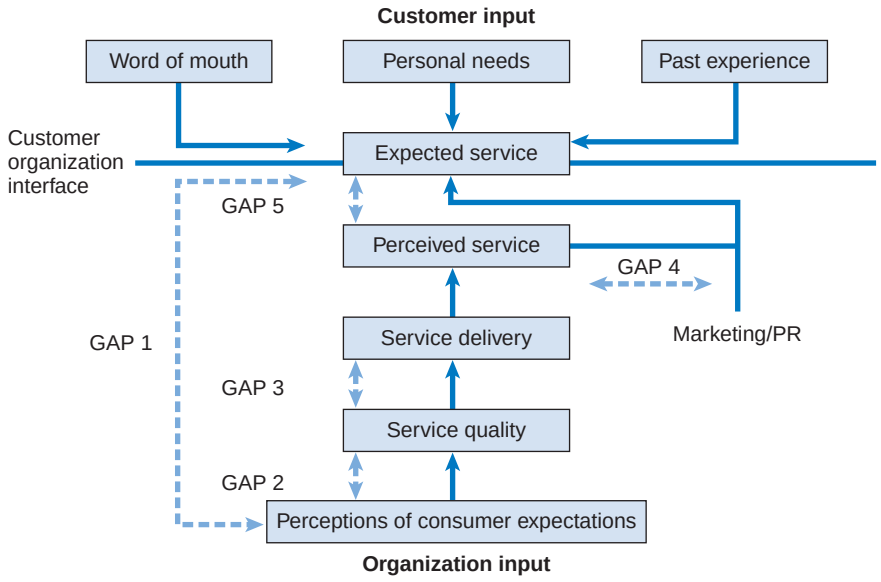
Segment: Wealthy empty-nesters. Strategy: Improving call centre customer service

Type of factor/level	Criteria	Current	Target	Metric	How measured	Who measures
Qualifying level	• All calls answered in six rings	50%	95%	Abandoned calls	Call stats	Customer services
				Availability	Management reports	Customer services
	• Available 8.00 am–8.00 pm, 6 days	8.00 am–6.00 pm, 5 days	Parity	Customer satisfaction	Market research	Market research
	• Agent friendly and professional	70%	100%			
	• Able to deal with queries related to core product – other queries resolved by calling customer within 24 hours	40%	80%	Mystery shop	Mystery shop/ market research	Market research
Competitive advantage level	• All calls answered in six rings, 24/7	24/7 not offered	95% (1 yr)	Call stats	Management report	Customer services
	• Able to deal with queries related to all products held by customer – resolved during call	Not offered	100% (yr 2) 60% (yr 2)	Customer satisfaction	Market research	Market research
	• Able to answer queries about other products available			Mystery shop/ customer stats	Market research	Market research
	• Third-party partners meet required standard	Not offered				Operations dept
		Variable level	5 main partners (yr 2)	Audit/customer satisfaction/ mystery shop	Operations reports	
Productivity	• Use of CRM system	50% of calls	80%	CRM stats	CRM system	CRM team
	• Average length of call	10 mins	5 mins	Call stats	Telephony stats	Customer services
	• Data collected/amended	Ad hoc	All possible calls	Database audit	Data quality report	Database team
	• Additional products sold	3% of calls	6% of calls	Sales stats	Sales reports	Sales

- *empathy:* the ability to deliver a caring, individualized service;
- *recovery:* the ability of the organization to rectify problems (added in the late 1980s by a further researcher).

From this initial research, the authors developed a service quality gap model. In this model, service quality was defined as a function of the gap between customers' expectations of a service and their perceptions of the actual service delivered. This is the part of the overall SERVQUAL model that is useful in identifying whether an organization is aligned with the needs of customers, and is shown in Figure 7.6. (For further details of the SERVQUAL methodology, see Parasuraman, Zeithaml and Berry, 1990.)

The customer/organization interface is where the expectations, and perceptions, of the consumer – based on needs, past experience, the views of others and the claims made by the organization in its marketing and public relations activity – meet the reality of what the company is actually delivering. Obviously, market research can play a major role in understanding consumers, their needs and expectations, and what influences their attitudes and behaviour. As important is to ensure that all of those responsible within the organization (or those responsible for external, third-party providers) for ensuring that a defined level of service is delivered are committed to meeting the defined level of service that will create competitive advantage. Each of the 'gaps' shown in Figure 7.6 can lead to the service provision failing to match market needs. In essence, this is the customer service subset within Porter's value chain described earlier in this chapter. The point is that



Source: Parasuraman, Zeithaml and Berry (1990)

Figure 7.6 'Gap' analysis for the customer service value chain

marketers need to ensure that there is alignment at the customer/organization interface. However, traditionally, marketing may be responsible only for the marketing activity that informs consumers or makes the promises, but this must be aligned with perceived, or expected, levels of service – Gap 4 in Figure 7.6. Therefore, marketers need to take responsibility for ensuring this alignment is in place and committed to by all others involved in service delivery, and that the appropriate internal and external metrics are in place to measure performance over time.

A 'gap' analysis can also be helpful in identifying actions, covered in Chapter 8.

7.7 Helpful pointers

Common mistakes made by companies undertaking an impact factor analysis are:

- Thinking that improving performance for qualifying factors beyond that of competitors will confer competitive advantage. This will only lead to wasting scarce resources that could be more effectively employed in addressing needs identified in the competitive advantage analysis.
- Not being objective when comparing the performance of their own organization against that of key competitors, or not considering the actions competitors might take in response to their own moves in the market.
- Not taking the consumer's perspective when assessing what will create competitive advantage in the market.
- Not undertaking a thorough enough analysis of their supply chain to identify areas where efficiencies or improvements might be possible in order to reduce costs or improve profitability.
- Not monitoring the impact of productivity factors to ensure that these do not compromise achieving necessary performance against qualifying and competitive advantage factors, for example forcing customers to use a particular channel when contacting the organization in order to create maximum cost savings.

Finally, think of the following points when analysing impact factors and how the appropriate metrics can be identified:

- There are some offers and levels of performance that are now expected by this segment. What do you have to do just to stay in the market alongside good competitors?
  - Identify the qualifying factors that are the least you must do.
  - What metrics enable you to track them?
- What would make consumers want to buy from you, rather than from a competitor?
  - Which competitive advantage factors would really make a difference to this segment?
  - What would you measure to establish whether this competitive advantage, or a strategy/value proposition based on it, was achieving your goals?

- You want to optimize your return from the segment while making sure that any efficiency measures do not impact negatively.
  - Identify the productivity factors that are relevant.
  - What metrics will help you monitor them?
- Whilst the analysis is segment specific, some impact factors may span other, or all, segments.
  - This could apply, for example, to customer service. One leading financial services organization when introducing a website to reduce the load on the call centre, and thereby reducing costs, promoted this development to high-value customers as providing the benefit of 24/7 access.
- In the Marketing Metrics model, strategies are derived from the impact factors, which in turn determine the responses to the needs of the segment.
- There are three kinds of impact factors:
  - qualifying: maintain position, potential business losers;
  - competitive advantage: differentiators, business winners;
  - productivity: internal efficiency/cost improvements.
- Identifying impact factors will often require external market research, which will require external spend. However, the cost should be balanced against the danger of not having the information. Opportunities exist to consolidate research and keep costs to manageable levels. Do not ignore the knowledge and experience that are available within most established organizations which can be harnessed in developing a full picture of the market and filling gaps in information – just ensure that the final agreed view is objective.
- Addressing the issues raised in the factor analysis will often require the marketing team to liaise with other key teams within the company in order to develop effective business cases, or arguments, to stimulate commitment and change.

Do not forget that, regardless of who has to take action to address any of the impact factors, the responsibility for monitoring their impact rests with marketing.

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8

Turning strategy into action, and measuring outcomes

So how many bacon and egg breakfasts do I have to sell to pay for that?'
(Sir Charles Forte in response to a marketing proposal)

Summary

The impact factor analysis described in Chapter 7 enables strategies to be identified and developed for each segment. The metrics for measuring the performance of these strategies have also been defined and listed. However, strategies can be delivered only through appropriate *actions*. It is the actions that incur costs, that lead to revenues being generated and that lead to increased efficiency. Pinpointing these actions, and the associated performance measures, are the topics covered in the first section of this chapter. This obviously leads to considering the *budget* implications – the costs of delivering these actions, and the forecast revenue flows or efficiencies that together form the basis for developing a compelling business case for implementing the proposed strategy. As recommended by Binet and Field (2007), this should be task or zero based (developing a new budget based on the cost of the resources required), with budgets being determined by the goals, strategies and actions set for the segment, rather than rolling forward an annual budget for marketing that is then divvied up across various activities,

aimed at different audiences. Finally, this chapter covers the linkages that can be expected as a result of implementing a costed strategy – the assumptions made about likely cause and effect. This stage of the model relative to the others is shown in Figure 8.1.

8.1 Developing action plans

As described in earlier chapters, actions necessary to deliver a strategy may be only partially owned by marketing. Marketing, however, cannot take responsibility for ensuring that all actions required by other parts of the company to deliver an agreed

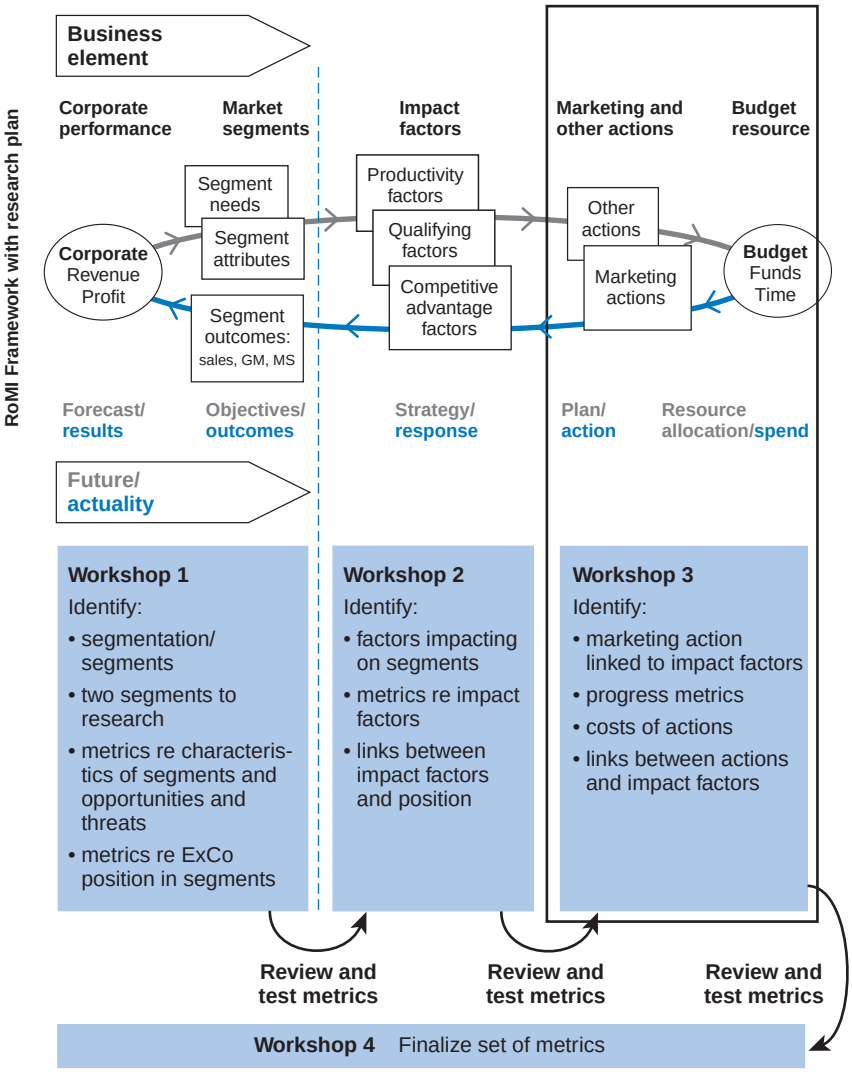


Figure 8.1 Marketing Metrics model process: actions and budgets

strategy are implemented and that other teams are measuring performance. The marketing team has to develop a convincing plan that clearly demonstrates to other areas of the company why actions are required, and the benefits that lead to achieving corporate goals, in order to gain cooperation. This is easy to say, but company structure, preoccupation with achieving short-term goals, conflicting priorities, variable levels of commitment from senior management, accounting conventions and so on are all examples of challenges that are likely to be faced in gaining the necessary cooperation from colleagues. For example, if required actions require collaboration with operations and logistics, then there will be the need to influence decisions across all these areas. Porter's value chain model, described in Chapter 7, can be very helpful in identifying where actions might be necessary, who might need to be influenced, and the arguments that might be successfully used to gain cooperation.

The marketing team may be responsible for assessing both the value required by customers and their value to the company, but the whole organization is involved in delivering, and sustaining, that value.

Actions might be linked to individual impact factors by segment or to a particular strategy; they might cover a need identified across several, or all, segments. For example, the need to answer a service call in six rings might be an appropriate strategy for all valued customer segments.

8.1.1 Identifying actions

Some actions are more obvious than others. For example, an FMCG company that regularly introduces new products to the market will have a defined process developed over time that identifies the key actions necessary across the organization. Whatever the process that is used, it must help ensure that all necessary actions, and the dependencies between them, are identified. A tool developed at Cranfield University School of Management to provide such a process is the Benefits Dependency Network (BDN), shown in Figure 8.2. Whilst this model was initially developed to identify appropriate IT solutions in order that business goals can be achieved, in a modified form it can be used to help identify the actions necessary to achieve marketing strategies, and the metrics necessary to track performance. The example shown in Figure 8.2 is based on an analysis conducted for a leading international packaging company as an input to its key account management strategy.

The process runs from right to left, starting with the *strategy* defined in the impact factor analysis described in Chapter 7. The position relative to the impact factor analysis is shown, as this is where the strategies are identified.

The first step is to brainstorm all the possible *benefits* that might be derived from this strategy – for the organization, customers in the segment(s) and other stakeholders. This also provides a framework for developing any necessary business case for supporting investment.

The next step is to identify all the *actions* that are critical to achieving success for the strategy, followed by identifying *enabling actions* – the other actions neces-

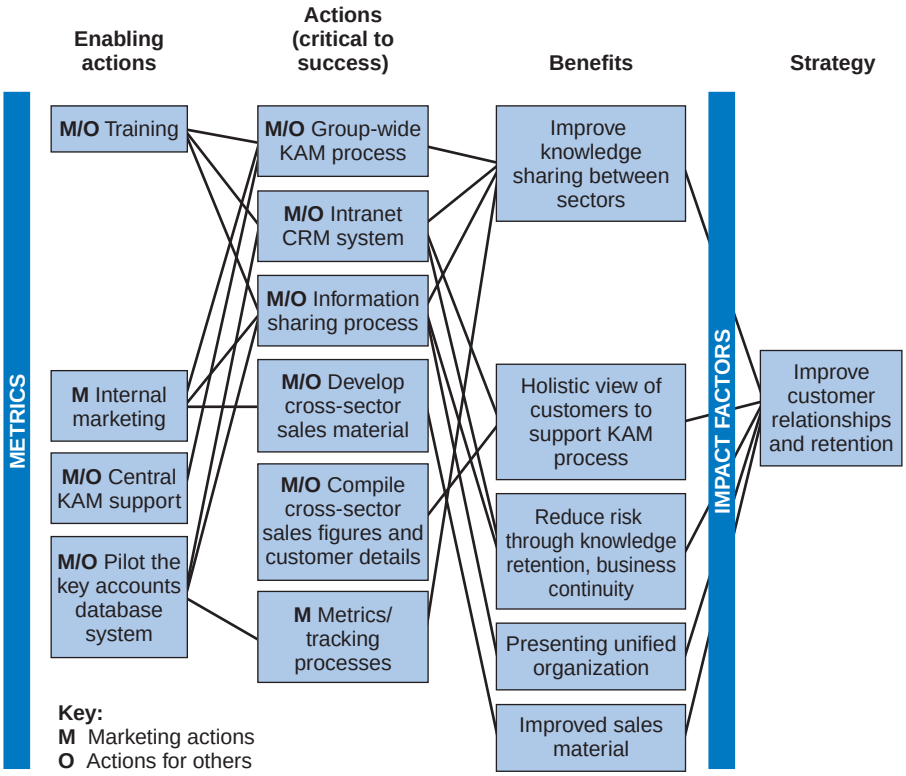


Figure 8.2 Using the Benefits Dependency Network to derive actions (key account management, global packaging manufacturer)

sary to ensure that those critical to success can be implemented. The last step is to finalize the *metrics* necessary to track progress.

In this particular example, the strategy was to improve relationships and retention with key customers, based on an analysis of customer needs. The goal was to provide competitive advantage in the market. One of the benefits identified was that the proposed strategy would enable current and potential customers to have a clear understanding of all that the company might have to offer them – and provide this in a consistent way at all touch points. A further key benefit would be improved knowledge management about customers and their needs. Finally, it was felt that the business risks faced by the company would be reduced, owing to improved market knowledge and increased retention of existing customers.

Actions critical to success included a unified process for handling key accounts, compiling holistic data about customers and sales, new sales support literature, and developing a measurement process. A key investment would be in a new intranet system to be developed by IT to a specification developed by marketing plus input from other areas, such as sales. All of these actions would require significant support or collaboration with areas outside of marketing. A metrics process was also identified as a key action for marketing to track progress.

The key actions could be delivered only if a number of enabling actions were also put in place, such as appropriate training programmes (in association with human resources), support to enable the key account process to be embedded across the organization, internal marketing to 'sell' the new strategy to employees, and a pilot to test the proposed intranet system (to be developed by IT).

The process used to apply the BDN process was initially a one-day workshop, including key people from outside marketing, followed up with a detailed plan refined through further discussion across the company.

As a result of using the BDN process, the company realized that the current system was inappropriate for meeting the key account goals. The process identified the need for a more user-friendly intranet-based product, which was subsequently developed and implemented. In addition, by using the BDN process, those responsible for the necessary key actions could be readily identified. Collaboration was enhanced by ensuring that all the key parts of the company were involved in the discussions.

In the organization concerned, the key members of an implementation team were identified as needing to be:

- a sales director representing one of the main market sectors;
- an executive sponsor;
- an IT/data strategist;
- a member of the sales team;
- a project manager.

Organizations within the Cranfield Key Account Management Research Club (Mouncey, McDonald and Ryals, 2004) confirmed that the key benefits of using the BDN model were:

- *economic* – establishing whether, and where, the project will add value;
- *political* – obtaining funds, winning hearts and minds;
- *change management* – early identification of issues (eg feasibility, desirability, resources, ownership, organizational impact);
- *control* – establishing project measurement criteria (eg benefits, costs, resources, etc).

> The BDN helped us work through the requirements needed to implement a new system that was more appropriate to our business than the previous one. Looking at the objectives first and working through the benefits and the requirements in detail was very beneficial. Looking at the graphical representation helped to visualize and work through some of the changes required.
>
> *(Global manufacturer)*

> It enabled us to understand better what we were actually trying to achieve.
>
> *(Global information company)*

8.1.2 Capturing actions, metrics and costs

Table 8.1 shows the template that can be used to capture all the marketing actions necessary to achieve each of the competitive advantage factors identified in the impact analysis. This template captures for each action:

- who is responsible for that action within the marketing team;
- the metric(s) that will be used to track the impact of the action;
- how frequently the action needs to be measured;
- who will be responsible for undertaking the measurement;
- who will see the metric(s);
- the likely cost of each marketing action.

Table 8.2 shows a similar template for capturing the information about the other actions that will be necessary outside the marketing team. The example included is the action on IT to build the website as specified in the brief prepared by marketing shown in Table 8.1. The key issue here is to ensure that the template captures all the necessary actions required from other parts of the company and is therefore completed with input from all concerned.

Templates similar to Tables 8.1 and 8.2 will need to be completed for qualifying and productivity factors.

8.1.3 Analysing actions by strategy

In Chapter 7, an alternative analysis format for impact factors by strategy was described in section 7.5 and illustrated in Table 7.4. Table 8.3 is the template that should be used for capturing actions if this version of the model is being applied. This captures the marketing and other strategies necessary for all appropriate qualifying, competitive advantage and productivity factors for the strategy. The example combines the factors analysis shown in Table 7.4 for enhancing the service provided by the call centre and the actions shown in Tables 8.1 and 8.2 for developing a website to help achieve an overall strategy, 'Provide "best in class" customer service'.

8.2 Developing the budget

By budget, we mean the allocation of resources. This is an *input* to marketing activity. We don't mean the sales forecast, as this is an *output* metric. Unfortunately, the same term is often applied to both of these, when in fact they are radically different.

In many organizations the annual round of budget planning starts with what was spent last year, therefore leading to a repetition of the same round of activity, which over time can become increasingly divorced from the real needs of the business. We would argue that this is not the best way to address the future needs of a busi-

Table 8.1 Marketing actions template (competitive advantage factors)

Action	Who responsible	Metric	Frequency	Who measures	Who sees output	Cost £
CAF 1 24/7 website						
Develop website specification	Manager customer communications	Meets customer needs	Three measures: • Inception of project • After initial design • After final version	Market research dept	• Website development team	£5,000
Launch e-mail to customers	Manager customer communications	• Awareness • Website usage	• Monthly survey of customers • Daily	• Market research dept • Customer service team	• Marketing director • Marketing and customer service teams	£10,000
CAF 2						

Table 8.2 Other actions template (competitive advantage factors)

Action	Who responsible	Metric	Frequency	Who measures	Who sees output	Cost £
CAF 1 24/7 website						
Build website	IT	• Critical path in the brief • Budget	Monthly updates	Marketing and IT	• Marketing and IT Directors • Manager customer communications • Development team • Marketing/IT finance managers	To be agreed
CAF 2						
CAF 3						

Table 8.3 Summary of actions by strategy

Strategy: Provide 'best in class' customer service

Actions	Who responsible	Metric	Frequency	Who measures	Who sees output	Cost £
Marketing actions Develop website spec. Develop brief for 24/7 enhanced phone service (answered in 6 rings, 60% queries answered during call)	1 Manager marketing ops	1 2	1 2	1 2	1 2	1 2
Other actions Develop website Develop plan to enhance contact centre	3 Manager customer services	3 2	3 2	3 2	3 2	3 2
Total (£)						

Key:
1: see Table 8.1 for details
2: see Table 7.4 for details
3: see Table 8.2 for details

ness in today's highly competitive markets – and this is not the way that is proposed within the Metrics model.

However, we also recognize that users of the model may have to apply it within the conventions used by their organizations. So, whilst the model does not absolutely require that budgets be structured differently, we advocate a structure that enables the resources necessary to achieve defined objectives to be identified, in other words the resources necessary for implementing the actions for each segment identified by applying the model, as described in the previous sections of this chapter.

The budget should therefore be structured according to the impact factors that the action is designed to address. They would be quantified by building up a picture of the action required to implement each strategy.

This approach that we describe is very different from traditional practices. It begins the process of tracking the *links* between the *use* of resources and the *effect* they will produce in the marketplace. This is in effect a zero-based or activity-based approach where the resources needed to achieve a specific goal are identified as the budget, rather than starting from the expenditure in the previous cycle. Budget categories are then defined by groups of actions, ideally according to the impact factor they are designed to address. Categories need to be reassessed annually: some will continue from one year to the next and others will not. This alone will be valuable in helping to break away from established practices unrelated to achieving precise goals.

If an activity-based approach is introduced, the agenda for the company, and the likely resources that need to be deployed to achieve goals, will become much clearer, both in terms of what *should* be the result if strategy is actioned, and also in terms of what will *not* be achieved if resources are not allocated to facilitate defined strategy. It will also make it easier to link the marketing budget with the budgets of other functions, which should also show resources allocated to those of their actions that are directed at specific impact factors. In addition, taking this 'bottom-up' approach to defining resource needs and assembling budgets, linked to achieving specific goals, should enable the marketing team to engage more effec-

profits. The number of brand attributes at play and the way in which emotional and functional attributes are interrelated make this assessment complex. However, in order to simplify this complex process you can develop a brand equity measurement system that isolates and analyses the attributes that explain changes in propensity and helps predict future financial behaviour.

An example of a brand equity measurement system is Brand Finance's Brand Value Added® (BVA®) drivers of demand analysis, which reveal the major drivers of demand and a brand's performance relative to that of competitors against each driver. The analysis is divided into two areas: 1) driver importance/brand contribution; and 2) driver performance/sensitivity.

Driver importance/brand contribution involves identifying the key drivers of demand by different segments and determining the brand contribution to each driver. This helps brand managers answer the following questions:

- Which drivers have most influence on overall 'brand preference'?
- Which ones can we influence?
- Where should we focus our communication?
- What brand image adds to the business?
- What is the argument for additional investment in the brand?
- Where does image have a strong influence and where should the organization focus?

Driver performance/sensitivity involves determining how a brand performs compared to competitors on key drivers of demand and determining the elasticity of each attribute. This helps brand managers answer the following questions:

- Where are we performing poorly against competitors?
- What should we emphasize?
- Where do we need to improve?
- How can we understand the impact of changing the customer rating on a particular attribute on overall 'brand preference'?
- What is the sensitivity of changes in customer behaviour (and hence business performance) to changes in brand preference?

Based on this analysis you can determine the elasticity of changes in brand preference and changes in customer defection and acquisition, which will ultimately influence the financial performance of the branded business.

Case study 12.1: Hovis – leveraging off historical 'brand equity'

In 1886, Richard 'Stoney' Smith invented a way of retaining wheatgerm in flour. In 1887 the brand was created in a newspaper competition, in which a student called Herbert Grimes won a £25 prize for the best name – Hovis, which he derived from the Latin phrase *hominis vis* (strength of man). In 1987 Hovis became the first major brand to be valued in the Rank Hovis McDougall takeover defence against GFW of Australia. This started an international debate about accounting for brands.

In 2000 Hovis was owned by Doughty Hanson, a private equity company. Hovis had operated for 115 years as the quintessential wholemeal loaf, but now operated in the £1-billion-plus wrapped-bread market. But the problem was that the market segment was declining and the Hovis brand was becoming a 'loss leader' for retailers.

Everybody still loved the Hovis brand, but it was too strongly associated with the traditional wholemeal (brown) product. Consumers were being driven to buy other bread brands such as Kingsmill or Warburtons, as they supplied both white and brown bread.

To escape declining growth, Hovis decided to relaunch by going back to the brand's foundations and leveraging off its historical brand equity as the experts in delicious, high-quality, everyday bakery products that are all good for you.

With 53 per cent of its success attributable to econometric modelling work, Hovis relaunched with new packaging. In addition, it developed a new innovative product, Hovis 'Best of Both' – 'soft white bread, with all the natural goodness of brown'. Hovis 'Best of Both' re-engineered category value by adding genuine value for consumers and provided them with a real reason to buy Hovis.

As a result of leveraging off their historical 'brand equity', Hovis's wrapped-bread category increased by over 32 per cent. Every £1 spent generated £1.67 extra profit. Sales rose from £150 million in 2002 to £285 million in 2005. The financial value of the Hovis brand increased by over 31 per cent in the first year and 60 per cent after two years.

12.4.3 Value mapping

It is vital not only to have an understanding of the drivers of value amongst all the stakeholder groups of a business but also to have a sufficient understanding of where value is being created in the entire value chain of the branded business. In order to help understand this you can undertake a value mapping study. Value mapping is a process of developing a thorough understanding of the key resources

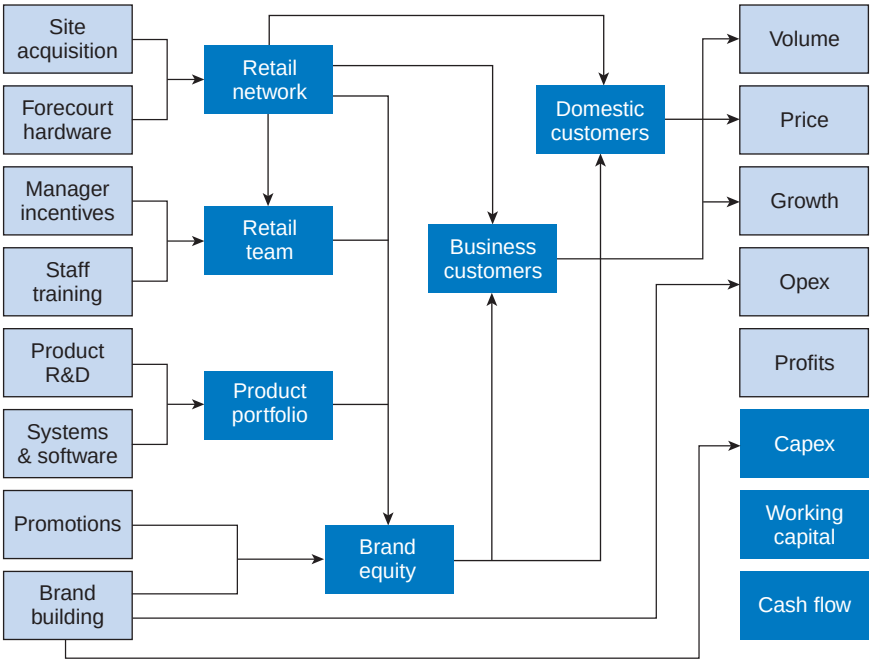
and assets in the business together with an appreciation of the linkages between these through the business value chain.

Value mapping is based on data collected during the brand audit and management and/or other stakeholder interviews. From these data the project team will establish a value map of the business, which should be presented in a conceptual framework highlighting what it is that key resources and assets of the branded business are driving, for example volume, price or the growth of the entire business (Figure 12.6).

Value mapping becomes an excellent tool at the start of any valuation to identify key tangible and intangible assets in the business and ultimately guides the valuation, scorecard and/or dynamic modelling process.

12.4.4 Brand valuation and sensitivity analysis

The brand audit, brand equity measurement analysis and value mapping analysis provide in-depth insights into the entire branded business, from which valid assumptions can be made in the brand valuation model. A brand valuation model is a framework that allows for optimal resource allocation and strategy selection across all market segments.



Source: Brand Finance plc, 2008

Figure 12.6 Brand value mapping (retail fuel)

There are two critical questions to answer in brand valuation. The first is: exactly what is being valued? Are we valuing the trademarks, the brand or the branded business? The second important question is: what is the purpose of the valuation?

An important distinction can be made between technical and commercial valuations. Technical valuations are generally conducted for balance sheet reporting, tax planning, litigation, securitization, licensing, mergers and acquisitions and investor relations purposes. They focus on giving a point-in-time valuation that represents the value of the trademarks or of the brand as defined above. Commercial valuations are used for the purposes of brand architecture, portfolio management, market strategy, budget allocation and brand scorecards. Such valuations are based on a dynamic model of the branded business and aim to measure the role played by the brand in influencing the key variables in the model.

We recommend that the starting-point for every valuation – whether technical or commercial – should be a branded business valuation. This provides the most complete understanding of the commercial context of the brand. A branded business valuation is based on a discounted cash flow analysis of future earnings for that business discounted at the appropriate cost of capital. The value of the branded business is made up of a number of tangible and intangible assets. Trademarks are simply one of these, and 'brands' are a more comprehensive bundle of trademark and related intangibles.

There are a number of recognized methods for valuing trademarks or brands as defined here.

You can look at historic costs – what did it cost to create? In the case of a brand you can look at what it cost to design, register and promote the trademarks and associated rights. Alternatively, you can address what they might cost to replace. Both the historic cost method and the replacement cost method are subjective, but we are often asked to value this way because courts may want to know what a brand might cost to create.

It is also possible to consider market value, though frequently there is no market value for intangibles, particularly trademarks and brands.

Generally speaking the most productive approach to brand valuation is to employ an 'economic use' valuation method, of which there are a number.

First, there is the price premium or gross margin approach, which considers price premiums or superior margins against a 'generic' business as the metric for quantifying the value that the 'brand' contributes. However, the rise of the private label means that it is often hard to identify a 'generic' against which the price or margin differential should be measured.

Economic substitution analysis is another approach – if we didn't have that trademark or brand, what would the financial performance of the branded business be? How would the volumes, values and costs change? The problem with this approach is that it relies on subjective judgements as to what the alternative substitute might be.

The difficulties associated with these two approaches mean that the two most useful 'economic use' approaches are the 'earnings split' and 'royalty relief' approaches.

Under a 'royalty relief' approach you imagine that the business does not own its trademarks but licenses them from another business at a market rate. The royalty rate is usually expressed as a percentage of sales. This is the most frequently used method of valuation because it is highly regarded by tax authorities and courts, largely because there are a lot of comparable licensing agreements in the public domain. It is relatively easy to calculate a specific percentage that might be paid to the trademark or 'brand' owner.

Under an 'earnings split' approach you attribute earnings above a break-even economic return to the intangible capital. This involves four principal steps. The first is an appropriate segmentation of the market to ensure that we study the brand within its relevant competitive framework. The second step is to forecast the economic earnings of the branded business earnings within each of the identified segments. These are the excess earnings attributable to all the intangible assets of the business. The third step is to analyse the business drivers research to determine what proportion of total branded business earnings may be attributed specifically to the brand. The final step is to determine an appropriate discount rate based on the quality and security of the brand franchise with both trade customers and end consumers.

Regardless of which method is used, the valuation usually will require a sensitivity analysis in which one flexes each of the assumptions made in the analysis one at a time to demonstrate the impact changes in each variable have on the overall valuation. However, this is a simple mechanical exercise intended to show which assumptions the valuation is most sensitive to. The valuer's dilemma lies in trying to determine which of the key assumptions is most likely to change and how, which is where all the brand audit data and brand equity measures become significant.

In our experience, it is very important to express the final valuation number in context. This means explaining exactly what has been valued, using what method, and what the key insights are as to the influence of the brand on the key operating variables of the business. This emphasizes the importance of developing a valuation model that is presented in a user-friendly manner to help management make crucial decisions around marketing and branding strategy objectively and with a high degree of financial rigour.

One way in which you can effectively express a valuation model in a simple format to help answer key marketing and branding investment decisions is a brand scorecard.

12.4.5 Brand scorecards

Marketers are increasingly being challenged by their boards and chief financial officers to answer key questions:

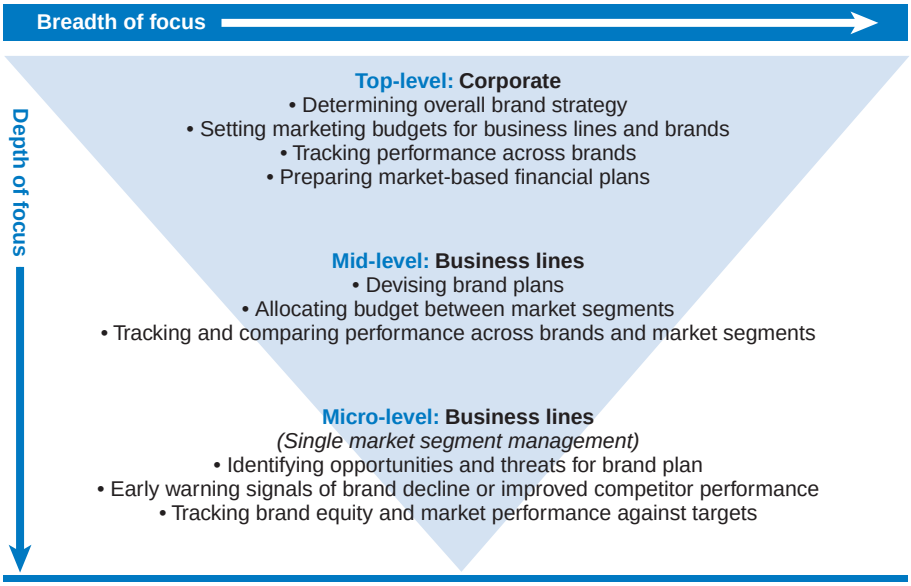
- How much should we invest in marketing and branding?
- Which markets, customers, brands and channels will generate the highest return?
- Which strategy will generate the greatest value?
- How are our brands performing relative to competitors and targets?

In order to answer these vital investment decision questions, brand managers should consider developing brand scorecards to inform brand management decisions before the finance department does it for them.

The success of a brand scorecard relies on the synergy between financial, market and customer analytical data. This integration of data allows organizations to gain greater commercial insight, improvements in the collection and utilization of data, and better value from data held in silos.

All relevant data collected from the brand audit, brand equity analysis and value mapping analysis and brand valuation are fed into the building of the scorecard.

The development of the scorecard is dependent on who will be predominantly using it. As you can see from Figure 12.7, different management levels will use the scorecard for different purposes. As a result it becomes imperative that all relevant stakeholders that will be involved in using the scorecard are identified to ensure it is tailored accordingly and includes the brand metrics. In addition, you will need to identify what resources are required to build and maintain the scorecard and which audiences will be tracked.



Source: Brand Finance plc, 2008

Figure 12.7 Users of the brand scorecard

Typically there are four main components included in a brand scorecard. First, there is the top-level dashboard, which provides an in-depth summary of financial and brand health trends. It acts as a traffic-light system alerting the relevant users of the scorecard to any threats and opportunities that may become apparent in the present marketplace.

Second, there is the competitive benchmarking component. This consists of numerous charts and data tables that will provide the user with an in-depth tracking of competitive performance over time. Based on this analysis, brand managers are able to make more informed decisions.

Third, there is the brand valuation model component (Figure 12.8). This will track value changes over time, as well as reflecting the expected impact of different strategies on the value of the branded business. For example, hypothetically in the telecommunication industry you will be able to determine the expected increase in mobile phone subscriber value to the branded business as a result of rebranding.

Last, there is the statistical analysis component of a brand scorecard. This involves quantifying the relationship between marketing activities, brand equity and market performance. This analysis provides the brand manager with a significant amount of valuable relationships that can form the basis of assumptions driving marketing and branding decisions.

These four components provide a holistic perspective of the branded business by connecting the relevant marketing metrics to financials. This allows for an optimal brand investment analysis together with a dynamic scenario analysis of best-case and target scenarios to be conducted.

The scorecard is ultimately linked into the business processes to ensure that it becomes essential and actionable. It can then be used to drive decisions relating to:

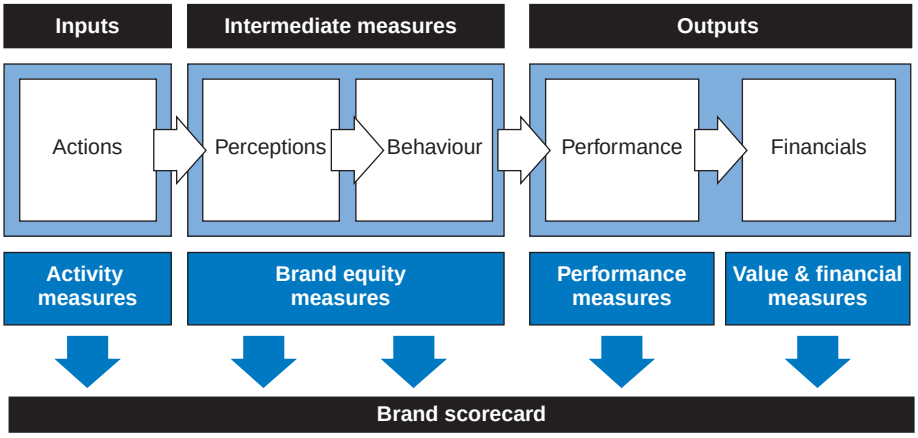


Figure 12.8 Components of a brand scorecard

- *business performance*, which includes investment and priority decisions;
- *personal performance*, which includes linking manager and team objectives, key performance indicators and reviews and compensation;
- *share performance*, which involves the inclusion of marketing as part of analyst briefings and annual reports;
- *brand performance*, which includes improving strategy and planning, performance tracking and marketing accountability.

An example of a completed brand scorecard is shown in Figure 12.9.

Another effective manner in which brand/marketing managers can determine the relevant amount of investment required to achieve optimal marketing return on investment is through a statistical analysis called marketing mix modelling.

12.4.6 Marketing mix modelling

Marketing mix modelling is a statistical analysis to isolate and quantify the impact of different marketing activities. It is a model that guides the mix and combination of future marketing activities, making it a highly complex analysis that cannot be fully covered in depth in this chapter.

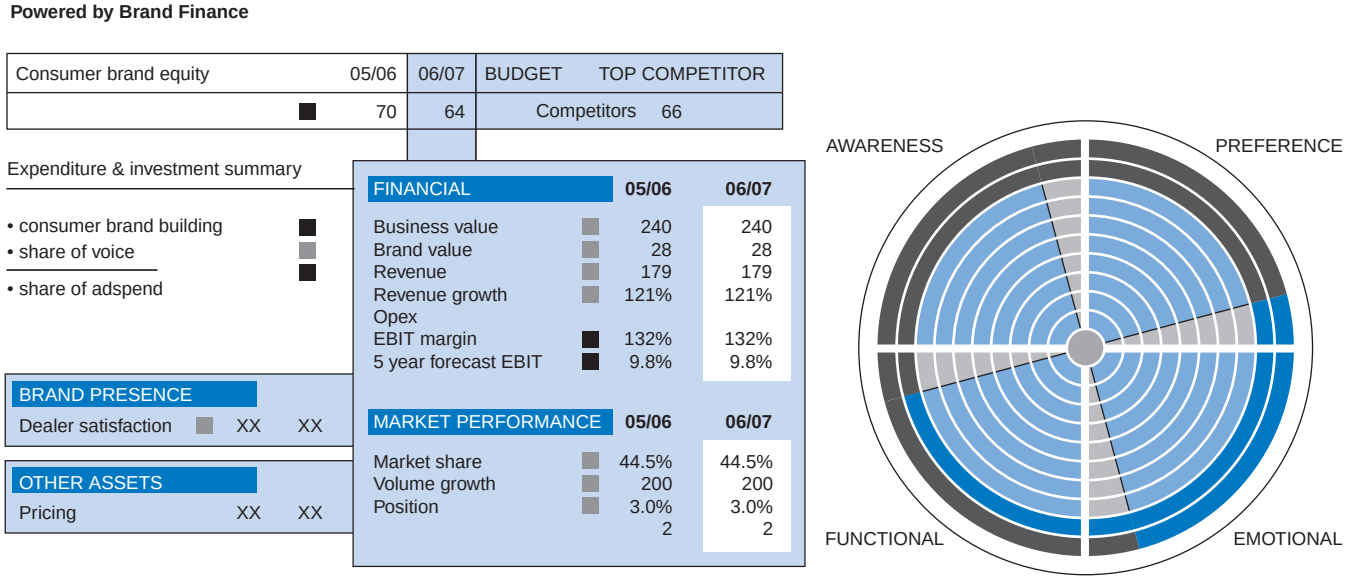
The model can be developed only if there is an understanding of what the sales and profit objectives to be achieved by the marketing department in the financial year are. These objectives should be based in terms of customers, average transaction value, frequency, penetration rates and product range. The objectives will form the basis of determining the optimal marketing budget using a demand driver approach.

The demand driver approach requires you:

1. to know the product sales potential by customer segment;
2. to know the bottlenecks preventing increased product penetration;
3. to know the impacts and returns from differing marketing levers;
4. to use the most cost-effective communication channels for the task.

All these four steps will require a thorough econometric analysis into the most effective marketing activities to achieve the required objectives.

In order to determine the relevant payback of each activity the model will identify the difference between strategic and tactical marketing spend. Strategic marketing spend is geared to supporting long-term brand values such as image and awareness and covers a payback period of approximately three years, which gives a reason for consumers to buy a brand – a ‘pull’ strategy. In contrast, a tactical marketing spend is targeted to stimulate immediate sales promotions and distribution drives with a payback period of around 12 months, which gives the consumer an incentive to buy – a ‘push’ strategy. Often you will find that not all marketing spend is strategic, but all of it needs to pay back at some point.



Source: Brand Finance plc, 2008

Figure 12.9 An example of a brand scorecard

Completion of the model will help improve brand and marketing managers' understanding of factors that influence short-term sales. It should also provide them with strategic insights that will shape overall business planning as the external environment changes and evolves, as well as providing key insights and understanding of why campaigns perform better in some situations than others.

It is often useful to flex all valuation models in order to determine the effect of varying brand strategies on financial performance.

12.4.7 Dynamic scenario analysis

The word 'scenario' is a literary term meaning 'an outline of the plot of a dramatic or literary work'. While a literary scenario might be credible, it is inevitably imaginary, and there may be alternative plots or sub-plots. Brand planning can be much the same.

The original literary term has been adapted by commerce to describe 'a possible set of future events', 'an outline or model of an expected or supposed sequence of events' or 'a postulated sequence of possible events'. Because all scenarios describe the future they are inevitably hypothetical and uncertain. Some postulated scenarios may be quite implausible. To be taken seriously they must be logical, internally consistent and credible.

In Michael Porter's words a scenario is 'an internally consistent view of what the future might turn out to be – not a forecast, but one possible future'. Therefore, when one talks about scenario analysis it involves an in-depth evaluation into the future possibilities of a brand, which can be derived from flexing a valuation model in order to estimate the impact of alternative strategies on business value and brand value. As a result of such an analysis, a brand or marketing manager will be able to assess the short-term profit and long-term value implications of a range of potential strategies.

Scenario analysis forms a pertinent part of brand managers' responsibility. The credibility of a brand scenario needs to be explored and tested using consumer and trade research and market, marketing and financial due diligence. If deemed consistent and credible the value impact can be tested with a brand valuation model. If the new scenario implies that greater value will be created through it than through the pre-existing scenario then it should be actively pursued. This can be demonstrated in a case study of the brand Courvoisier.

Case study 12.2: Courvoisier – scenario debate

In 1999 there was a debate within the global brand management group in Allied Domecq as to whether the Courvoisier brand should be classified as a 'core' brand or whether it should be divested, given its poor financial performance and declining net present value (NPV). The problem was that

the previously preferred scenario for the Courvoisier brand, which was based on high-end cognac product sold to high-net-worth individuals in Asia, Europe and the East Coast of the United States using traditional marketing and distribution at a premium price, wasn't working. Given the high cost of production, high stockholding costs and the low rate of sale the brand had a low and declining NPV.

Market research indicated that lower-end cognac, sold with contemporary marketing techniques in different bottle sizes to mid-market ethnic consumers in the heartland of the United States, would radically change the value of the brand.

The two scenarios were modelled, and the latter approach indicated a higher level of profits and cash flows, with lower capital investment and a faster rate of sale. Variables were flexed, but even allowing for changed assumptions the net present values of the two scenarios were quite different. This led to a change in brand strategy and a rapid improvement in financial performance of the Courvoisier brand. In the recent acquisition of Allied Domecq's brand portfolio by Pernod Ricard, Courvoisier was referred to as a key brand.

In this example the two scenarios for Courvoisier implied radically different capital values for the brand, the higher of which was actually realized when the altered scenario was implemented.

12.5 Conclusion: financial implications for brands

This chapter has described the process for identifying branded business value and the specific value of intangible assets including trademarks or brands. While it is important to know the financial value of a trademark or brand within a branded business, the most important thing to know is the value of the branded business as a whole and how it can be maximized.

The 'brand valuation' framework described indicates how to understand the impact of each audience on the financial model, and how to map value, track brand equity, report performance to managers via scorecards and then plan business and brand value enhancement strategies using all the information. The approach is holistic because it incorporates both marketing and financial measures, all stakeholder audiences and both short- and long-term perspectives. It is both a historical measure of performance and a prediction of future performance.

In our view this all-encompassing framework is a vital tool for brand managers. It empowers them to manage their brands just as CEOs manage the wider business. In fact, brand managers who have trained and operated with such accountable and strategic measurement frameworks have a higher-than-average propensity to become CEOs!

Any questions relating to the methodologies outlined in this chapter should be directed to d.haigh@brandfinance.com. Brand Finance plc is one of the world's best-known and longest-standing organizations specializing in the valuation of brands.

Appendix

Econometrics

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Business Economics Limited

A.1 What is econometrics?

Econometrics is the application of statistical techniques to the study of economic relationships. It uses data to quantify the relationship between a set of variables that describe an economic system. Econometrics is a widely used technique across a range of businesses. In particular, it is used as an aid to decision making in marketing, where it provides the methodology for marketers to make predictions about the impact of marketing activity on a company's sales, profitability and shareholder value.

A.2 How is econometrics carried out?

In our experience, many organizations collect substantial amounts of data about their business – often at considerable expense – but these data are not always analysed fully and consequently do not play their full role in informing business decisions. Econometrics is one technique that can assist evidence-based decision making.

At heart, the concept is simple. Econometrics allows you to test which variables (called 'independent variables' or 'drivers') have a significant effect on a variable in which you are interested (called the 'dependent variable'). For example, the dependent variable may be sales volume, and the independent variables may include price, advertising, bank holidays, the weather, competitor prices, competitor advertising, public relations events, economic indicators, etc.

Not only is econometric analysis able to tell you which of a long list of possible drivers is important and which is unimportant, but for those that are important it is able to quantify the magnitude of their impact on the dependent variable in which

you are interested. This ability to select the significant variables and to quantify the magnitude of their impact enables a predictive model to be constructed. This can then be used to explore scenarios for various decisions that can be made by the business and sensitivities to external factors beyond the control of the business.

In order to do its work, an econometric analysis needs to look at variations in the dependent and independent variables. Unlike the case with other types of statistical analysis, these variations are not usually planned as controlled experiments in an econometric analysis but just happen as a result of changing circumstances and the reactions of the business to the environment in which it operates. The types of variation that are analysed fall into two main categories: 1) variations over time (called 'time-series analysis'); and 2) variations at a point in time between different groups or categories (called 'cross-sectional analysis'). These two forms of variation can, of course, be combined in a single analysis, sometimes called 'panel data analysis'.

Although powerful and widely used, econometrics is a specialist subject. Large organizations may well have a dedicated in-house team to carry out econometric analyses. Smaller organizations usually outsource this type of analysis to consultancy firms.

There are a number of other techniques that marketers can use to quantify the impact of their activities, in addition, or as an alternative, to econometrics. These include conjoint or 'trade-off' analysis, which interprets market research on how consumers value various product or service attributes, including price; statistical control experiments where comparisons are made between the behaviour of consumers, some of whom have been exposed to a marketing stimulus and others who have not; and judgemental modelling techniques, which rely on management and expert experience to quantify key marketing relationships.

A.3 Examples of what econometrics can do

Econometrics is of interest to business in general and marketing in particular because it provides a rational and often insightful framework for decision making. A few examples of marketing issues on which it is frequently applied are:

- demand forecasting;
- evaluating the effectiveness of advertising, promotions and other marketing activities;
- identifying key drivers of market changes and trends;
- quantifying price sensitivities;
- identifying and quantifying the impact of competitor behaviours.

A number of detailed statistical tests are available to test the validity and reliability of an econometric model in order to have confidence that it can be used as a reliable basis for planning and decision making. In addition, however, we can look at how well the model is able to describe the existing data. A typical comparison between the model predictions and actual sales volumes is shown in Figure A.1.

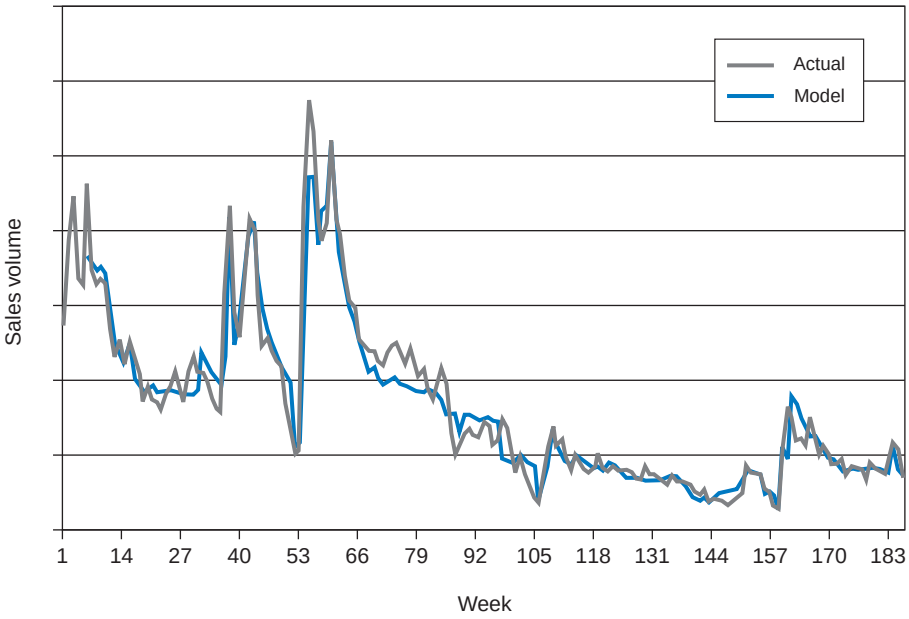

Figure A.1 Actual sales compared to model predictions

However, econometrics can do more than just provide an equation that can be validated against historic data and used to prepare estimates for the future. It can also break out the various factors that have contributed to variations in the past and thereby provide insights and understanding. A simple example in which sales are broken down between base demand, demand created by TV advertising and demand created by direct mail is shown in Figure A.2. This shows the extent to which TV advertising and direct mail campaigns have contributed to sales over the period.

A.4 Summary and conclusions

Econometrics is a powerful technique that is able to inform business decisions by providing evidence-based analysis. The analytical techniques required are specialized but, even so, are widely used because of the insights that they are able to provide. Of course, in order to deliver robust conclusions, econometric analysis relies on good data being available. Often the data are available but, when this is not the case, asking what data would be needed for an econometric analysis can be a valuable prompt for improved data capture.

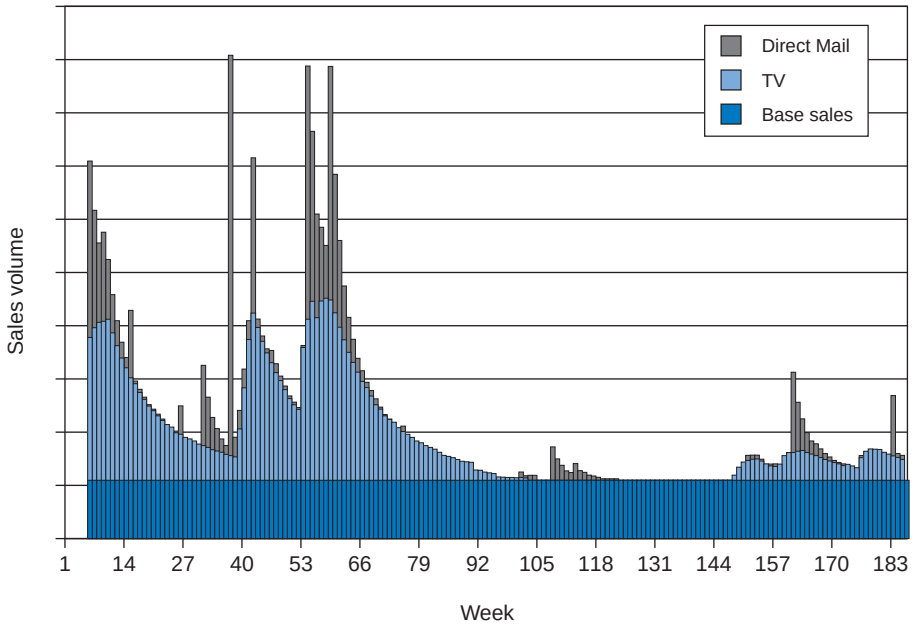

Figure A.2 Impact of promotional activity on demand

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