Two time published Admap report

Top 10 drivers of advertising profitability

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Top 10 drivers of advertising profitability

This update to the 2006 report 'Advertising’s Greatest Hits', shows that growth in digital advertising has made the science of budget allocation across channels and territories even more important in advertising’s RoI.

By Paul Dyson, Data2Decisions

In 2006, Karl Weaver and I wrote ‘Advertising’s greatest hits: profitability and brand value’, an article which listed the 10 most significant factors impacting the profitability of media investments (Admap, February 2006). It was developed from our experience at Data2Decisions and borne from a belief that advertisers were focusing on the wrong things.

Back then, we were frequently asked to measure the impact of media tests around quality viewing, break ecology, target audiences and media multipliers. While these were all important, and could add a few percentage points to the return from the media investment, there were much bigger opportunities to improve the impact of advertising, which clients seemed to miss – for instance, budget setting, phasing, and biggest of all, creative quality. By tackling these more effectively, we believed marketers could easily double the return from advertising, or, in the case of creative, improve the RoI by at least a factor of 10.

We also wanted to highlight that brand size was probably the biggest determinant of media RoI. We had explored this before (Admap, November 2003) but marketers were still missing the point and either setting unrealistic targets for their brands’ RoIs or allocating budgets to smaller brands, which, unless there was a good strategic reason to do so, would mean a lower overall return. ‘Brand size’ topped our list in 2006 with a possible multiplier of 16 on advertising return.

Based on our 20-plus years’ collective experience of modelling the impact of advertising on sales, we developed a list of the top 10 factors driving advertising profitability (Figure 1). Eight years later, we have taken stock of all the changes and compiled a brand new list to help marketers make more impactful decisions about their advertising investments.

Before we move onto the updated list, it is worth explaining what we mean by profit multiplier. This is not RoI, but the difference between revenue generated by advertising and the cost of advertising. So a £4 million campaign that generated £8 million incremental sales would have an RoI of £2.00 (£8m/£4m) or an advertising profit of £4m (£8m minus £4m).

The distinction is important because advertising tends to exhibit diminishing returns, which means the RoI will tend to fall as budget is increased. So, if we increased our campaign to £5m, we might find incremental sales have also increased – but by slightly less than the previous rate – to £9.5m: the RoI has dropped to £1.90 but the profit from advertising has increased to £4.5m. So we find advertising profitability a much better metric when comparing the...

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**FIGURE 1: TOP 10 FACTORS DRIVING ADVERTISING PROFITABILITY**

<table>
<thead>
<tr>
<th>Position</th>
<th>Factor</th>
<th>Profit Multiplier</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Market size</td>
<td>16.00</td>
</tr>
<tr>
<td>2</td>
<td>Creative execution</td>
<td>10.00</td>
</tr>
<tr>
<td>3</td>
<td>Budget-setting and allocation</td>
<td>2.00</td>
</tr>
<tr>
<td>4</td>
<td>Variable media costs</td>
<td>1.60</td>
</tr>
<tr>
<td>5</td>
<td>Laydown</td>
<td>1.10</td>
</tr>
<tr>
<td>5</td>
<td>Media multiplier</td>
<td>1.10</td>
</tr>
<tr>
<td>7</td>
<td>Brand life cycle</td>
<td>1.08</td>
</tr>
<tr>
<td>8</td>
<td>Quality viewing</td>
<td>1.05</td>
</tr>
<tr>
<td>8</td>
<td>Task</td>
<td>1.05</td>
</tr>
<tr>
<td>10</td>
<td>Audience</td>
<td>1.04</td>
</tr>
</tbody>
</table>

Source: Data2Decisions
payback from media strategies with different budgets.

And in our example, the profit multiplier would be £4.5m/£4m = 1.125.

Throughout the past eight years, we have witnessed a digital explosion. Our previous top 10 list was published in March 2006 – just as Jack Dorsey was opening the first-ever Twitter account. The iPhone hadn’t been launched and it was another four years until the iPad appeared in 2010. This has resulted in an always-on, multi-screen media consumer. It has also created new opportunities for brands to advertise and communicate with those consumers, an opportunity that is ever-closer to the point of purchase.

We’ve also seen brands get bigger during the past eight years. According to Millward Brown’s BrandZ™ study, the Top 100 brands grew by $310 billion in 2013 – an average of 12%. Prior to 2013, these same brands had grown by an average of 6% per year since 2008, during one of the toughest recessions of the past 100 years.

This growth has been helped by the internationalisation of brands but also by mergers and acquisitions. This has led to the growth of the ‘portfolio’ – either a large portfolio of diverse and varied brands (e.g. Diageo) or a deliberate strategy to build an umbrella brand (e.g. Dove) to take advantage of halo opportunities.

All of these changes have made marketing and communications much more complicated for businesses compared with eight years ago. There are many more ways to reach consumers and many more brands and countries across which budgets can be allocated. This has increased the opportunity to impact profitability but, at the same time, has made the process much more involved, with a greater need for experts and data.

Consequently, we have seen a significant impact on the payback from advertising. Figure 2 reveals our updated top 10 ways to improve advertising RoI.

At first we thought ‘digital’ would be a new entry; however, digital is effectively another media channel so technically it can’t make the list. Nonetheless, its impact on other drivers is wide and varied. Digital affects budget allocation across channels and provides an opportunity for media creativity to evolve. It has also impacted the way consumers consume and interact with other channels.

By the end of 2013, our view was that the impact of digital advertising was still limited compared with, say, TV. This was partly driven by the inability of digital to reach consumers as well as traditional channels. That’s not to say the RoIs aren’t good: we see plenty of decent RoIs from display, online video and Facebook campaigns; however, our optimisers rarely suggest allocating more than 15-20% of budget to online campaigns (and usually less than 10%) because the channel tends to saturate quickly in terms of reach.

Les Binet’s commentary on the famous Cadbury Gorilla commercial sums up this point well (Admap, March 2012). The advertisement has amassed more than seven million views on YouTube since its debut more than six years ago, which sounds amazing; however, it achieved significantly higher reach in just 30 seconds on TV, the first time the ad was aired.

Today, though, we stand on the edge of a major shift in online. Digital channels such as Facebook are talking about reaching even bigger numbers of consumers, on a par with TV. And they are demonstrating how ads can be targeted quickly and how frequency can be controlled better than other channels, leading to less waste and better RoIs. The icing on the cake is that young adults are easier to reach online – something that traditional channels find difficult to do. It will be interesting to evaluate how effective digital is as a medium compared with others such as TV, once the reach of online and offline channels aligns.

Online has started to impact our top 10, mainly by offering additional or different reach to traditional channels. It can also be relatively cheap compared with TV, so media RoIs can usually be improved by switching some budget to online. Hence, we are revising our estimate up for the impact of three of our top 10: budget-setting and allocation, laydown, and media multiplier.
What has become clearer throughout the past eight years is the importance of reach. Of course, this is nothing new, but what we now know about the impact of reach on RoI has grown.

Since 2006, Data2Decisions has amassed a large database of learning across many countries. An analysis of these 1,500+ RoIs shows that countries where reach is higher for TV achieve higher RoIs. It also shows that countries where cost per GRP is lower also achieve higher RoIs. While this is not surprising, it has led us to introduce a new category: budget-setting across geographies.

We believe the opportunity to impact return on global budgets via allocation across geographies is significant and bigger than budget setting within a country or within a brand alone. So this new factor goes straight into the list at number three.

While there are huge gains to be made by taking a global view of budget-setting, many businesses are not set up with a central function to do so. In the cases where we have evaluated the likely gains of allocating budget across countries, the opportunities were significant — on average a multiplier of around five.

There has been a trend towards global brands and we are seeing more businesses starting to take control of budgets centrally. This opportunity to impact RoI via budget setting is one of the advantages of central control and, consequently, we expect more businesses to adopt this approach in the future.

One area where we have done a lot of work since 2006 is budget-setting across portfolios (i.e. all the brands a business might own in one country). Our experience suggests this is a bigger opportunity than previously thought, with an average profit multiplier of three. This is helped by the growth in portfolios since 2006 — acquisitions continue to happen (e.g. Orange and T-Mobile, Dixons, Cadbury, ING), making portfolios both more common and larger and so the ability to impact RoI greater than when we last reported.

Previously, budget-setting was represented in our list as one catch-all factor, which scored a multiplier of two. In the new list, we have split this factor into three separate factors in our new list: geographies (5x multiplier); portfolios (3x multiplier); and brand (i.e. across the different variants within a brand — 1.7x multiplier).

When we talk about budget allocation we also include channels in that definition. Consequently, all of these multipliers have been helped by the growth in digital advertising, which has made allocation across media channels even more important.

There are three ways digital has impacted these RoIs: improved reach — especially the younger audience; lower cost — at the moment digital can often offer good value for reaching consumers; better targeting of individuals — fragmented channels can create smaller, more homogeneous audiences, making it easier to reach a desired audience, which is also true of traditional channels such as TV and print.

Of course, digital also offers a new range of ways to interact with consumers: in our view, we are still building a knowledge base on the value of display, online video/VoD, blogs, social, etc.

Interestingly, the growth in portfolios has some side-effects, which have impacted our factor at number two (and a non-mover in the top 10), namely creative quality, including:

- **Halos:** With larger portfolios working under the same brand name, we have seen advertising halo effects grow over the past eight years, pushing advertising RoIs up.
- **Tagged ads:** We have observed the consistent effectiveness of tagged advertising for a number of clients, often adding 50%-75% to RoIs. Tagged advertising is the practice of tagging on a message for a different brand in the portfolio for the last 5-10 seconds of an ad. So, we might see 25 seconds focused on one product, followed by a further five seconds at the end for another, non-competitive, product in the portfolio. For some clients, the first 25 seconds can be an equity or brand message. Whatever the approach, this type of advertising is invariably effective at pushing up RoIs and is only possible via a client portfolio.

- **New product development:** New products are usually launched with a significant advertising campaign. While launch advertising tends to have a high percentage uplift on sales, the RoI can be low because it is a high percentage uplift on a low base sales level. Portfolios provide protection against this impact by allowing new product advertising to have a large halo impact on the existing portfolio, again helping to increase the RoI.
This all led us to increase the opportunity for creative quality to impact RoI from 10x in 2006 to 12x in 2014.

Our number-one factor impacting advertising effectiveness is again brand size – which convincingly holds on to its top spot. Indeed, we feel it has strengthened its position at the top due to the fact that brands continue to grow in size as a result of internationalisation of brands.

We have talked about the online explosion and the fragmentation of media channels, which have led us to redefine what we previously labelled ‘media multiplier’ as ‘multimedia campaigns’. The various opportunities that digital advertising presents – from search optimisation to online video and social networks – and the way the various channels can be used to extend reach and communicate to consumers in different ways have seen a big change in how media agencies work. No longer are media plans restricted to a handful of channels, rather agencies are starting to talk about media ‘ecosystems’ or ‘connected planning’.

We are also starting to see better RoIs from this approach, so multimedia campaigns is one of the climbers in our list with an increase in cost of implementation.

We have also redefined the category ‘task’ (reflecting the fact that RoI tended to vary depending on the advertising task – equity, promotion, etc.) into ‘product vs. equity vs. season’. We have seen more clients categorise their advertising into one of these three categories and have seen bigger differences in RoI within a brand than previously. Therefore, this category has increased its multiplier from 1.05x to 1.4x and has moved up from ninth to eighth on the list.

All of the above has increased the importance of getting the phasing or laydown of media correct across time. Consequently, its multiplier has increased from 1.1x to 1.15x; however, it has dropped from fifth in the list to ninth, due to the increase in other factors and the redefinitions we have introduced.

A couple of categories have dropped out of the top 10: brand life cycle (1.10x multiplier) and quality viewing (1.04x). Of course, this doesn’t mean they are not important. It just means there are other factors that need focusing on first as they offer a bigger opportunity. Provided the key factors have been sorted out, then an extra 4% on a £10m budget is still very much worth chasing.

We also place frequency planning outside the top 10 (e.g. the practice of setting frequency targets over a fixed period such as ‘maximise 3+ over 4 weeks’). After the 2006 paper, we were asked by a number of people why we hadn’t included the impact of frequency planning in our list. Our view is that this approach to planning is difficult to assess and doesn’t really reflect how consumers respond to advertising (e.g. it doesn’t allow for the impact of carry-over effects). We have trouble measuring the impact of different frequency strategies which suggests to us the effect is small and, possibly, not big enough to cover the increased cost of implementation.

The interesting point is that our new list now has five factors (previously two) that we believe can more than double the profit from advertising. And the factor in 10th position, namely target audience, could still impact RoI by 10% compared with only 4% previously.

The changes we have seen throughout the past eight years since we first compiled this list have, no doubt, made advertising more complex, from creative development through to channel choice and planning.

But this has given us more opportunity for control and a greater understanding of how to make a difference, so we are now in a better place to maximise the payback from our advertising.

However, more than ever, clients need experts to help them get the most from their media budgets – experts who understand the media landscape and how to use it most effectively; and experts to measure, monitor and maximise the payback. Complexity and speed make the communications industry a very different animal to eight years ago.

We think digital is going to have a bigger impact throughout the next eight years than it did throughout the past eight. Digital has grown and stands ready to compete on a more even footing with traditional channels such as TV.

We also expect a trend in budget centralisation and, therefore, allocation across geographies. Once businesses have capitalised on the opportunities to maximise RoI across brands and portfolios, their need to continually improve margins will force them to turn their attention towards centralisation and cross-country budget-setting – especially as this would seem to offer significant opportunities.

We also anticipate clients moving to wider optimisation – not just looking at optimising media on its own, but together with other marketing activity and especially their promotional plans. Promotions cause massive changes in volume and we repeatedly see advertising benefiting from this via bigger volume uplifts. But does it pay to stimulate more volume at a lower price? Do we need to promote and advertise at the same time or would it be better to do these at different times, perhaps using advertising to build loyalty back up after a deep price cut?

These are complex questions which require much deeper analysis – at SKU and retailer level – to answer them with accuracy. But it is something we are starting to do with clients already. So, we may need to update this list much more quickly next time.

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