Calculating Return on Marketing Investment (ROMI)

By Ian Rheeder, CM (SA), MSc (April 2021)

ROMI has fast become the number one metric and your ticket to the boardroom

In a more fragile economy, understanding how to calculate ROMI has never been more important. Through marketing (which should lead every facet of an organisation[1]), everything either improves or decays. Fittingly then, knowing how to calculate ROMI will fix many of the confidence issues facing marketing managers.

Marketing Not Allowed Into The Boardroom

Looking at the most comprehensive marketing leadership study ever undertaken[1], we cite that not knowing how to have a high-level ROI conversations in the boardroom is the biggest weakness of a marketing and sales manager.

> *"Woe to the company whose marketing is still siloed."* -- M. De Swaan Arons[2]

Not capable of talking the ROI language causes the marketing manager to shy away from discussing marketing with all departments. It's also the reason marketing is so often siloed and not assured a position in the C-Suite. Ironically, even though we know that marketing is far too important to be left to just the marketing department, this is still the case—marketers are isolated because they're known to just "wing" it. Aligned to this opinion are Philip Kotler's *Ten Deadly Marketing Sins*[3], where all his sins are all *company-wide* issues; issues caused by marketing not embracing a company-wide approach.

ROMI To The Rescue

Why are the South African based Nando's and Barloworld Equipment (Caterpillar) marketing managers so valuable to their organisations? Both admitted that they calculate ROI on every single marketing initiative. What's more interesting is Doug Place at Nando's spends 50% of his marketing budget internally on staff. It's easy to work out your ROMI (says Doug) when your calculation factors in the savings (return) on reduced staff turnover, reduced training costs, higher quality food, less theft and higher productivity. Imagine how respected he is in the boardroom when the HR director and CFO listens to his ROI language. All of a sudden marketing is allowed to get deeply involved in people, processes and other Ps besides promotion. Why? Because everyone now understands that you understand what's going on regarding the bottom-line.

> *"Measurement is the first step that leads to control and eventually to improvement. If you can't measure something, you can't understand it. If you can't understand it, you can't control it. If you can't control it, you can't improve it." H James Harrington (Author: Business Process Improvement)*

So What is ROMI?
ROMI (%) measures the **net profit or savings** ($ output) from a marketing initiative ($ input). It is important to look at the short and long-term ROMI effects too. By calculating your ROMI on each activity (even future activities like sales) senior management can easily make decisions on your entire marketing mix.

With validated data (i.e. a 5% increase in employee engagement equates to 3% increase in sales; or if a 1% increase in Top of Mind Awareness equates to 1% increase in market share), we can easily start calculating ROMI. For instance, at BMW we know that there is a 70% chance of selling a car if they just got someone to test-drive it. Or knowing your conversion rate for sampling is always 2%. Knowing these validated statistics makes calculating ROMI really easy. ROMI thus offers a way to prioritize your budget on a scientific basis. With calculations like this, marketing investments can be redirected away from under-performing initiatives to better performing investments like "people" or even corporate social investment (CSR) initiatives. During Covid-19 many companies were looking at long-term brand equity targets (i.e. loyalty or customer-lifetime-value or customer equity), knowing full well that after the pandemic they would generate positive ROMI. It's important to have a short term ROMI and long-term approach too.

The long-term "horizon" (i.e. 5-year) calculation is more sophisticated. It's more complex because one needs to factor in repeat purchases, word-of-mouth, retention rates, risk, and discounted cash flows; however, with the Excel spreadsheet tool (available from Markitects), the calculation is made easy.

Warning
Unfortunately ROMI is difficult to calculate when you don't have a research budget, or when you are running many campaign simultaneously. So always using ROMI as a criterion to determine your entire integrated marketing communication (IMC) budget is questionable. Sometimes your gut-feel might be your best judge when you are "winging it". If this is the case, you must still attempt to calculate your ROMI and at least aim for a 0% ROI estimation. Note that a zero % ROI means you did not lose money. What is recommended though, eliminate programmes with a negative ROMI.[5]

Do you know how to forecast fairly accurately?
Baseline: One of the basics for calculating ROMI is knowing your traditional *baseline* of sales. Crucial to your calculations is using analysed *past* sales data (the *seasonal indexing* forecast method) together with your most *current* sales data (*naïve* forecast method), to forecast the *future* baseline period. Anything above the baseline forecast can then be attributed to *incremental sales* due to your marketing investment (this can also be validated through your targeted research or scraping off Google statistics).

Context: It's important to also have the micro-environment (4C: Company, Customer, Competitor, Channel) and macro-environment (PESTGEL) discussion with the board when agreeing on your current baseline. The "G" (i.e. "Global" Covid-19 pandemic) can drop your baseline by 70%. Or a "Competitor" closing their doors can improve your baseline.

Calculating Seasonal Indexing is really easy, and shouldn't take you longer than 30-min. All you need to do is input you past sales data in the Markitects Excel tool.

Practical Case Studies
Most managers are either untrained or too scared to calculate ROMI. A leading FMCG marketing director once said to me that all her marketing initiatives ran at a positive ROI or she would have been fired long ago. We took her biggest campaign spend (R15 million incremental vs. previous year) for one of her products and calculated a -99% ROMI (that's minus 99%). She should have had massive feedback from her board on how she was destroying shareholder value! Here's the problem; nobody in the organization cared that she did almost zero extra sales for spending an additional R15 million. Why? Because nobody was discussing ROMI. No one cared *until* ROMI (-99%) was presented to the board. We will show you this exact case study on the ROMI training.

Summary
Mathematician Lord Kelvin once said "To measure it is to know. If you cannot measure it you cannot change it." Business consultant Peter Drucker said "What gets measured, gets done."

It's often said that "50% of marketing is working… I just don't know which 50%." So make it your aim that after ROMI training you will start calculating what is working and what is not working. Decide which projects are worthwhile *across the entire organization* and watch the respect for your designation soar.

Start measuring, and gain your valuable seat in the boardroom.

References:
1. EffectiveBrands did their Marketing2020 study; they surveyed 10,000 marketing executives from 92 countries, using 80 questions; and compared high-performing and low-performing organisations. (Ref. Harvard Business Review, Jul-Aug, 2014, p.57)

2. De Swaan Arons, M., Van den Driest, F. and Weed, K. (2014). *The Ultimate Marketing Machine*. *Harvard Business Review*, Jul-Aug, 2014, p.55-63

3. Kotler, P. (2004). Philip Kotler's *Ten Deadly Marketing Sins*. John Wiley and Sons.

4. Harrington, H. (1987:43). The Improvement Process: How America's Leading Companies Improve Quality. s.l.:McGraw-Hill,.

5. Farris, P.W. et al. (2006:321). Marketing Metrics. Wharton School Publishing.

Ian Rheeder -- Chartered Marketer (SA), MSc (MOTI)
GIBS Adjunct Faculty, Owner Markitects
ian@markitects.co.za; Cell: +27(0)83 300 8080