

7.4: Return on Investment (ROI)

Learning Objectives

After studying this section, students should be able to do the following:

1. *Define* and *evaluate* return on investment (ROI).
2. *Explain* why return on investment (ROI) can make advertising accountable.
3. *List* and *discuss* the keys to using return on investment (ROI) successfully in the pursuit of profit and channel effectiveness.

Did You Get What You Paid For?

Return on investment is the amount of profit an investment generates. In other words, did your action result in more (or less) than what it cost to implement? The ROI approach to budgeting looks at advertisement as an investment, not a cost. And like any investment, the company expects a good financial return on that investment. By making the investment in advertising, the company expects to see profits from that investment.

The idea behind ROI is that for every dollar you spend on advertising, you get a dollar-plus-something of profit in return. The challenge with ROI is that it's difficult to interpret and analyze the contribution of a specific ad, media channel, or campaign to overall profit. Is the profit coming from a short-term sales blip or is it contributing to longer-term profits?

$$\frac{(\text{gross profit generated by advertising} - \text{cost of advertising})}{\text{Cost of advertising}} = \text{ROI}$$

$$\frac{(\$3,000,000 - \$800,000)}{\$800,000} = 275\%$$

Figure 7.6 ROI is a way to determine the sales generated from advertising relative to the cost of the advertising.

Why ROI Is Important

ROI is the language of business. Although many marketing people traditionally evaluate a campaign's success in terms of intangibles like brand awareness, top management insists on more tangible results: ka-ching! Advertisers face increasing pressure to translate the results of what they do into ROI terms. If they succeed, they can assure the bean counters that if they're given a certain amount of budget, they will earn the company x percent more. But it's not so easy to quantify the effects of ad messages, and it never has been. One well-known quote (so well known it's practically a cliché) that has at times been attributed to Henry Ford, retailing executive John Wanamaker, and others sums up this dilemma: "I know that half of my advertising works—I just don't know which half."

Dig Deeper

How many people watch TV commercials, and how effective are these spots in influencing actual purchases? These are vitally important questions—especially because the networks set their rates for advertising based upon how many people see their shows. To date there still is no foolproof way to deliver these **metrics**, and it's the source of a lot of controversy in the advertising industry.

The dominant measurement system is the Nielsen Television Ratings that the networks have relied upon since the earliest days of television. The Nielsen Company collects these measures by recruiting a panel of consumers who keep a diary of what they watch and by so-called set meters that it connects to members' TV sets to transmit data about which channels get selected. These methods suffer from obvious problems—for example, our memories about what we watch often are distorted and biased, and just because a set is tuned to a channel doesn't mean anyone is actually watching. Nielsen is working hard to update its technology with People Meters that individual members of the household use to record their viewing behaviors. GfK AG's Mediamark Research Inc. also is developing a pager-size media-measurement device. And, to keep pace with consumers' changing habits, Nielsen has started to measure out-of-home viewing (in bars, dorms, and other locations) as well as the usage of digital video recordings like TiVo. Nielsen is also working on a new measurement system it calls Anytime Anywhere Media Measurement. This system will track a group of sample viewers—but it will monitor their usage of several different media including the Internet, mobile devices like iPods, and traditional television.

The company that comes up with a truly reliable system to measure how consumers interact with media (and the advertising they contain) will be worth its weight in gold. One new research firm called TRA (True ROI Accountability for Media) is trying another strategy: it merges data from people's cable set-top boxes with consumer-purchase databases, such as the information stores gather from frequent-shopper cards. For instance, a company could see whether households that watched an ad for its toothpaste later bought that brand of toothpaste. In a test of its system, TRA is using data from cable boxes to measure second-by-second viewership of TV programs and commercials in three hundred thousand households in Southern California, and it aims to sign up more than one million U.S. households across the country in the near future.

A different approach hopes to use cell phones to measure what consumers listen to and see. The startup firm Integrated Media Measurement Inc. has developed software that enables specially adapted cell phones to take samples of nearby sounds, which it then identifies by comparing these to a large database. The company claims that this technology can track exposure to television, radio, CDs, DVDs, video games, sporting events, audio and video on portable gadgets, and movies in theaters. These are some of the questions the company hopes to answer:

- How often are TV shows watched outside the home?
- Which songs prompt listeners to change radio stations?
- Which movie trailers get viewers to go to the theater?
- Which technology will prevail?

Stay tuned...

ROI Is the Real Goal (SOV Is Only the Means to an End)

At the end of the day, then, share of voice is only a means to the end. Ultimately, advertisers want consumers to purchase what they make, not just think their ads are awesome. If the money spent on advertising never generates any returns, then what is the point—other than to improve the bottom lines of ad agencies and enrich the portfolios of creative directors? As Gavin Ailes, business director at The Search Works in the United Kingdom, explained, if a company gets two dollars back for each dollar they invest, “that’s great, they shouldn’t really worry too much whether they have ‘share of voice’ or whatever among a particular group.”

ROI Makes Advertising Accountable

An Institute of Practitioners (IPA) report entitled *Marketing in the Era of Accountability* is based on the IPA's database of effectiveness awards case studies. The report found that advertising campaigns that set hard objectives, such as to “improve profits,” are more effective than those that focus on intermediate goals, such as degree of brand awareness. Fewer than 20 percent of companies evaluate their communications campaigns on the basis of their effect on profits, however, because it is easier to measure an intermediate metric than an ROI metric.

SS+K Spotlight

As msnbc.com set its goals for the branding campaign, the client had to identify what metrics (measures of effectiveness) would be most meaningful to their mission. All marketers ultimately aim to increase revenue for their business as a result of marketing efforts. Every element of a campaign has accountability to perform or meet that goal; otherwise it's not likely to appear again.

With the first round, msnbc.com decided to invest in some short-term vehicles—Web ads and click-through rates—to determine ROI. They also invested in some long-term vehicles such as the screensaver and the NewsBreaker online game we'll check out later.

Keys to Using ROI

Using ROI effectively depends on several factors, including visibility, the difference between revenue and profit, channel effectiveness, and taking a long-term perspective.

Visibility: Can You See the ROI?

Some firms are in the enviable position of seeing a return on their investment more directly than others. For example, Domino's Pizza can see the results of its advertising almost immediately—a TV ad immediately spurs calls to its outlets as people order the ExtravaganZZa Feast the spot featured. As the chain's marketing director explained, “The time it takes from initial consideration to consumption can be less than an hour. We can see the impact of a TV ad almost immediately.”

Online advertising is also amenable to rigorous ROI measures. Watching impressions, counting click-throughs, and using cookies let advertising managers know how many people saw an ad, clicked on the ad, and bought from the ad. Web traffic can be tracked, and advertising spending can be aligned to sales.

Dig Deeper

As difficult as the ROI of traditional advertising vehicles is to measure, word of mouth is even harder to measure. As online content chatter on blogs and Web sites continues to mushroom, advertisers need to measure just what consumers are saying about their products and how active they are in spreading the word about viral marketing campaigns or other online promotions. Buzz Metrics, a subsidiary of the Nielsen Company, offers marketers research services to help advertisers understand how CGM (consumer-generated media) affects their brands. Nielsen's Buzz Metrics search engines identify online word-of-mouth commentary and conversations to closely examine phrases, opinions, keywords, sentences, and images people use when they talk about a client's products. The company's processing programs then analyze vocabulary, language patterns, and phrasing to determine whether the comments are positive or negative and whether the authors are men, women, young, or old to more accurately measure buzz. BuzzMetrics' and BrandPulse reports tell advertisers who is talking about their products online and what they say about the ads they're seeing.

ROI Requires More Profit, Not Just More Revenue

Ideally, payback should be about profit, but many companies confuse added profit with added revenue. To avoid these mistakes, clothing manufacturer VF Corp (whose brands include Lee, Wrangler, Nautica, and The North Face, among others) spent two years and millions of dollars studying consumer responses to its marketing efforts while seeking to determine which of its brands have gotten the best ROI from advertising. "We are convinced we can be more effective by having a better understanding of marketing return on investment and will get paid back on our investment several times over," said Eric Wiseman, president/COO at VF.

In 2006, VF spent about \$325 million on advertising across all its brands. The Nautica brand is already reaping the benefits of VF's ROI research. The company increased Nautica's marketing budget the next year. "Our budget is up and we are moving the mix around," said Chris Fuentes, vice president of marketing at Nautica. "We've looked at each element of our marketing—magazines, newspaper, outdoor, sponsorship, public relations—[and] we can isolate what is working. We're understanding now what is driving consumption and building brand equity."

The research helped the company decide that Nautica's advertising budget should be increased because the advertising was providing a good return on investment. What's more, the research helped Nautica pinpoint which of its campaigns were most effective in bringing that return. Nautica is using that information to decide how to allocate its advertising budget. Nautica uses an integrated marketing program of print, outdoor, and Internet advertising. The research showed that newspaper ads generated underachieving results, so Nautica will spend less on them, but it will boost its Internet presence to target young men for its new N series jeans. Nautica spent \$20 million on ads in 2006.

ROI for Channel Effectiveness

ROI can also help manage an advertising campaign as effectiveness measures help identify which specific media platforms deliver the best bang for the buck. Nautica relies on its ROI research to drive budget allocation among different campaigns, allocating more to those that have provided the best return in the past. For example, Nautica's sponsorship of the AVP Pro Beach Volleyball Tour produced good results. So, in 2007, Nautica increased its presence there, adding on-court billboards and a scoreboard bug on the TV screen, and having announcers and pro Misty May outfitted in Nautica apparel.

Dig Deeper

One promotional channel that's been getting a lot more attention in recent years is **POP (point-of-purchase) advertising**—ad messages that shoppers see when they are physically located in a purchasing environment. Like traditional advertising, it's hard to determine how effective these messages are—though we know that in some categories (e.g., grocery) many shoppers don't make their final decisions until they're wheeling their carts through the aisles (never go food shopping when you're hungry!).

A major new initiative called P.R.I.S.M. (Pioneering Research for an In-Store Metric) is attempting to quantify the impact of these messages. Participating companies include Procter & Gamble, Coca-Cola, ConAgra, General Mills, Kroger, Walgreens, Wal-Mart, 3M, Walt Disney, Kellogg, Miller Brewing, and even Nintendo. Ad agencies OMD and Starcom MediaVest Group, as well as multiple retailers, are also involved. The measurement model predicts consumer reach by category or area of the store, by retail format, and by day of the week, delivering unprecedented insight into the store as a marketing channel.

The consortium's research team began working on the theory that, by predicting in-store traffic, then determining what marketing communications are in the store, it could calculate the "opportunities to see" a specific communication. By using existing statistical models that factor out duplicate impressions (accounting for multiple "visits" to the area by the same people) a measurement for consumer reach could be calculated for specific locations in the store. Initial tests have been promising. The CEO of Procter & Gamble recently predicted, "P.R.I.S.M. will transform how we think about in-store consumer communications and behavior."

Avoid Overemphasis on Short-Term ROI

Most advertising ROI metrics tend to focus on short-term profits from the immediate response to an ad. This emphasis is appropriate in some contexts; for example, that's one of the big advantages of direct marketing, because the firm can immediately trace the impact of a mailing or e-mail blast and decide right away if it boosted orders.

On the other hand, brand-building campaigns produce a low ROI in terms of short-term profits, but they are crucial for the long term. In these cases managers may need to adopt a broader field of vision and be patient, even if they are bleeding red right now. For example, one company discovered that every dollar the company spent on TV advertising yielded only eighty cents back in short-term sales. Executives were thinking of chopping the TV budget, but the general manager said, "Just because print and promotion activities have the highest ROI, doesn't mean they should get the majority of the money. Print only accounts for a small fraction of total sales, and while TV has a lower ROI, it's responsible for a huge amount of ongoing sales." This reasoning shows that the bigger picture must be taken into account when managers make budget decisions. Making this case can be a daunting task for advertising agencies, especially when their clients are under pressure to show profitable returns to their shareholders.

Key Takaway

At the end of the day, it's all about ROI. Ad agencies and other promotional companies are coming under increasing pressure to show specifically how their activities deliver value to the client—by quantifying how much financial return the client receives in exchange for the money it spends to advertise. Showing ROI is difficult when many campaigns are more about building long-term awareness and loyalty than prompting immediate purchases (sales promotions, online advertising, and direct marketing are better able to link specific messages to specific results). However, there is a silver lining: this greater discipline forces advertising agencies to be more accountable—and in the process perhaps change the mindset of managers who tend to view advertising as a cost they need to minimize rather than as an investment in the brand's performance.

EXERCISES

1. Explain the concept of return on investment (ROI) and its importance to the budgeting process.
2. Give two examples of how industry uses return on investment (ROI) to measure how consumers interact with media.
3. Explain how return on investment (ROI) makes advertising accountable.
4. List and describe four keys to using return on investment (ROI) successfully.

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