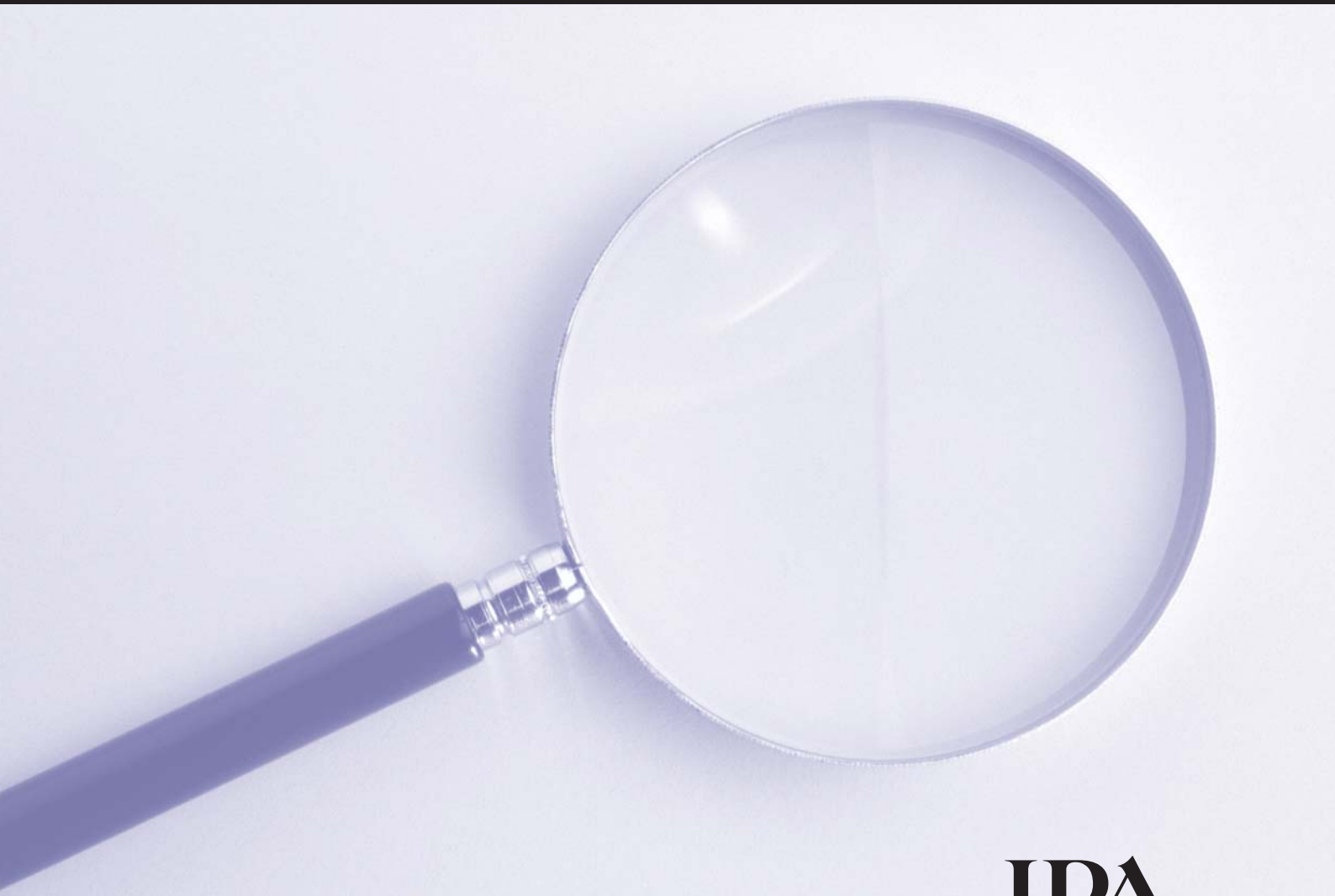
# KPIs for marketing reporting

## A framework for effective marketing disclosure



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# Foreword

Recent legislative changes to narrative reporting, introduced by the Companies Act 1985 and strengthened by its successor, the Companies Act 2006, are now having a significant impact on companies' annual reports. Disclosure requirements have become more demanding, and the response of companies correspondingly more focused.

Many reporters are still addressing one of the main changes introduced by regulation – the use of Key Performance Indicators (KPIs) to chart progress in achieving their strategy. Typically, of the five to eight KPIs a company selects for disclosure purposes, market practice suggests most will be reporting financial performance. The balance focus on non-financial issues, where the advice of the Association of British Insurers[1] emphasises the importance of disclosure based on material considerations, including the activities driving value in the company's operations.

Disclosure on marketing activity, for many companies, addresses both needs: the core purpose of marketing investment is to maintain and improve brand momentum in order to return a profit to shareholders. Yet marketing KPIs are, as yet, all but absent from the narrative reports and business reviews of FTSE 350 companies. This is despite the fact that brands form 12% of company market value on average, and a full 20% of intangible value[2].

This publication focuses on financial and non-financial KPIs for marketing investment. It aims to:

1. Demystify marketing metrics.
2. Give guidance on the metrics that matter most in the context of corporate reporting.
3. Provide a useful framework against which companies who invest in marketing can decide on the KPIs that are appropriate to them.

In addition, it proposes three changes to disclosure practice to ensure delivery of more transparent and effective reporting of marketing performance.

We hope it will help clarify the role for marketing reporting among all preparers of narrative reports, put effective marketing disclosure on the boardroom agenda, and position IPA member agencies as willing allies and advocates of this process.

**Moray MacLennan**
**IPA President and**
**Chairman Europe, M&C Saatchi**

[1] Developments in Narrative Reporting: An ABI Position paper 2006
[2] Brand Finance; Global Intangible Tracker (GIT TM) 2006

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The IPA is also grateful to those industry thought leaders who have found the time to comment on drafts along the way, and help refine thinking. Particular mention should go to Les Binet *(DDB Matrix)*, Martin Deboo *(Investec)*, Peter Field *(marketing consultant)*, Seamus Gillen *(Value Alpha)*, Alex Hunter *(IPA)*, Gurdeep Puri *(Leo Burnett)*, Richard Warren *(Delaney Lund Knox Warren)* and Karl Weaver *(Data2Decisions)*.

In addition, four publications have guided our thinking:

*Marketing in the Era of Accountability,* Les Binet and Peter Field
(IPA/WARC, 2007)

*Marketing Payback: Is your marketing profitable?,* Robert Shaw and David Merrick
(Pearson Education Limited, 2005)

*Marketing and the Bottom Line,* Tim Ambler
(Pearson Education Limited, 2000)

*Value Based Marketing,* Peter Doyle
(Wiley, 2000)

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# Management summary

- There are signs that **appetite for marketing information is growing**, particularly among larger long-term investors and their equity analysts.

- Although marketing is recognised by shareholders to be an inexact science, companies still need to demonstrate that they are managing their marketing activities responsibly and professionally, with **appropriate assessment of risk and reward** for every decision that is taken.

- However, there appears to be a mismatch between the **bottom-up data needs of campaign managers in marketing**, who are seeking to optimise individual brand campaigns, and the **top-down data needs of the chief financial officer, and CEO**.

- This document seeks to remedy that situation by applying learning about the metrics that matter, from general industry learning and new analysis of the **IPA dataBANK** of best practice cases in effectiveness.

- It argues that in order to define a relevant set of KPIs for marketing it is important to first set an **appropriate strategic framework**.

- It demonstrates that marketing success is a function of the following **value chain**:

  1. **'Business' value growth**
     Marketing seeks to impact positively on sales **and** profit. Effective marketing can increase sales over several years, so marketing should be treated as an investment with a medium- to long-term payback. Marketing creates value for business when market share is gained (or share losses are prevented), and incremental profits generated exceed marketing investment.

  2. **'Customer' value growth**
     Marketing seeks to i) attract new customers, ii) encourage existing customers to spend more and iii) keeps existing customers for longer. Marketing creates value for the business by increasing consumer demand, thereby increasing customer numbers and/or profit per customer (often by increasing the prices that customers are willing to pay).

  3. **'Brand' value growth**
     Marketing seeks to create an emotional connection between the company, its products and services and the public. Marketing creates value for the business when this turns prospects into customers, and customers into loyal brand advocates, willing to recommend the company and its brands to others.

- It asserts that all three provide evidence for successful marketing, and that measures at each of these levels are necessary to give an accurate report of **payback** from marketing performance.

- It identifies three main contributors to successful marketing management and effective future business performance, which can act as **predictive indicators of success**: A&P investment strategy, promotional strategy and innovation intensity.

- It also proposes that, ultimately, the key financial measures of marketing success should be **marketing payback** and **return on marketing investment** (**ROMI**). Payback is important because it correlates the top-line and bottom-line business effect achieved through marketing, while ROMI can show the efficiency with which these effects are achieved.

- It then identifies 20 **performance indicators** for marketing from which **five are identified as key**: value market share, ratio of new to existing to lapsed customers, share of voice relative to share of market, ratio of winning to mediocre to unsuccessful campaigns, and marketing payback.

- Finally, it calls for three significant changes in reporting practice to encourage better marketing disclosure:
  1. Standardisation of A&P reporting
  2. A 'Marketing' section in the narrative report
  3. Formal marketing reporting in every boardroom where marketing is a significant budget item.

# Section 1
# The importance of marketing KPIs

In the context of corporate reporting, the most appropriate definition of key performance indicators (KPIs) is that provided by the Accounting Standards Board in its Reporting Statement on the Operating and Financial Review[3], namely:

> **"KPIs are factors by reference to which the development, performance or position of the business of the entity can be measured effectively. They are quantified measurements that reflect the critical success factors of an entity and disclose progress toward achieving a particular objective or objectives."**
>
> ASB Reporting Guideline; Definitions, point 3, page 8, 2005

KPIs provide the benchmarks against which relative corporate success can be measured. To be effective, they should be:

- internally consistent and externally verifiable
- comparable over time (to demonstrate trends in the business over time)
- comparative over time (to demonstrate relative performance in the market, and versus the competition, over time)
- material to business performance (i.e. a driver of value).

In the context of corporate reporting, the time frame needs to be yearly at a minimum, and increasingly six- monthly or quarterly. To be useful at board level, KPIs probably need to be reported on a quarterly basis.

## Why marketing KPIs matter

Effective reporting of marketing KPIs matter because:

1. Marketing assets are one of the main drivers of turnover growth and profit improvement, particularly for companies which are consumer-facing. Companies have a responsibility to demonstrate that they are providing incremental value to the bottom line over and above what they are investing in the top line.

2. For some companies investment in marketing activity, commonly described as advertising and promotion (A&P), is the single biggest item of operational expenditure (OPEX) on intangibles in any given year, and companies should demonstrate that they are investing responsibly.

3. Strategic marketing investment, designed to build brand value, takes time. While it is possible to identify lead indicators of performance in the period when the activity is taking place (in a given year), the impact of this type of marketing activity can take 18 months to three years to deliver its full effect. Companies should set expectations of performance which acknowledge this time frame (three to five years).

[3] The Accounting Standards Board Reporting Statement on the Operating and Financial Review (OFR), published in January 2006, sets out best practice guidelines for companies' narrative reporting. The OFR is the predecessor to the enhanced business review requirements set out in the Companies Act 2006.

4. Marketing is a competitive differentiator. The quality of marketing matters because it is both more effective and more efficient. Companies have the opportunity to demonstrate that their marketing is punching above its weight in the market.

5. Current and future customers are cash-flow generators for business. Brands add value when they accelerate cash flows, increase cash flows and extend cash flows. Marketing needs to demonstrate the positive impact brand management is making on its customer base.

Although marketing is perceived by shareholders to be an inexact science, companies still need to demonstrate that they are managing their marketing activities responsibly and professionally, with appropriate assessment of risk and reward for every decision that is taken.

> **"The analyst community is becoming increasingly marketing-savvy and is ready to be engaged in a more informal dialogue about the relationship between marketing investment and shareholder value."**
>
> Martin Deboo, Investec; How analysts think about intangibles and brands, IPA Intangible Revolution seminar, February 2007

A company that can diagnose whether, and why, its marketing is working is a company that is well run and suitably equipped to make decisions about investing significant funds on behalf of shareholders, for the good of the business.

## Why marketing KPIs are currently in short supply

IPA analysis of FTSE 100 narrative reports for the financial year 2006/07 demonstrates that marketing KPIs are currently in short supply (see Appendix 2 for full report).

Of the 388 KPIs deployed by 75% of the FTSE 100, financial indicators predominate (62%). Within the 149 non-financial indicators used, 33 relate loosely to customer service, but only ten relate specifically to brand, or marketing or reputation. Across all of these measures only customer satisfaction is used with any frequency.

Our literature review suggests that there are five probable reasons for this paucity of marketing data:

1. Lack of involvement from marketing in the process of preparing corporate reports.
2. Lack of confidence in the credibility of marketing data on the part of the finance department and other report preparers.
3. Lack of hard independent data which is 'fit for purpose'.
4. Lack of availability of consistent year-on-year (YoY) data.
5. A corporate unwillingness to provide competitors with sensitive marketing data.

Regrettably, it appears that many marketers lack the analytical skills required to make sense of the data and resources at their disposal in a way which serves the needs of the board room. There is often a mismatch between the **bottom-up data needs of campaign managers in marketing**, who are seeking to optimise individual brand campaigns, and the **top-down data needs of the chief financial officer, and CEO**, who want data which enables them to make decisions about current and future marketing investment in the context of overall business and competitor performance.

Fig 1. **Customer service and marketing KPIs in FTSE 100 reports 2006/7**

| **Customer service** | **33** |
|---|---|
| Customer satisfaction | 7 |
| Customer numbers | 5 |
| Customer retention rate | 3 |
| Customer service awards | 2 |
| Number of customer complaints | 2 |
| Orders on time | 2 |
| Churn | 1 |
| Credit cards in issue | 1 |
| Customer care | 1 |
| Customer delight | 1 |
| Number of features in best-buy tables | 1 |
| Telephony answer rates | 1 |
| Customer service index | 1 |
| Financial advisor practice service ranking | 1 |
| Interruptions | 1 |
| Minutes lost | 1 |
| Product availability | 1 |
| Product quality | 1 |
| **Brand** | **4** |
| Brand promise | 1 |
| % Revenue from top 18 brands | 1 |
| Brand perception | 1 |
| Global brand volume | 1 |
| **Marketing investment** | **1** |
| Media investment (as % of net revenue) | 1 |
| **Creativity** | **1** |
| Quality of creative output | 1 |
| **Reputation** | **4** |
| Reliability | 2 |
| Industry awards | 1 |
| Supplier viewpoint survey | 1 |

Source: IPA June 2007

In the words of one CFO:

> **"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; Marketing in 3D, January 2008

## Deterrents to marketing reporting

There are, undoubtedly, considerable challenges for marketing reporting:

1. **Group, region, business unit, line of business, brand**
   For multi-brand, diversified, global businesses it is particularly problematic to know at what level of detail to report. Our recommendation would be to follow the example set by blue-chip multi-brand consumer-facing businesses such as Unilever, which identify a manageable number of lead brands in key markets as exemplars of marketing activity, and report on the remainder in aggregate.

2. **External versus internal marketing**
   The important role of employees as 'brand ambassadors' is becoming more recognised, particularly in service businesses. The internal communications function may reside in the corporate communications or group marketing department, and a budget may be generated for internal marketing communications. There is no consensus as yet about how to report on this budget. Should it be allocated, for example, to human capital or to marketing? For this reason, it lies outside of the scope of this document.

3. **Corporate reputation versus brand**
   'Reputation management' has hitherto been considered to be distinct from 'brand marketing', and mainly focused on public relations and crisis management. We predict a merger between these two disciplines going forward, to create a new form of 'corporate marketing' which focuses on corporate brand management and is proactive in character and message. Our recommendation, therefore, is that corporate brand and reputation measures should be included in our discussion of marketing KPIs.

4. **Sector differences**
   Different sectors have different value drivers. Success in securing exploration and production contracts is vital to businesses in the energy sector, while mobile telecommunications companies focus on licenses, 'churn rates' and 'average revenue per user' (ARPU). Retail businesses, on the other hand, use 'like for like sales' and 'sales per square metre' as a benchmark for success. Purchase cycles differ substantially between sectors, as do definitions of loyal customers. Our belief, however, is that these variations can be accommodated.

# Section 2
# A strategic framework for marketing KPIs

In order to define a relevant set of KPIs for marketing it is important to first set an appropriate strategic framework for marketing. Necessarily broad-brush for the purposes of this exercise, it is our belief that it will be relatively easy to apply this framework to specific businesses and sectors.

## What does marketing success look like?

Marketing success is a function of the following value chain:

1. **'Business' value growth**
   Marketing seeks to impact positively on sales **and** profit. Effective marketing can increase sales over several years, so marketing should be treated as an investment with a medium- to long-term payback. Marketing creates value for business when market share is gained (or share losses are prevented), and incremental profits generated exceed marketing investment.

2. **'Customer' value growth**
   Marketing seeks to i) attract new customers, ii) encourage existing customers to spend more and iii) keep existing customers for longer. Marketing creates value for the business by increasing consumer demand, thereby increasing customer numbers and/or profit per customer (often by increasing the prices that customers are willing to pay).

3. **'Brand' value growth**
   Marketing seeks to create an emotional connection between the company, its products and services and the public. Marketing creates value for the business when this turns prospects into customers, and customers into loyal brand advocates, willing to recommend the company and its brands to others.

All three are, of course, evident in successful marketing; and, increasingly, with advances in technology, each can be tracked, on a continuous basis, sometimes in real time. Our belief is that measures at each of these levels are necessary to give an accurate report of **payback** from marketing performance.

## What are the predictors of marketing success?

The future of corporate success is never certain. Nevertheless, in the case of marketing, it is possible to identify 'lead' indicators, which are, more likely than not, predictors of future value generation. There are three main predictive indicators of successful marketing: A&P investment strategy, promotional strategy and innovation intensity.

**1. A&P investment strategy**

i) There is a correlation between size of budget and **dominant position** in the market. Market leaders tend to **spend most** in their sector.

ii) Companies who **spend consistently** tend to do best. There is a correlation between consistency of spend and **maintenance of a dominant position**.

iii) Companies **who spend relatively more** than their position in the market would suggest tend to **grow faster than the market**.

Size and maturity of brand, and quality of campaign, can modify these findings at the margin.

**2. Promotional mix**

i) The relative balance in spend between **strategic investment** in brand building and **tactical investment** in discounted price promotions is an indicator of business prospects. Discounted price promotions are rarely profitable for big or premium brands in mature markets and, in the long-term, promotions can erode brand value and exacerbate price elasticity. Promotional wars can commoditise whole categories. For big brands, shifting spend from discounted price promotions to brand communications increases both short-and long-term profit.

ii) The ability to deliver **integrated marketing campaigns**, to the same brand idea, across different channels and media, is a predictor of marketing success. The IPA dataBANK shows that the most effective campaigns use a combination of emotionally rich audio-visual media (TV, cinema, radio, online) and a direct response element (direct marketing, online). Those companies who demonstrate management ability in building partnerships with **a small group of trusted agencies** tend to do this best. Media modelling tools and techniques now exist to help optimise media value.

**3. Innovation intensity**

Innovation can impact on marketing performance at many different levels:

i) Companies who create relevant and timely **new news** in established markets tend to do best. Examples of new news might be design innovation, product innovation or message innovation.

ii) Companies who create relevant **new markets** tend to do best. There is a correlation between being first to market and brand leadership.

iii) Companies who set **new trends** in creative content or channel and media usage tend to do best. The networked society, enabled through web 2.0, presents new challenges and opportunities for content creators and producers.

An understanding of a company's profile on all of these dimensions of marketing performance can help investors understand the likely future prospects for organic business growth and profitability.

## What is the financial payback from marketing investment?

Financial measures of marketing payback are still in their infancy. The key financial measures of marketing success should be **payback** and **return on marketing investment** (**ROMI**). In calculating either of these metrics, the **net present value** (**NPV**) of future cash flows must be taken into account in order to assess whether marketing activity truly adds value.

1. **Payback**
   A calculation of payback should correlate the top-and bottom-line business effect achieved from marketing. Arguably, the ultimate goal of any business, when it comes to a discussion of marketing, should be to improve payback over time. Marketing activity is long term in its effects and therefore a calculation of net present value is a vital part of the assessment of payback.

2. **ROMI**
   A strictly financial calculation of ROMI can show the efficiency with which these effects are achieved. On the whole, these calculations have been used to **explain success in the periods following marketing activity**, rather than to predict success in advance of marketing activity.

   Increasingly sophisticated modelling tools and techniques now exist to help evaluate the impact and likely outcome of different budget scenarios. Looking ahead, ROMI could be employed both for **specifying and allocating budgets** across portfolios of businesses, products or services.

   However considerable caution must be exercised in the deployment of ROMI calculations. The reality is that a simplistic approach to maximising ROMI can lead to budget cuts, reduced profits and the destruction of shareholder value. An assessment of the likely future financial payback of any activity, involving a sophisticated NPV calculation, is potentially a more reliable measure.

There is evidence, both in the UK and the USA, of a growing interest in perfecting calculations of payback and ROMI, to the point where it can be used both as a predictive planning tool for marketing activity, and a remuneration incentive for marketing departments and their agencies. The IPA is at the forefront of developments in this area in the UK, and is working with the Chartered Institute of Management Accountants (CIMA) and the Incorporated Society of British Advertisers (ISBA) to develop knowledge, understanding and best reporting practice, across the marketing, marketing finance, procurement and agency functions.

Extracts from the IPA guidance note on how to calculate payback and ROMI are provided in Appendix 1.

# Section 3
# A model framework for marketing reporting

Using these definitions and predictors of marketing success as our foundation, we have arrived at the following framework for marketing reporting. Any framework, of course, comes with caveats:

- There are more metrics than any company would have space or need for in their annual report. We have highlighted in **colour** those which we consider to be the most important **key** performance indicators.
- Some of the metrics listed may be deemed to be market-sensitive, and therefore inappropriate for disclosure to the market. In those cases, we would recommend that they are considered, at a minimum, for **internal reporting** to the board.
- Some of the definitions within these metrics are **purposefully general**. For example, 'customer' is used in its broadest sense to embrace both end consumers and trade customers. Reputation and brand are bunched together. For some companies the corporate brand will be their only concern, for others, with a multi-brand business portfolio, the interrelationship between the corporate brand and business, product and service brands will need to be identified. These terms will need to be refined in the context of a particular business.
- Some of these metrics are **necessarily soft**, and take non-financial measurement into a new realm. Consumer responses mark out the difference between success and failure in marketing. Therefore it is important that useful human response factors such as 'buzz', engagement and word of mouth are included.
- Many companies may not currently have access to some or all of these metrics. Help is at hand in the form of a 'where to…' guide in Appendix 3.
- For some companies not all of these metrics may be relevant. The recommended range of metrics listed should be considered to be **a menu of possible options**, to stimulate discussion, debate and decision making.
- Many preparers of narrative reports may have difficulty in relating to the wording of these metrics. However, where lack of clarity exists, we hope this will create the opportunity for an early meeting with the marketing department to find out more.
- Although an attempt has been made to be comprehensive, readers may find that the list is incomplete. We have been sparse in our recommendations for metrics which relate to reputation, brand and quality of communications. Appendix 4 suggests relevant additional reading.

In all cases, our recommendation would be that these metrics are tracked and reported, ideally on a quarterly basis, in order to develop and build data sets which are consistent, comparable over time, and, preferably, also comparative in the market. Where companies select not to use the KPIs listed as a quantified measure of marketing performance we would recommend, nevertheless, that the topic area, suggested by that metric, be the subject of discussion in the narrative report.

Fig 2. **A model framework for marketing reporting**

# 20 performance indicators* for marketing reporting

| What | How | Why |
|---|---|---|
| | **Measures of success** | |
| **Business value** | 1. Changes in sales value (not just volume) | Price strengthening enhances profit. Changes in volume growth can hide the impact on profit of discount activity. |
| | 2. Changes in market share | Relative position in the market is more important to long-term performance than actual sales. Increased sales can hide market share losses. |
| **Customer value** | 3. Volume of new customers | Penetration gains year on year and on a continuous basis are vital to business health. |
| | 4. Changes in value from existing customers | An increase in average spend per customer is an indicator of customer satisfaction and customer preference. |
| | 5. Volume of lapsed customers | An increase in numbers of lapsed customers suggests declines in customer satisfaction, and declines in customer preference versus the competition. |
| | 6. Ratio of new customers to existing customers to lapsed customers | When new customers, as a % of total customers show decline, this is a warning sign for future business performance. |
| **Brand value** | 7. Changes in levels of awareness | An indicator of brand saliency. But awareness is insufficient on its own. |
| | 8. Changes in perception | Improvements in brand image tend to reflect more favourable attitudes and opinions. |
| | 9. Changes in levels of engagement | Engagement is an indicator of brand strength and emotional connection. It can also be expressed in terms of brand affinity and brand consideration. |

*KPIs are identified in colour

| What | How | Why |
|---|---|---|
| **Predictors of success** | | |
| **A&P investment strategy** | 10. % increase YoY (allowing for economic and media inflation) | Declining brands are less able to justify investment; growth brands justify more, particularly in emerging growth markets. |
| | 11. Advertising to sales ratio (A/S ratio) | Marketing leads sales not vice versa, so A/S ratio needs to be set against anticipated market and sales growth. |
| | 12. Share of voice versus share of market | When share of voice exceeds current share of market (excess SOV) it may be an indicator of market aspirations – an aggressive strategic intent to take share from the competition. |
| **Promotional mix** | 13. Ratio of budget allocation between tactical price promotion and strategic brand-building activity | Growth in discounted price promotional activity is an indicator of weakening brand health and/or weakening relationships with trade channels. |
| | 14. Relative effectiveness of media mix strategies | Well integrated campaigns around a unifying brand or campaign idea tend to optimise media value. |
| | 15. Ratio of successful to mediocre, to unsuccessful campaigns | An indicator of sound management in campaign planning and evaluation, and a commitment to continuous improvement in communications strategy and execution. |
| **Innovation intensity** | 16. Number of examples of successful new news | A barometer of future prospects from established businesses. |
| | 17. Number of examples of successful new market entrants | A barometer of future prospects from new business opportunities. |
| | 18. Numbers of 'winning' campaigns | Measures of campaign 'buzz', WOM tracking and net promoter scores are early predictors of winning campaigns. Creative quality and differentiation improve the chances of campaign effectiveness. |

| What | How | Why |
|---|---|---|
| **Financial metrics** | | |
| **Overall** | 19. Marketing payback | The net profit generated from marketing investment (after marketing and overhead costs). |
| | 20. Return on marketing investment (ROMI) | A relative measure of marketing effectiveness and efficiency. |

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## Putting the framework into practice

It is our view that this framework can provide the basis for productive early discussion between preparers of annual reports and the marketing department, with their agencies.

For some companies, it is unlikely that data will be readily available in a format for reporting from the outset, but with this framework as a guide, there is no reason why this cannot be achieved in time. For those companies already in the habit of preparing a marketing dashboard for internal reporting to the board, providing this sort of information should be relatively painless. Where a company accepts it can strengthen its management metrics and commits to new, additional KPIs, it will probably want to have them in use for a full year before reporting on them externally.

A 'traffic light' system of colour coding (where green indicates growth, amber indicates stability, and red indicates decline) can be a valuable addition to make interpretation of the trends easier. Clarity and simplicity are vital ingredients for making external marketing reporting accessible.

# Section 4
# The way forward for marketing disclosure

In those companies where market responsiveness to brand assets has a significant impact on total business performance, there is an obligation for companies to improve their disclosure of marketing metrics.

Although the market is naturally conservative, there are signs that appetite for marketing information is growing, particularly among the larger long-term investors and their equity analysts.

This publication is intended as a stepping stone in this direction. We intend to make it the subject of consultative seminars with key stakeholders from the investment, corporate reporting, research and marketing communities; and to monitor and track developments in marketing reporting through our association with the annual IR Magazine UK Award for Best Narrative Reporting.

Looking ahead, we have three additional suggestions to propose to the market:

## Standardisation of A&P reporting

There is currently no obligation, under IFRS, for the budget allocation to A&P to be broken out in the Profit and Loss account in the financial report: nor is the definition of A&P specified, or the division between trade and consumer marketing activity explained. We would like to campaign for change in this area to bring greater clarity to A&P reporting.

## A 'Marketing' section in the narrative report

Headings give focus, and we would like to propose that preparers of business reviews include a heading entitled 'Marketing' to act as a reminder of the need for enhanced coverage of this business critical topic. This might be included, for example, with the Resources and Relationships section of the narrative report.

## Marketing reporting to the board

We have tracked, with interest, the growth in the number of sub-committees on the board with special responsibilities e.g. audit, remuneration. We acknowledge that formal auditing of marketing investment is unlikely. Nevertheless, in order to encourage better reporting and sound stewardship of marketing investment, we would like to recommend that boards of companies where marketing is a significant budget item should always receive a formal marketing report, linked to KPIs, at their meetings.

We actively welcome reaction to these proposals, as we look to find ways to turn vision into reality.

# Appendix 1
# How to calculate payback and ROMI

The following material draws significantly from the new IPA publication authored by Les Binet and entitled *Measuring Marketing Payback* (IPA, 2008).

## **Step 1 -** Incremental sales

The first step towards calculating marketing's financial payback is to estimate the **incremental sales** generated by your activity. To do this, you need to compare actual sales with 'base sales' – how much you would have sold if you hadn't run the marketing activity in question.

Estimating incremental sales is by no means easy, but various common methods include:

- econometric modelling
- test and control areas
- extrapolating from a past trend.

Important points to remember in this calculation include:

- Measuring incremental sales is not the same as measuring sales growth. Lack of growth is not necessarily a sign of ineffective marketing – it may be that sales would have been even worse without marketing support.

- The effects of your marketing may persist some time after the activity itself has stopped. This may require you to forecast sales some way ahead into the future.

- Beware of post-promotional dips.

- Too many marketing personnel focus on sales volume and neglect revenue. Ideally you should measure both.

- Marketing for one product may also boost sales of other products in your portfolio. Such 'halo effects' are the main way brand-building contributes to shareholder value, so don't forget to take them into account.

- Direct response data do not give you all the answers. Direct response activity may have other effects besides generating direct responses. Some people may respond to your activity long after the event, via a completely different channel. Also, not all direct sales are incremental sales.

## **Step 2 -** Incremental profit

The next step is to calculate the revenue generated for the client, remembering to take into account any effects on price. What the client actually gets are the value of wholesale sales, which are retail sales less the retailer's (or other channel intermediary's) mark-up.

*Incremental revenue = Incremental retail sales value – Intermediary cash margin*

Having calculated the value of the incremental sales to the client, the next step is to calculate the contribution that those sales make to profit. To do this, one needs to take account of the incremental costs incurred.

*Incremental costs = Variable cost per unit x Incremental units*

Subtracting these costs from the incremental sales revenue gives the marginal contribution to profit:

*Marginal contribution = Incremental revenue – Incremental costs*

Alternatively, rather than using unit costs, one can do exactly the same calculation using the contribution margin, if this is known. The calculation then becomes:

*Marginal contribution = Incremental sales revenue x contribution margin %*

## **Step 3 -** Net profit

Having calculated the marginal contribution, the final step is to subtract the cost of the campaign to calculate the net profit it generates:

Net profit generated = Marginal contribution – Cost of campaign

**The net profit generated is the ultimate measure of effectiveness, the measure of how much money the campaign made for the brand's owners.**

Important points to remember in these calculations:

- **Revenue is not the same as profit**

- **Don't subtract fixed costs** – The kind of sales uplifts produced by successful marketing can usually be accommodated within existing production capacity, at least in the short term. So the only additional costs incurred are the variable costs associated with production and the cost of the campaign itself.

- It's very important to **base the payback calculation on the 'contribution margin', rather than the net profit margin** that appears in the client's accounts or other management data. The net profit margin takes account of fixed costs, whereas the contribution margin only accounts for variable costs.

**Net present value – long-term effects**
In the above it has been assumed that payback is calculated over a fairly short period – say six months to a year. However, much brand-building activity does not pay back over such a short period. Yet it can still be sensible to invest heavily now behind the promise of growth (or the avoidance of decline) in the future.

The above calculations remain valid, however you need to take account of what is called the 'time value of money' – the idea that profits in the future are worth less than profits now, using discounted cash-flow analysis (DCF). DCF allows you to convert any stream of future payments to its 'net present value' (NPV) – the value of that income stream as a lump sum here and now.

In calculating NPV it is important not to assume that the current strength and position of the company will continue unimpaired, even if the investment isn't made. The comparison should be made between the projected discounted cash flow and the likely base case of a decline in performance in the absence of investment.

Rather than net profit, the ultimate measure of payback becomes the NPV of the incremental cash-flow generated by the campaign, which is:

*NPV (Incremental revenue) – NPV (Incremental costs)*

You may need to take account of some additional costs when calculating long-term payback – for instance, a long-term increase in demand might require an increase in production capacity.

## Return on marketing investment (ROMI)

Net profit generated is the ultimate measure of marketing effectiveness. However, if you want to measure financial efficiency as well, then you need to do a return on investment (ROI) or return on marketing investment (ROMI) calculation.

*ROMI = (Net profit / Cost of campaign) x 100%*

The terms of this equation are the same as those generated for the payback calculation. We recommend that the term 'ROMI' is always used when calculating the return from marketing, in order to avoid confusion with other ROI measures like ROCE.

ROMI is a useful measure, because it allows you to compare the efficiency of different campaigns with different budgets. It also allows you to compare the return from your campaign with the returns from other alternative investments.

## Payback and ROMI for company reporting

The above examination of payback and ROMI is applicable primarily to individual marketing campaigns over a short period. The requirement to report annually is problematic in properly expressing group marketing success. In reporting it at a group level it is necessary to create a new metric with a broader scope.

This aim can be achieved by reporting an aggregate payback for a selected group of five products across the year. By combining incremental sales figures for five separate products, and taking the sum of marketing expenditure on these products across a year, a metric can be created which gives a strong indication of the wider success of company marketing, without revealing any figures for weight of marketing spend, or incremental spend attributable to any particular product or market. Trend data are particularly important in this case. To capture the full return of marketing activity historic data would need to be disclosed for at least two years prior to the reporting period. In these calculations a NPV assessment is of particular importance.

# Appendix 2

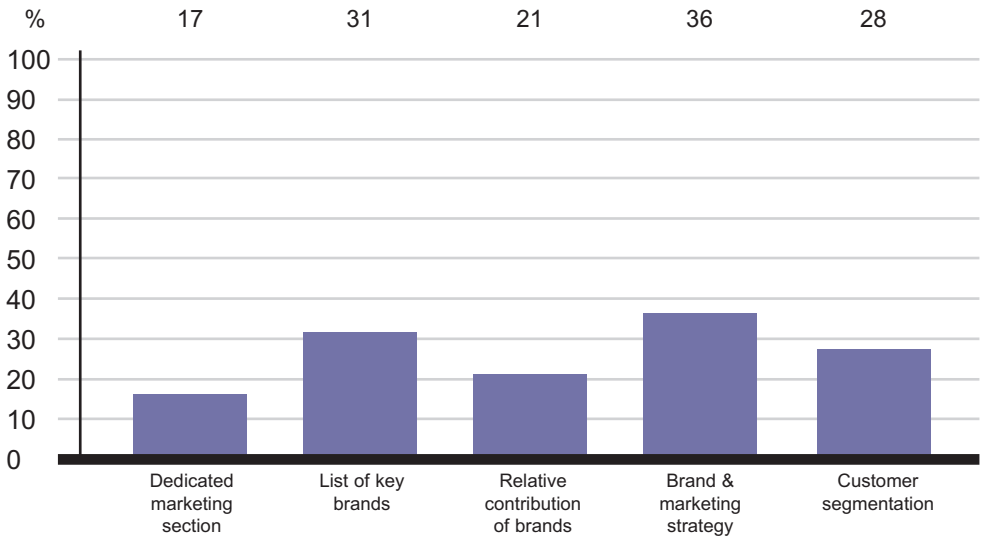
## 2.1 IPA analysis of KPIs in FTSE 100 narrative reports

During 2007 the IPA conducted an in-depth examination of FTSE 350 annual reports as part of the judging process for the IR Magazine UK Award for Best Narrative Reporting. The broad conclusions of this process were published in the IPA report Best practice in narrative reporting. However, alongside this analysis, the IPA conducted a separate study of KPIs and marketing information in FTSE 100 reports.

**Key marketing information**
This study found that marketing information was generally very poorly represented. Fifty-six of the FTSE 100 are consumer-facing sectors with heavy A&P investments, and yet the number of reports which discussed marketing strategy and brands was very small.

Very few had a section dedicated to the company's brands or marketing strategy, though almost all had dedicated sections on human capital, and even environmental impact. The chart below shows what marketing information appeared in 2006/07 annual reports, and the percentage of companies which disclosed on each item.

Fig 3. **Marketing information in the FTSE 100 narrative reports**

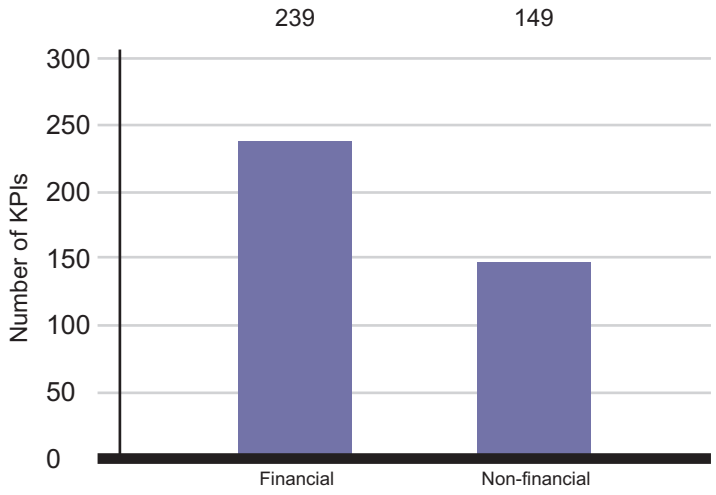



Source: IPA 2007

**Key performance indicators**
The IPA study of KPIs in FTSE 100 narrative reports showed a very mixed engagement with the topic as a whole. Companies had, in many cases, adopted a cautious approach, choosing not to disclose KPIs in the first year.

The first stage of the study focused on auditing the incidence of each KPI. Only 75 of the FTSE 100 deployed KPIs. Three-hundred-and-eighty-eight KPIs were deployed at an average of approximately five per company. In general, financial indicators predominated (62%); however, there were a surprisingly high frequency of non-financial measures. Of the 388 KPIs deployed, 149 (38%) were non-financial.

Fig 4. **KPIs in FTSE 100 narrative reports 2006/07**

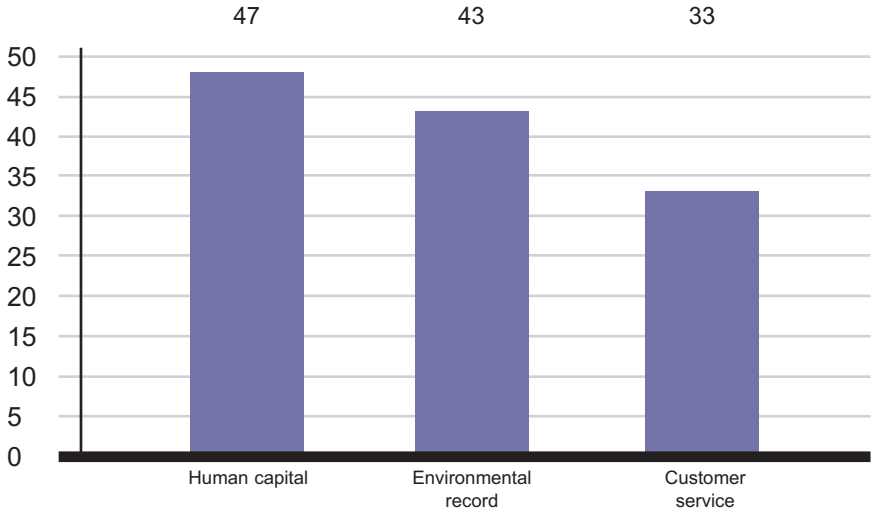



Source: IPA 2007

**Non-financial indicators**

During the next stage of research, the KPIs were categorised. Non-financial indicators were heavily weighted towards human capital and environmental record. Of the 149 deployed, 90 related to these two areas. Although there were a further 33 which related to customers, these were very inconsistent, and related to customer service. They did not relate to marketing strategy or brand value in the main.

Fig 5. **Non-financial KPIs in FTSE 100 narrative reports 2006/07**

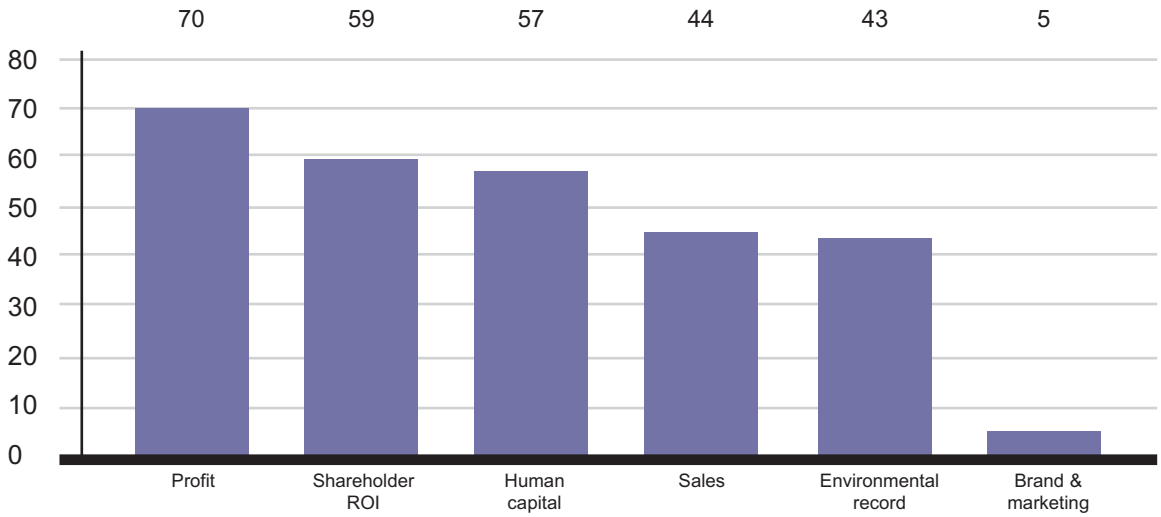



Source: IPA 2007

**Marketing and brand KPIs**

KPIs which directly relate to marketing and brand were deployed by a very small percentage of companies when compared to metrics which measured other key business drivers. KPIs relating to these two areas were 30 times more frequent than those which measured marketing and brands.

Fig 6. **KPI categories in rank order of mention in FTSE 100 narrative reports 2006/07**




Source: IPA 2007

## 2.2 IPA/Cass analysis of marketing reporting in FTSE 100 presentations to City analysts

During 2007, the IPA also undertook, with Cass Business School, a detailed analysis of marketing information appearing in presentations to analysts, in the knowledge that these presentations form a vital source of interpretive context for analysts in their assessment of a company, and are generally regarded to be more important than the annual report in communicating with large institutional investors.

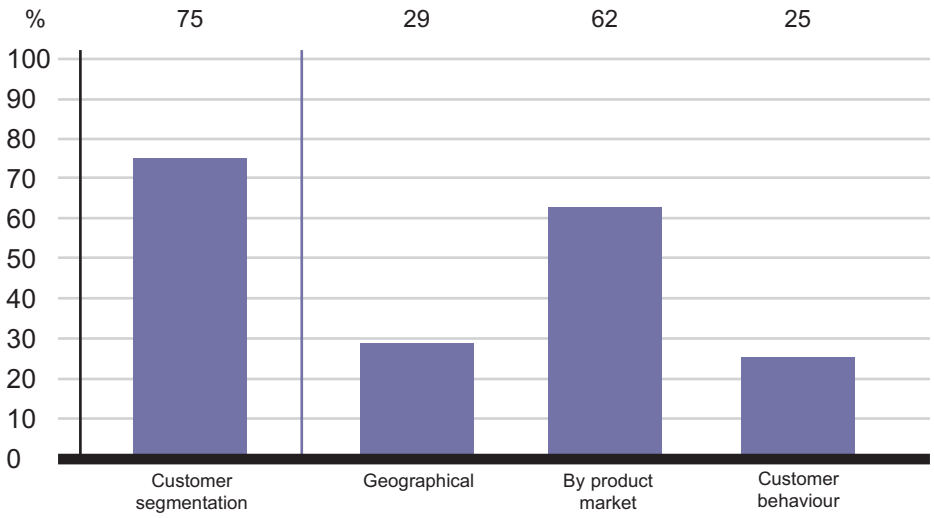
Our analysis focused on presentations made by FTSE 100 companies during the first six months of 2007. The definition of FTSE 100 companies used was set on May 24, 2007 to match the IPA audit of narrative reports. The examination included the written presentations, and where available the podcasts and webcasts of the presentations including the Q&A.

**Overview**
On the whole, overall levels of detail were significantly higher than in narrative reports. However, there was a still a lack of clarity and consistency in the information provided, and there was very little provision of comparative or continuous data from which to draw conclusions on overall trends.

Specifically, marketing information related to:
- customer segmentation
- market share
- market strategy
- marketing investment
- marketing metrics
- marketing ROI (ROMI).

**Customer segmentation**
A large majority (75%) of FTSE 100 companies provided some sort of customer segmentation for at least some products. Companies with no segmentation given – 25% – were all business-to-business or utilities. Those that included some sort of segmentation generally discussed their sales efforts and their ability to tailor sales outreach to customer needs, rather than divisions in the marketplace. On the other end of the spectrum, some consumer product companies presented detailed consumer segmentations, discussing marketing activities aimed at each segment and justifying their decisions with market trends and demographic information for each. The large majority of the companies profiled took an intermediate approach.

Fig 7. **Customer segmentation in FTSE 100 presentations to analysts**

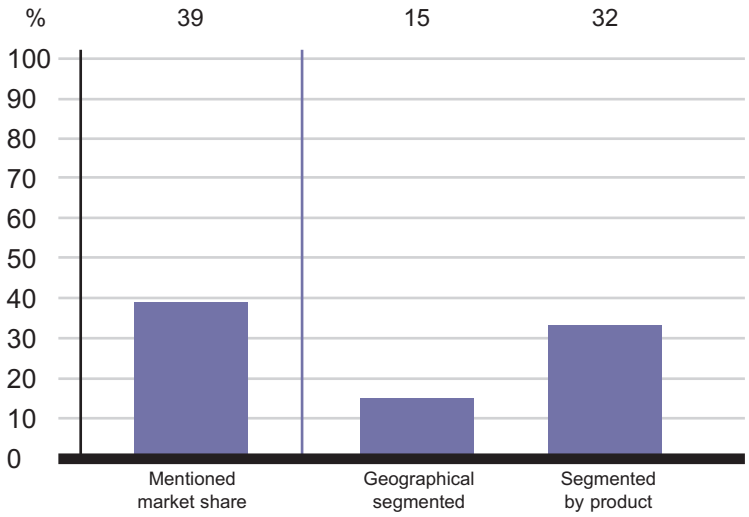



Source: IPA/Cass 2007
Copyright: IPA

The two most common types of segmentation presented were geographic segmentations (29%), with results or goals divided by country, continent, or region, and internal or divisional segmentation (62%), with results or goals divided according to the corporation's internal organisation. One quarter of companies (25%) provided segmentation based on some aspect of customer behaviour relevant to the company. This metric gives a very convincing picture of marketing expertise when it is used, as identifying the relevant behaviour is in itself a display of market knowledge.

**Market share**
Over one third of companies (39%) discussed market share, either for the company's entire product line or for specific brands. Fifteen percent of companies presented market share by geographic territory, while 32% focussed on market share by product. There are some overlapping in reporting. In many cases, increasing market share for a particular product or the company as a whole was listed as a strategic goal. In other cases, 'growth' was presented as a goal.

Fig 8. **Market share in FTSE 100 presentations to analysts**

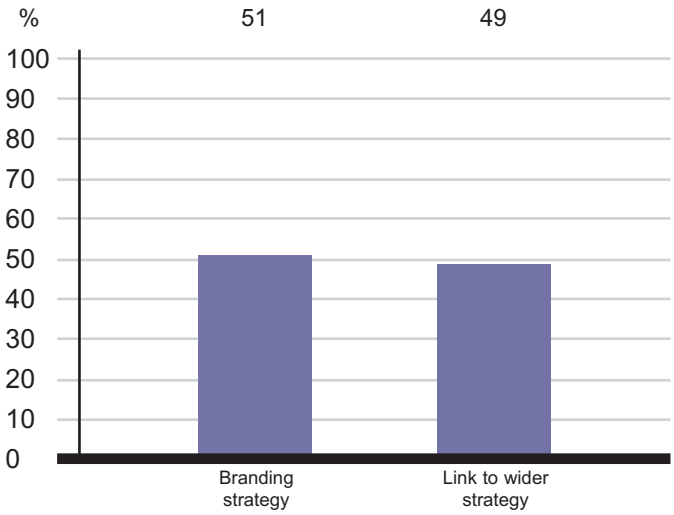



Source: IPA/Cass 2007
Copyright: IPA

**Marketing strategy**

The strongest presentations of marketing information were those that linked strategic marketing decisions making to the overall profit goal. Basic linkages of marketing decisions to overall corporate strategy were made only 49% of the time, with strategic directions for branding discussed only slightly more often (51% of the time).

Fig 9. **Marketing strategy mentions in FTSE 100 presentations to analysts**




Source: IPA/Cass 2007
Copyright: IPA

**Britvic**
A particularly effective example of describing marketing strategy occurred in the Britvic presentation examined. The presentation gave results and targets for the beverage company's products divided by category, but went beyond the level of detail that most firms which use this sort of divisional segmentation provide. For each general category, Britvic provided information about market trends, the rates at which the market appeared to be changing, and the projected effect on Britvic's brands in that category. This information was clearly related to the company's position on value versus volume and the communications strategy for each brand discussed, giving an overall picture of profit-focused marketing without disclosure of sensitive data.

**Marks and Spencer**
Marks & Spencer's presentation provided information about what percentage of customers purchased top-of-the-line products in several areas of the company, and then offered information on how marketing could be tailored to these shoppers, maximising profit-per-customer while minimising cannibalisation of other product sales. This was linked to long-term product development strategy.

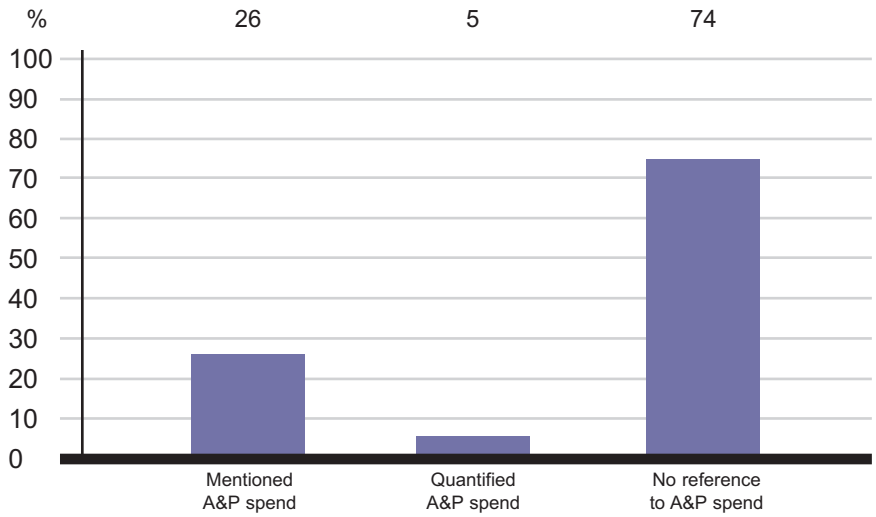
**Burberry**
In the Burberry presentation a 'product pyramid' showed different categories of consumer need and fitted these to different parts of Burberry's product line. Each of these 'fits' was then discussed as a potential source of long-term profits. For example, an outerwear line that offers an image of luxury, presented by integrated communications, can both add sales volume from wealthy customers and help the brand create an image of exclusivity to support a 10-15% price premium.

By making a profit-linked rationale clear, Burberry was able to make a strong, financially-rooted case for long-term strategic marketing decisions, such as the launch of a new fashion line, which would not be profitable in the short term.

## Marketing investment

Specific marketing detail occurred less often than more general strategic information, with only 26% of companies discussing their A &P investments at all. Only 5% of FTSE 100 companies quantified their marketing investment in their presentations.

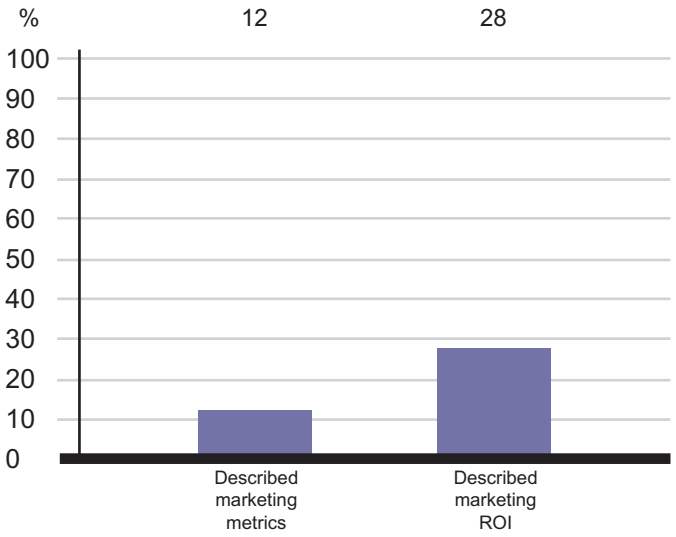
Fig 10. **Marketing investment reporting in FTSE 100 presentations to analysts**




Source: IPA/Cass 2007
Copyright: IPA

**Marketing metrics and ROI (ROMI)**
Only 12% of companies made reference to some sort of metrics for marketing in the presentations, although these were not always clearly derived and were therefore presumably not always useful to analysts wishing to compare a metric across companies. Only 28% mentioned marketing's contribution to their companies' value even indirectly.

Fig 11. **Marketing metrics and marketing ROI (ROMI) reporting by FTSE 100 companies in presentations to analysts**




Source: IPA/Cass 2007
Copyright: IPA

**Question and answer sessions**
A general overview of the question and answer records available provided two useful, if unsurprising, observations.

- First, presentations that contained marketing information provoked more questions about marketing overall. In other words, companies that demonstrated sound marketing data were rewarded with increased analyst attention to their marketing expertise.

- In the absence of extensive marketing information in the presentation, the only question which appeared on a regular basis was about A&P expenditure as a percentage of sales in consumer-facing companies.

# Appendix 3
## Where to go for more advice and help

There are over 270 agencies in the IPA membership, and you may find that one of them is working for you already. If you don't know, but would like to find out, please contact Tom Mott (tom@ipa.co.uk).

If you are not currently working with an IPA member agency, but would like IPA advice and help on this topic, please contact IPA consultant, Janet Hull (janet@ipa.co.uk).

A number of IPA agencies provide econometrics and strategic marketing analytics services, among them:

**Aevolve** *(Vizeum and Carat)*
Contact: Mark Greenstreet
E-mail: mark.greenstreet@aemedia.com

**Brand Science** *(MDOMD, M2M, OMD, PHD, Rocket)*
Contact: Sally Dickerson
E-mail: sally.dickerson@brandsciencenetwork.com

**DDB Matrix**
Contact: Les Binet
E-mail: les.binet@ddblondon.com

**Leo Burnett**
Contact: Gurdeep Puri
E-mail: gurdeep.puri@leoburnett.com

**MediaCom**
Contact: Jeremy Griffiths
E-mail: jeremy.griffiths@mediacom.com

**Mediaedge:cia**
Contact: David Fletcher
E-mail: david.fletcher@mecglobal.com

**Mindshare**
Contact: Simeon Duckworth
E-mail: simeon.duckworth@mindshareworld.com

**Naked Numbers**
Contact: Scott Thomson
E-mail: scott_thomson@nakedcomms.com

**Ninah Consulting** *(Zenith Optimedia)*
Contact: Mike Campbell
E-mail: mike.campbell@ninah.com

**Starcom MediaVest**
Contact: Nigel Waring
E-mail: nigel.waring@smvgroup.co.uk

Other relevant consultancies, known to the IPA, but outside of the membership, include:

**Brand Finance**
Contact: Mike Rocha
E-mail: m.rocha@brandfinance.com

**Data2Decisions**
Contact: Karl Weaver
E-mail: karlweaver@d2dlimited.com

**Millward Brown Optimor**
Contact: Joanna Seddon
E-mail: joanna.seddon@us.millwardbrown.com

**Peter Field**
E-mail: peter.field@dsl.pipex.com

**Profit Impact of Market Strategy(PIMS)**
Contact: Doug McConchie
E-mail: doug.mcconchie@malikpims.com

**PriceWaterhouseCoopers**
Contact: Andrew Sharp
E-mail: andrew.sharp@uk.pwc.com

# Appendix 4
# Additional reading

## IPA publications

*Advertising Works 15,* Ed. Laurence Green (WARC, 2007)

*Advertising Works 16,* Ed. Richard Storey (WARC, 2008)

*Advertising Works and How: Winning communications strategies for business,* Ed. Laurence Green (WARC, 2005)

*Best Practice in Narrative Reporting: A review of FTSE 350 listed companies* (IPA, 2007)

*How Analysts View Marketing: An IPA study of City opinion* (IPA, 2005)

*Marketing in the Era of Accountability,* Les Binet and Peter Field (IPA/WARC, 2007)

*The Development of Intangibles Reporting: How intangible assets are transforming management and reporting practice* (IPA, 2007)

## IPA online

*Advertising in a Downturn* (IPA, 2008)

*Econometrics Explained,* Louise Cook and Mike Holmes Ed. Les Binet (IPA, 2004)

*Global Intangible Tracker 2006 and 2007: An annual review of the world's intangible value* (Brand Finance/IPA, 2006 and 2007)

*Measuring Marketing Payback,* Les Binet (IPA, 2008)

**www.intangiblereporting.com**

## Other

*A Review of Narrative Reporting by UK Listed Companies in 2006* (Accounting Standards Board, 2007)

*Advertising and the Long-Term Success of the Premium Brand,* Stephen Buck (WARC 2001)

*Improving Marketing Effectiveness,* Robert Shaw (The Economist, 1998)

*Marketing and the Bottom Line,* Tim Ambler (Pearson Education Limited, 2000)

*Marketing in 3D* (Deloitte, 2008)

*Marketing Payback: Is your marketing profitable?,* Robert Shaw and David Merrick, (Pearson Education Limited, 2005)

*Risky Business* (Deloitte, 2005)

*The SAGE Handbook of Advertising,* Eds. Gerard J. Tellis & Tim Ambler (Sage Publications, 2007)

*The Value Reporting Revolution,* Robert G. Eccles, Robert H. Hertz, E. Mary Keegan and David M.H. Phillips (Wiley, 2001)

*Value Based Marketing,* Peter Doyle (Wiley, 2000)

Institute of Practitioners in Advertising
44 Belgrave Square London SW1X 8QS
*telephone:* 020 7235 7020
*fax:* 020 7245 9904
*email:* janet@ipa.co.uk
www.ipa.co.uk
www.intangiblereporting.com

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