the many faces of ROI

The hunt for ROI continues

BY MARCIA LAYTON TURNER

PHOTOGRAPHY BY CHAD JOHNSTON/MASTERFILE

Blame it on John Wanamaker. The turn-of-the-century department store icon, who famously wondered which half of his marketing dollars were wasted, started a quest for return on investment that continues to this day.

So far, the results are not pretty. A recent survey found major corporations using no fewer than six different outcomes to measure ROI, everything from incremental sales from marketing to changes in purchase intent.

In fact, the confusion over how to measure ROI is such that the Association of National Advertisers recently joined with the American Association of Advertising Agencies to create a new way of measuring how consumers interact with marketing.

"In this age of accountability, new metrics are necessary to adequately reflect the impact of nontraditional messages," says Barbara Bacci-Mirque, senior vice president of ANA.

MASSIVE CALCULATIONS LEAD TO PREDICTABLE RESULTS

So, what's a beleaguered ad executive to do? Some are turning to econometrics, a highly sophisticated statistical modeling method that has the industry talking. Supporters say it can help companies determine ROI, predict outcomes and optimize their marketing spend.

Critics say something along the lines of, "yeah, right."

Essentially, econometrics involves stuffing a database with historical data (usually one or two years' worth) on sales, marketing spend, product enhancements, even outside factors such as weather or seasonal effects. Unlike other statistical modeling programs where you pick and choose what goes into the analysis, econometrics takes everything you have.

It sounds simple, but it requires a massive number of calculations and a boatload of data.

"You go through tens, maybe hundreds of thousands of different models with an automated statistical modeling process and you'll eventually come up with the right fit," says Randy Stone, chief executive officer of Marketing Management Analytics Inc. (MMA), a consulting firm based in Wilton, Conn. "It's like a pattern-matching test. You measure everything that was happening during a period of time, including marketing campaigns, competitors' activities, the economy, even the weather."

Econometrics finds relationships among all the data being analyzed, and that allows it to make predictions.

Once you understand how two factors, say sales and television ad spend, relate to one another, that information can be used to make predictions: Increase your spending X percent on television advertising and sales will jump Y percent.

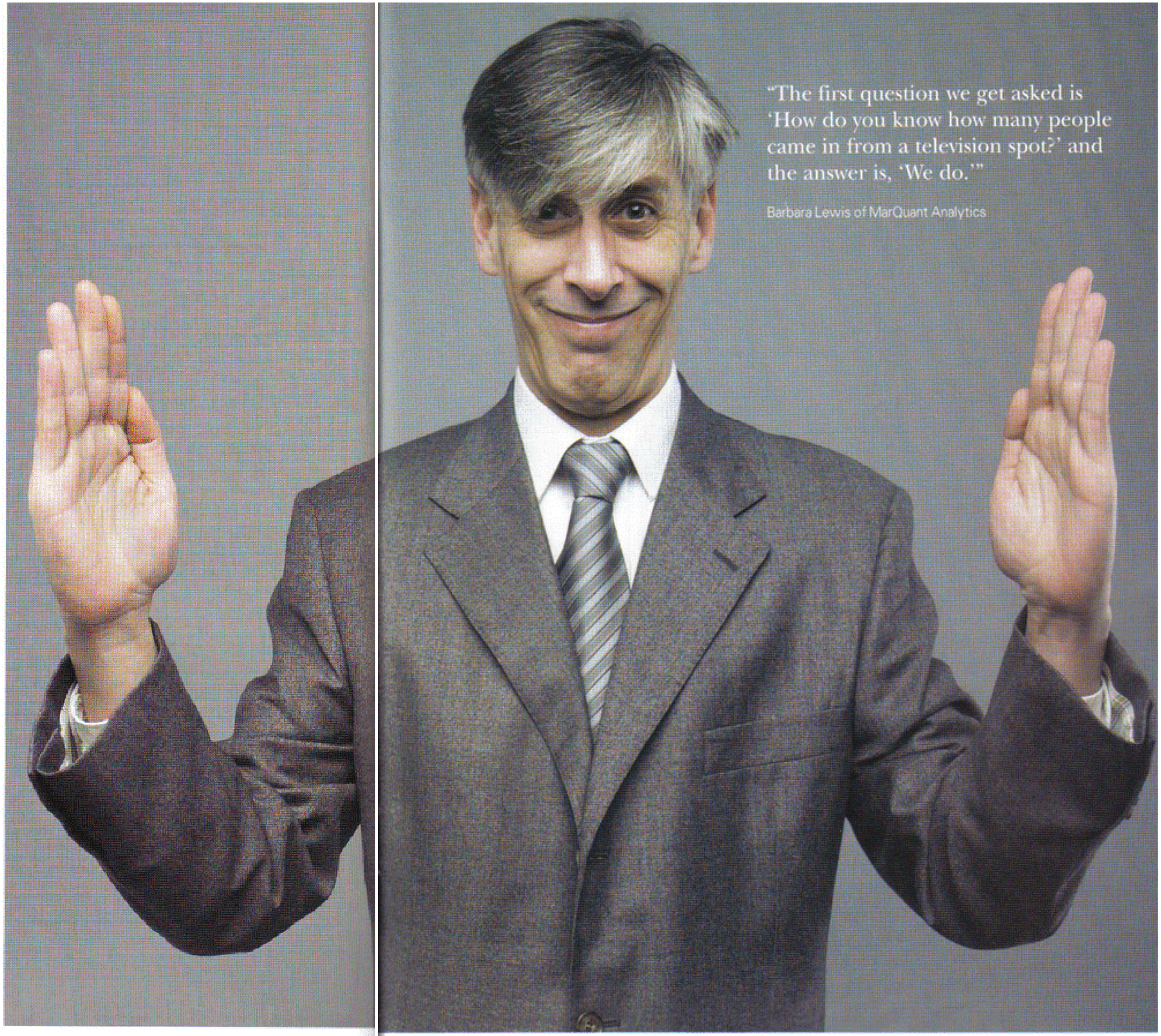
If it all sounds a little too good to be believed, well then, Barbara Lewis understands. "The first question we get asked is 'How do you know how many people came in from a television spot?' and the answer is 'We do.' Through analysis of all the data across many weeks, we're able to tease out the effects of the television spot on the number of customers," says Lewis, president of MarQuant Analytics, a Beverly Hills, Calif., firm that consults with companies to capture, measure and analyze data.

Lewis adds that once she and her colleagues run through the numbers, though, the skeptics become converts. "They see the process and they understand," she says. "Then they start to get excited."

She cites the example of a financial services client who uses econometrics to decide what to spend on marketing activities, its products, each region of the country and even on certain types of customers.

It's that ability to provide statistical insight into decisions that used to rely on gut instinct that has marketers intrigued.

Well known in academic circles for years, econometrics



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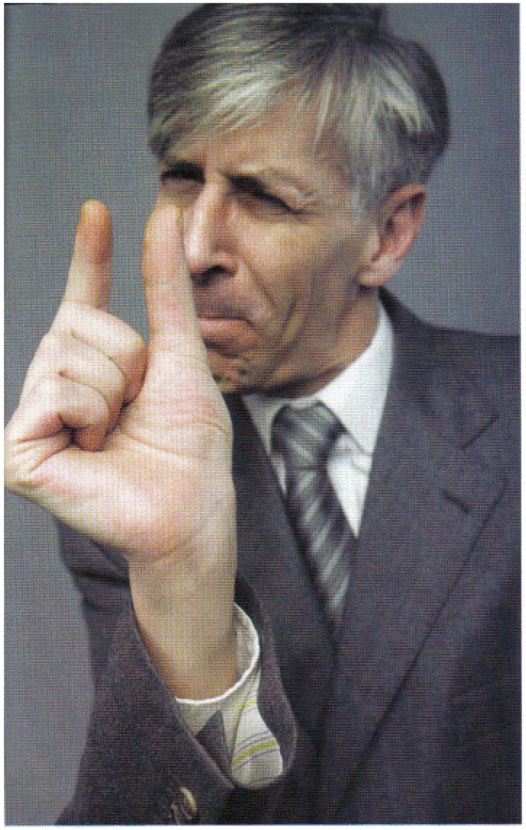

has only recently become the darling of the analytics set, thanks mainly to the massive amount of data that companies now track and the leaps in technology that make it possible for a laptop computer to run calculations that used to require a supercomputer.

A number of European companies have adopted the process, but U.S. corporations have been slower to follow.

Interestingly, Lewis notes, when doing analysis for the clients she works with — a gamut of blue-chip names — direct mail consistently has a high return compared to other marketing channels. "That might not be true for every company, but it is for the companies we work with," she says.

LOOKING BEYOND ROI

But determining pure ROI isn't the only game in town. Companies are also seeking budget optimization to get the maximum lifetime value out of their customers. It's part of a movement in the marketing world to look at return on customer, or customer equity, she says.

"They're not just looking at ROI," says Lewis. "That's short term; they want long term as well."

Sometimes, for example, the corporation's long-term interest is in gaining market share, she says, and it is willing to take a loss on its marketing in order to gain customers.

She also notes that larger corporations, with huge budgets and massive amounts of spending, tend to find the most value in econometrics.

"They spend hundreds of millions on their marketing budget and the authority is so big, they can't get their arms around it," says Lewis. "They can't figure out what's working and what's not working."

Right now, she says, most discussions about econometrics are happening with the analytics departments within corporations. Charged with finding ways to optimize spending, those departments are looking for a scientific method that can help them produce results.

Ultimately, though, those conversations need to include representatives from the financial side of the business — the people asking about return on investment — so they too can understand the way that marketing efforts can pay off for a company.

"We'd like to be talking at the chief financial officer level," says Lewis.

FOLLOW THE NUMBERS, BUT TRUST YOUR GUT

Not everyone is sold on econometrics, however.

Because econometrics focuses on what your company is doing right now, it may not be as helpful if you are launching a new product or expanding into a new territory, cautions Mark Dominiak, principal strategist at Insight Garden, a Whiting, Ind., marketing consulting company.

Consultant Erwin Ephron takes it a step further.

"Econometrics ROI is a backward-looking measure, as you can only tell what you have done," says Ephron. "You can't do econometrics modeling unless you have extremely good disaggregated data. It only tells you about what you did, not what you want to do."

Use it as an aid to making marketing decisions, but not as a replacement, says Ephron.

Marketing Management Analytics' Stone agrees. Don't rely solely on the numbers, he says, trust your gut, too. "Combined, you have a winning proposal. Don't allow the model to be the dictator."

Still, in a world of maybes, econometrics holds the promise of being one model that can actually help corporations get a handle on exactly what they get in return for the marketing dollars they spend.

"We are looking for the ideal budget: How should the company allocate its funding," says Lewis. "And econometrics can help us find that answer."