

The impact of advertising practices on sales marketing essay



With companies investing millions of rupees in advertising it is natural to examine its impact on the bottom line of the firm. Researchers are now more inclined and have diverted their attention towards examining the impact of advertising practices . Moreover, interest is rising in quantifying the impact of advertising practices on firm's profitability and Sales. This study focuses on studying the relationship of the impact of advertisement spending by firms on firm profitability and the effect on firm's sales. A total of 50 firms are taken as the sample size and we find evidence that while the impact is significant in statistical terms, incremental advertising practices has not contributed as many people have assumed in their minds.

In today's era one is constantly bombarded with all sorts of advertising. Studies show that advertisements have an influence or an effect on the purchase behavior of consumers. Consumers are looking for a product which adds " value" other wise they wont be able to differentiate between products. Consumers expect a return on investment. In other words, they expect value for each rupee they spend. At the other end the businesses expect a return on the investment they make on advertising. This is natural given the fact that promotion activities do cost the firms a lot. This return can take a form of increased profits or sales ratio. We can find each year companies investing millions of rupees in these activities. A bulk of this obviously goes into advertising budget. Naturally, marketers expect a return on investment on this. Their expectation stems from the likely impact, marketing investments have on the market performance and thus the sales of the firm.

Raymond (1970) believes that the effectiveness of advertising portrays different illustration to different groups. To a general manager it would be the impact of advertisements on organizations profits ratio. With marketing tools used for creating awareness and building a long lasting relationship, many studies have focused on copy and media effects and awareness building about the product. Metrics have been developed to assess and measure consumer awareness and loyalty. Few research studies concentrate on measuring the sales and profit effects (Gattignon 1993; Mantrala, 2002; Naik et al, 2007). A cursory glance at this suggests that these effects have been studied on the US consumers and markets. It therefore is imperative to study the impact of spending on advertising practices and its on impact on sales in case of Pakistani firms.

Statement of Problem

“ The Impact of Advertising Practices on Sales”

Advertising play vital role in creating product demand and market share. It connects the consumers by highlighting the versatile characteristics of the products that consumers may not know them before. Advertising create an urge for the products and consumers are virtually on the search for such products until they can actually consume and test them. Now in new millennium, even a tiny firm or a small country can use such techniques of advertising through dynamic media and information technology and can advertise across the globe in a matter of seconds. Firms or countries which were unknown before and had hardly any imprint or impact on global market place, now creating enormous demand for their products and services through media and information technology. But on the other hand many

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companies are not aware of the type of impact they have on their sales pattern.

Questions arise whether advertising adds value to the firm. With little research focusing on this aspect we concentrate our study towards this end. Our objectives can be summarized as

Does advertising add value to the firm?

Impact of advertising on Sales of the firm

Differences between the impact both in degree and time across the industry

Implications for the marketers.

Literature Review:

All advertising neither is nor designed to lead directly to sales. For example, some advertising may be aiming for long-term brand-image building. Whether it is designed for short-term or long-term purposes, advertising helps to grow or make at least stagnant sales (Sinha, Mantrala, and Zoltners 1992; Vidale and Wolfe 1957, Naik, Mantrala, and Sawyer 1998). Thus advertising is used independently to measure a change in sales (Lilien 1994). According to Abraham and Lodish (1990, p. 50), however, a real and important issue in advertising effectiveness is “ the incremental sales of a product over and above those that would have happened without the advertising or promotion.” If short-term advertising can result in a sustained high level of sales, the company is “ getting the most out of advertising.”

Although advertising managers have long considered the idea that

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advertising's impact on sales may persist longer compared to the current period "intuitively attractive" (Clarke 1976, p. 346), many of them still consider that advertising's effect on sales is for a shorter period. They also hold that, in all cases, more and longer uses of advertising are finer than less and shorter uses of it-whether or not advertising is directly boosting sales (Jones 1992, 1995). Abraham and Lodish (1990) suggest that, as a result, much advertising is wasted, largely due to the lack of measures that can show the manager the impact of short-term advertising on long-term sales. Because of our inability to isolate advertising effects from other effects, and to quantify such effects, Bass (1969, p. 291), among many others, lamented, "There is no more difficult, complex, or controversial problem in marketing than measuring the influence of advertising practices on sales."

In the past, many studies have been performed, trying to determine the major factor of influence on Sales. Early work on the advertising & Sales relationship tended to regard advertising as a barrier to entry, see Kaldor (1950), operating through its impact on product differentiation. In Comanor and Wilson (1974), Williamson (1963) and more recently in Kessides (1986) and Pitelis (1991) advertisement has been studied through its role as investment in excess capacity.

Every month, billions of rupees are spent on advertising and it is one of the most powerful forces for good or evil. It is considered good because media and advertising have positive impact on market demand, sales and market share. Duffy (1991) found that advertising has impact on the composition of aggregate consumer demand. It is considered evil because billions of rupees are wasted just to sell the same products and services by misleading
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consumers and misallocating resources. It is even more serious when the burden of such exploitation are borne by the very victims , the consumers and tax payers who have been already suffered because of such imposed advertising war on them.

Advertising changes the structure of the economy. Muller and Hamm (1974) have found that the structure of the economy changes and concentration tends to increase rapidly with high advertising intensities. Such findings reveal that advertising is one of the single most powerful tool in shaping consumer demand.

Repetitive advertising creates an appeal and also retention to the consumers and increases sales. Ehrenberg (2000) believes that advertising has extraordinary power, and in most time, it is effective. Such extraordinary power if unleashed to the consumers who are often not well informed about the different features of the product or service, they may easily be gathered.

Since competition among firms is growing, their main goal is to define their strategies in order to achieve maximum performance, resulting in greater accelerative sales. In the past, many studies have been performed, trying to determine the major factor of influence on industry sales. Early work on the advertising, sales relationship tended to regard advertising as a barrier to entry, see Kaldor (1950), operating through its impact on product differentiation. In Comanor and Wilson (1974), advertisement has been studied through its role as investment in excess capacity.

The relationship between advertising practices and Sales is perhaps the most-studied single phenomenon in business policy. Although, it has been <https://assignbuster.com/the-impact-of-advertising-practices-on-sales-marketing-essay/>

some decades since the first published studies report a positive market share profitability association (Gale, 1972, Shepherd 1972), the nature of this relationship continues to receive a great deal of attention (Buzzell and Gale, 1987, Jacobson 1988a, Cool et al., 1989, Boulding and Staelin, 1990, Venkatraman and Prescott, 1990 Schwalbach 1991, Szymanski et al., 1993, Fraering and Minor, 1994). While we observe that many practitioners hold the view that higher market share leads to higher profits, research findings indicate that the market share-profitability association is dependent upon strategic and competitive settings, and spurious effects account for at least a sizable component of the measured association. From all these, the following question arise: is the pursuit of market share an appropriate strategy for the increase of firms' profit? Business strategists are divided on this issue. Some studies indicate that low share businesses can be quite profitable (Woo, 1982, Schwalbach 1991). Moreover, a spurious correlation between Advertising practices and Sales has been found by Jacobson (1988a), Rumelt and Wensley (1981) and Jacobson and Aaker (1985). On the other hand, the dominant finding of prior research is a significant positive relationship between market share and profitability. O'Regan Nicholas (2002) has shown that firms with increased market share are likely to have higher performance and in particular achieve enhanced financial performance, greater customer satisfaction and overall incremental sales. This applies to all firm sizes. To ensure competitive advantage, firms need to consider market share in conjunction with overall profits.

Scholars support two schools of thought about the effects of advertisement as a competitive factor. In the first school of thought (industrial economics)

advertisement is considered as a factor of product differentiation particularly when the latter is plasmatic. It has been proved that advertisement increases sales and reduces consumer welfare by creating product differentiation (Caves and Williamson, 1985) and barriers to entry (important sunk cost). That type of differentiation appears only in markets of imperfect competition. Another school is focused on the informative character of advertisement, claiming that advertisement makes markets more competitive and reduces market share by supplying consumers with information about price and quality (Greuner, Kamerschen and Klein, 2000).

(Taken from advertising and market share in greek)

Marketing persistence measures the extent to which a relatively short-term change in the marketing mix, such as advertising expenditures, leads to a long-lasting effect on sales (see, e. g., Dekimpe and Hanssens 1995a, 1995b, 1999; Mohrle 1997; Simon 1997).

Although it has been only recently applied to marketing, hysteresis, or persistence, has attracted increasing attention because it offers an innovative perspective on the important issue of effective long-term marketing resource deployment. If companies can measure how incremental sales are gained without additional advertising expenditures, scarce resources can be saved for other purposes (Slywotzky and Shapiro 1993).

THE LONG-TERM EFFECT OF ADVERTISING PRACTICES ON SALES

Reviews of the relevant literature (e. g., Baghestani 1991; Bass 1969; Bass and Clarke 1972; Chowdhury 1994; Clarke 1976; Dekimpe and Hanssens
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1995a, 2000; Little 1979) find that the key reasons for this belief are that, unfortunately, past research showed little evidence of the effect of short-term advertising practices on long-term sales, and research that did show that short-term activities created long-lasting effect was largely anecdotal.

A typical approach was to assume that a fixed fraction of the effects in one period is retained in the next (Clarke 1976). But this approach cannot estimate the persistence effect of advertising practices (Dekimpe and Hanssens 1995a). Cross-sectional designs have also been used to study the long-term impacts of marketing activities (e. g., Bass, Cattin, and Wittink 1978; Urban et al. 1986), but they cannot consider events that happen over time or infer how short-term dynamics translate into long-term equilibria. Aaker, Carman, and Jacobson (1982) examined the sales-advertising dynamics involving feedback. Helmer and Johansson (1977), Leone (1983), and Doyle and Saunders (1985) studied the dynamic impact of advertising practices on sales based on the Box-Jenkins transfer-function analysis. Although those studies used time-series techniques, they are mainly data-driven (Dekimpe and Hanssens 2000, p. 184) and unable to perform persistence estimation

Due to modeling limitations, long-term advertising effects are often either completely ignored in an evaluation, or counted as some sort of “invisible bonus” or “added values” (McDonald 1992, p. 55).

In an attempt to address these limitations, Dekimpe and Hanssens (1995a) devised a marketing-persistence model to examine advertising, sales, and gross margin data for a 76-month period from a large home-improvement

chain. They concluded that the “ net effect shows that current advertising investments result in a positive dollar inflow in the long run” (p. 14).

In another study that applied their marketing-persistence model, Dekimpe and Hanssens (1995b) collected 46 studies using univariate time-series marketing and sales data published in leading marketing and advertising journals (e. g., Journal of Advertising Research, Journal of Business Research, Journal of Marketing, Journal of Marketing Research, Marketing Science) between 1975 and 1994 to perform a meta-analysis. They found that 72% of the North American consumer goods in their sample were “ evolving,” that is, sales remained at increased levels for a long-lasting period after the advertising was withdrawn. Their small sample size, however, prevented them from comparing the impacts of advertising on durables and nondurables. Nor did they quantify persistence.

More recently, Ouyang, Zhou, and Zhou’s (2002) study, by applying a marketing-persistence model, showed the existence of a long-term impact of advertising practices on the sales of consumer durables in China. They suggested that more research is needed to compare the persistence phenomena in the durables and nondurables markets.

The literature on advertising and consumer behavior has long suggested that consumers’ processes in receiving, using, and retaining advertising information to assist their purchase decision making is very different for high- and low-involvement products (Assael 1998; Bloch 1982; Bowen and Chaffee 1974; Duncan 2002; Krugman 1965; Muehling, Laczniak, and Andrews 1993; O’Cass 2000; Shimp 2000; Slama and Tashchian 1987;

Vaughn 1980, 1986; Zaichkowsky 1986). Relevant to this study is the view that consumers are generally more highly involved and selective when making a purchase of durable goods than when purchasing nondurables because they are more concerned about reducing risk when purchasing durables. As a result, advertising tends to create a long “memory” effect in the minds of buyers because “thinking” is the key element in the hierarchy of effects (Vaughn 1980). Consequently, consumers are supposed to remember past advertising and develop “goodwill” toward the advertised brands if their experience with the brand has been positive (Givon and Horsky 1990). It has also been suggested that the dynamic impact of advertising on sales can work indirectly through purchase reinforcement: Advertising gives consumers an incentive to make both an initial purchase and repurchase (Horsky and Simon 1983). Thus, buyers tend to stick to the brands they have purchased before.

On the other hand, consumers often feel little involvement in buying nondurable products because they are frequently purchased, inexpensive, and have few differentiating attributes. Buyers may not search for information before purchasing a nondurable product, and it is difficult for them to form real attitudes or strong preferences toward a brand afterwards. In this case, consumers are a passive audience to advertising and pay little attention to ads before the purchase. Even if they catch product information in ads before buying the product, they may forget it quickly after the purchase (Krugman 1965). “Reacting” is a more important element than “thinking” in the low-involvement hierarchy of effects (Vaughn 1980). As a

result, it takes repeated advertising to build up and maintain brand image and sales. Typical example is soft drink advertising practices.

Persistence Modeling

According to Dekimpe and Hanssens (1999) and Hanssens and Ouyang (2000), there are four possible persistence scenarios to depict the relationship between advertising Practices and sales:

- * “ business as usual” (“ zero” persistence, stationary): temporary advertising activity that creates temporary sales results;
- * hysteresis (full persistence, a theoretical extreme): temporary advertising activities that result in sustained sales changes;
- * evolving business practice (partial persistence): sustained advertising activities that are accompanied by persistent sales, and;
- * escalation (negative persistence): sustained advertising activities that are nor accompanied by increased long term sales, due to unexpected factors.

In their attempt to examine these scenarios, Dekimpe and Hanssens (1995a, 1999) first performed Augmented Dickey-Fuller unit root tests to determine if sales are stationary (zero persistence) or evolving. For identified evolving cases, VAR (Vector Auto-Regressive) models were used to examine the long-term relationship between sales and advertising, in which the impulse-response function of any pair of variables (X, Y) was used to detect persistence, defined as the permanent effect on Y of a one-unit (or one

standard-deviation) shock in X. The shock of X on Y can thus be isolated from other sales drivers.

This approach produces numerical and visual paths of impulse-response weights that can be used to simulate the sales and profit consequences of a specific advertising activity. In other words, it derives the total long-term impact of, say, a defined advertising campaign in that an initial outlay receives credit for all subsequent effects from it. This is the empirical evidence of the hysteresis effect described by Little (1979). As reduced-form parameters, however, these paths cannot be cast in a dynamic optimization framework, because VAR is unable to indicate causal order and the estimated parameters cannot be interpreted directly (Hall, Lilien, and Johnson 1994).

Several researchers have also studied the long-term effects of marketing activities. Franses, Kloek, and Lucas (1999), for example, considered econometric modeling of weekly observed scanning data on a consumer brand. Srinivasan, Popkowski-Leszczyc, and Bass (2000) examined the long-term effects of temporary, evolving, and structural changes of prices on the level of market share.

Practitioners are getting slowly under pressure to report their contribution to the overall firm performance. The inherent complexity in quantifying the marketing activities has often become a hurdle in developing metrics for marketing measurement. O'Sullivan and Abela (2007) report that the ability to measure the internal marketing performance causes a significant impact on firm performance.

In recent years a number of studies suggest that a firm's advertising (Frieder and Subrahmanyam 2005; Grullon, Kanatas, and Weston 2004; Joshi and Hanssens 2007,) directly affects sales. This is in addition to the indirect effect of advertising practices through increase in sales revenues and profits. Srinivasan and Hanssens (2007) carry out an extensive literature survey on the impact of advertisement on sales.

The impact of the advertisement on consumers rests on the theory of message repetition again and again. It can be classified into 3 main effects:

- A). Current effect on behavior,
- B). Carryover effect on behavior and
- C). Non behavioral effect on attitude and memory

(Sawyer 1981; Pechmann and Stewart 1988; Sawyer and Ward 1976).

Researchers have tried to estimate the effects of advertising practices on brand sales using field data (Leone and Schultz 1980; Ambler and Vakratsas 1996). Most of these studies focus on many issues involved in efficiently capturing the unbiased effects of advertisements, given the limitations of field data (Parsons, Hanssens , and Schultz 1990). Deeper analysis of these studies finds that the effects of advertising are greater than zero but do vary by market and product characteristics (Farley, Assmus , and Lehmann 1984; Sethuraman and Tellis 1991).

Only few studies have addressed the effect of advertising effects on sales.

Little has been researched on focusing the impact of how the effects vary by

creative medium, and time of day for broadcast advertising (e. g., Bhattacharya and Lodish 1994). In particular, no study has researched the effects of advertising by these three factors simultaneously. While marketers know that that consumer behavior is influenced by multiple factors, yet little amount of research has been done on understanding the impact using the integrated marketing mix model (Sethi 1977, Feichtinger, Sethi Hartl, 1994). This is attributed to the fragility of advertising's effects and the complexities involved in getting bias-free estimates.

Naik and Raman (2003) present an insight as to how a marketer or a shareholder is keen on measuring the impact of marketing (advertising) on sales.

To assess these effects marketers often use regression analysis. Arguing that OLS models introduce biasing effects, they put forward the Weiner Kalman Filter(WKF) that provides estimates that are closer to the true parameters.

Advertising's effectiveness lies in its capability to help stimulate or maintain sales (Eachambadi 1994; Mantrala, Sinha, and Zoltners 1992; Naik, Mantrala, and Sawyer Sethi 1998; Vidale and Wolfe 1957). Thus, advertising is frequently used as an independent variable in explaining changes in sales (Lilien 1994). Abraham and Lodish (1990) believe that advertising effectiveness has to be captured by the additional sales of a product over and above those that would have happened in absence of any advertising or promotion. Although advertising managers have long believed that advertising's impact on sales can persist longer than the current period (Clarke 1976), the tendency to assume that advertising's effect on sales is

short-term is yet prevalent. They further argue that the longer uses of advertising are better than less and shorter uses of it irrespective of the nature of contribution of advertisement to sales (Jones 1992, 1995). The inability of measures to differentiate the impact of advertisement between its short term and long term effects have resulted in wastage of advertising expenditure (Abraham and Lodish, 1990; Bass 1969). Eechambadi (1994) uses the analogy of capital budgeting process to capture the effectiveness of ad spending on sales and profitability. He suggests that the brand managers be allowed to spend as much as they want on advertising if the return they generate is able to beat an internally agreed hurdle. His belief rests on the premise that absolute size of the ad budget does not matter but the return on that budget is the criteria for ad effectiveness.

The basic duopoly model leads to an equilibrium which can be determined analytically (Dixit, 1979); this basic model does not demonstrate any dynamic behavior. Introducing advertising into the model allows firms endogenously alter demand which does invoke dynamic behavior but is analytically intractable. Graham and Ariza (2003) present a model that optimizes allocation of firm advertising expenditure using a simulated annealing approach. Sterman et al (2007) use an approach that combines duopoly theory with the behavioural theory of the firm.

Luo and Donthu (2001) apply DEA - Data Envelopment Analysis - to the question of how to measure the efficiency of the advertising in the traditional media. Further Yunjae Cheong (2006) uses the similar model to carry out a study on the evaluation of ad media spending efficiency. This model focused on how one could measure, maximize and benchmark the effects of
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advertising media spending thereby improving the effectiveness of advertising and hence increasing sales. Yew, Keh and Ong (2005) report that intensive investment in advertising contributes positively to the one-year stock market performances of non-manufacturing firms.

However their results were inconclusive whether manufacturing firms benefit from investment in advertising as measured by the three-year stock market performance. Mathur and Mathur (1995) using event study methodology concluded that investors react positively to announcements of advertisement changes leading to higher market value for the firms.

Graham and Frankenberger (2000) examined the asset value of advertising expenditures of 320 firms with reported advertising expenditure for each of the 10 consecutive years ending in 1994, seeking to determine the impact of advertising expenditures on the Sales Performance

(Taken from advertising and firm value)

The impact of technological revolution in media and advertising contributed a great success in boosting the demand for both traditional and non-traditional goods and services, including travel and tourism, education, medical treatments, entertainment and a host of other goods and services. Everything is happening so fast that many firms and countries are facing constraints to match the supply with unprecedented demand response.

Isolation of advertising and long term effects

As pointed out by Bass (1969) and Dekimpe and Hanssens (1995a), past studies on the sales-advertising relationship were not designed to answer

the following two questions: How do we isolate advertising's effects from other effects? How do we quantify the long-term effects? There was a need for new modeling approaches that address these types of questions (Leeflang and Wittink 2000). In our study, we have presented a persistence model that both distinguishes and quantifies the long-term effect of specific underlying marketing actions.

Methods used in previous studies (such as autocorrelation analyses, etc.) were not capable of dealing with evolving marketing variables; they were limited within the scope of stationary variables. Our method, by using unit root tests, deals with nonstationary variables. Furthermore, VAR used in Dekimpe and Hanssens (1995a) did not indicate causal order and interpret estimated parameters directly. The cointegration tests used in our method proposes a solution to these problems and produce directional and quantitative results.

Our results show different advertising impacts on sales. These results support Ouyang, Zhou, and Zhou's (2002) findings. The results also support observations made in the literature on consumer behavior and advertising that the dynamic evolution of sales is related to the consumer's level of involvement with the product in making purchase decisions (see, e. g., Assael 1998; Givon and Horsky 1990; Krugman 1965; Muehling, Laczniak, and Andrews 1993; Shimp 2000; Slama and Tashchian 1987; Vaughn 1980, 1986; Zaichkowsky 1986). It is believed that only when there is a persistent relationship between a brand and the buyer will there be a persistent effect of advertising on sales of the brand, and vice versa. Accordingly, we have several suggestions for advertising managers who have the important goal <https://assignbuster.com/the-impact-of-advertising-practices-on-sales-marketing-essay/>

of gaining the most long-term market productivity from advertising expenditures with a defined budget.

First, periodic instead of continuous advertising is more cost-effective for consumer durables such as those studied here. Since buying frequency is low and the consumer's decision-making process is complex, a think-act hierarchy, or an involved consumer, is assumed. That is, to reduce risk, the consumer will commit to an extensive information search and a long thinking process, and will look at familiar brands, if there are any. His or her subsequent behavior is purposeful, resulting from insight and a belief in the brand, not from a random or impulsive act (Mulvey et al. 1994; Wells and Prensky 1996). A highly involved consumer tends to have a good memory for a relevant advertising message. Due to this lag effect, the message does not need to be repeated often if it can build a brand image in the consumer's mind successfully.

In contrast, a relatively more continuous or sustained advertising campaign is more suitable for consumer nondurables such as those studied here. Since buying frequency is high and little decision-making processing is involved, consumers do not actively seek product information; instead they tend to use whatever information is handy to them, and may "just do it" without thinking before or after the purchase (Beatty and Kahle 1988). As a result, to a large extent advertising is not expected to create more than temporary effects (Hoyer and Brown 1990). Whenever advertising stops, the successfully pushed-up sales tend to drop back quickly to the prepromotion level. Brand attitudes, if any, tend to be formed on a noncognitive basis (Mulvey et al. 1994). When such is the case, frequent advertising with a <https://assignbuster.com/the-impact-of-advertising-practices-on-sales-marketing-essay/>

direct selling message is needed to stimulate consumers to make repeat purchases. To encourage repeated purchases, marketers take many short-term actions, such as price promotions, coupons, displays, and repetitive advertising.

This is not to say, however, that image-building advertising is unimportant for low-involvement products. On the contrary, it may be even more important. As Assael (1998) points out, although consumers buy first, they may evaluate a brand after the first few purchases, when brand belief or brand loyalty may be formed. Even the most well-known brands rely on a combination of periodic brand-image advertising and frequent-reminder advertising to stay competitive. In recent years in the cigarette industry, for example, marketers from Philip Morris decided that the grand cowboy image of its flagship brand, Marlboro, had to go hand-in-hand with price promotions. Although the company did not dispense with the cowboy image, it downplayed it. Due to the many choices buyers have in the marketplace, the company let price promotions become a more dominant part of the marketing strategy for its frequently purchased product (Assael 1998).

Finally, the foundation of the persistence concept is that a single phenomenon—a “shock”—can lead to permanent change. In marketing, advertising cannot itself result in permanent sales increases, but a strong advertising “shock” can lead to a long-lasting change in sales (Simon 1997). Previous research has suggested that advertising “wear-out” is more often a creativity problem than a function of frequency (Belch and Belch 1998) and that “without compelling new copy, approximately one-half of established brand advertising does not produce any incremental sales” (Abraham and <https://assignbuster.com/the-impact-of-advertising-practices-on-sales-marketing-essay/>

Lodish 1990, p. 56). In this regard, the marketing-persistence concept gives us a new perspective from which to look at the issue of long-term advertising effectiveness. The more powerful a “big idea” or a “unique selling proposition” is in an advertisement, the longer the “overnight sensation” it can create, and the more the advertiser can gain from the advertising, at least for some products (Ries and Trout 1993).