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SECTION C: CONCEPTS FOR MARKETING PROGRAMS

C.1 Advertising Budget Formulation

CHARACTERISTICS OF THE ADVERTISING BUDGET DECISION

Setting the advertising budget is a decision area in which there is a disparity between theory and practice. However, a better budget decision will result if the marketing decision maker utilizes both theoretically correct and practically useful approaches.

What Is the Decision to Be Made? Setting the advertising budget is an annual task in most organizations. An advertising budget should normally be one of the outcomes of the **marketing planning process,** created as the costs of planned advertising programs are determined and compared to financial and environmental constraints (see Chapter 4). Budgets should be an outcome or result of the planning process.

In undertaking an advertising budget decision, the marketer should first clearly know what budget is to be set. Some recommended processes for setting advertising budgets presume that the task is to set advertising media budget levels. In practice, the advertising budget usually includes many additional items for which an expenditure level must be set. For example, sales promotion media, sales aids, advertising production, cooperative advertising support and materials, and advertising effectiveness research could all be funded from the advertising budget. Some firms go beyond this, setting the budget on a departmental basis, including such costs as advertising department personnel, association dues, storage of advertising materials, advertising consultants, and office supplies.[1] The budgeting process must give guidance in setting budgets for nonmedia expenditures as well as for media expenditures.

In a multiproduct business, the advertising budget decision is often made product-by-product with the total advertising budget for the business made up of the individual product budgets plus nonproduct and shared advertising costs.

Promotion Budgets versus Advertising Budgets. A promotion budget is the aggregate of the budgets for advertising, personal selling, sales promotion, publicity, and any other separately budgeted promotional elements. Some firms develop the total promotional budget as a "bottoms up" process by separately setting budgets for individual promotional elements and totaling them to form the total promotional budget.

The alternative "tops down" process sets a total amount to be spent for all promotional activities and then allocates the promotional funds among the alternative promotional elements. The **promotional mix** decision allocates the total pomotional budget among advertising, personal selling, sales promotion, publicity and other elements. (see GLOSSARY entry C.29). Historically, most firms have used the bottoms up approach with the budget for each promotional element being separately set. The bottoms up approach flows naturally from the marketing planning process that traditionally generates separate personal selling, advertising, sales promotion, and publicity programs, each of which requires a separate budget.

The advantage of the tops down approach to promotional budgeting is that it assures that the **promotional mix** decision will be explicitly made by considering how funds should be allocated among promotional elements.[2]

[1]For a discussion of items included in typical advertising budgets, see Vincent J. Blasko and Charles H. Patti, "The Advertising Budgeting Practices of Industrial Marketers," *Journal of Marketing* 48 (Fall 1984), pp. 104–10.

[2]For more on the individual budgets versus total promotional budget approaches, see Michael L. Ray, "A De-

Information for the Advertising Budget Decision. Setting the advertising budget is a marketing mix decision. As such, it should be made only after a **situation analysis** (see GLOSSARY entry A.17) has been conducted, the product positioned, and marketing objectives set. The situation analysis should provide information on the size of the market to be reached with advertising, the identity and location of the market, the competitors and their advertising budgets, and a history of the results of past advertising efforts. The **positioning** decision specifies the target market to be addressed and identifies the competition most directly related to the product. (see GLOSSARY entry B.1). Marketing objectives, which address problems and opportunities facing the product, will define tasks that the advertising is expected to accomplish. All of these informational items are necessary and are used in setting the advertising budget.

Application of the Budget-Setting Process. The **advertising budget formulation** process can be used for setting a total promotional budget or for setting the budget for one of the promotional elements such as advertising.

The most obvious application of the process is in setting the budget for advertising (or another promotional element) as part of the marketing planning process. On other occasions, a marketer may be called upon to evaluate the adequacy of an existing advertising budget either by itself or as part of a larger problem situation. In such cases, the steps in the budget setting process can be used to guide the analysis.

THE PROCESS FOR SETTING THE ADVERTISING BUDGET

Leo Bogart, an advertising practitioner and author, states:

> Essentially, setting the advertising budget is not very different from any other business investment decision. The firm looks at the total market for the product field and assesses its potential for growth. It examines its own competitive position, seeking to evaluate realistically the attributes of its product, packaging, pricing, and distribution relative to what other brands have to offer.[3]

Numerous formulas have been suggested for setting advertising budgets, but most of them are unidimensional and simplistic. As Bogart suggests, many factors must be considered in setting an advertising or promotion budget. Commonly cited budget setting formulas are described below, but the budget setting method recommended will draw from several of them.

Heuristic Budget Setting Methods. Several budget setting approaches rely on use of an easily applied rule of thumb. These approaches are widely used in practice, although all of them suffer because, if used alone, they base the budget on a single factor rather than multiple dimensions.

- *Percent of Sales.* One of the most widely used methods is to formulate the budget as a **percentage of sales.** (The percentage is termed the **advertising-to-sales ratio.**) The percentage used may be based on an industry rule of thumb or may simply be the result of past practice. Most often the percentage is applied to the projected sales for the coming year to determine the budget. A **case rate formula** uses a similar approach, setting an advertising rate per unit of sales and multiplying that rate times the projected unit sales to determine the budget. In the brewing industry, for example, a common rule of thumb is that advertising should not exceed $2 per barrel. The percent of sales approach is criticized as relying on the backwards logic that sales generate advertising expenditures rather than the more acceptable idea that advertising creates sales.
- *Competitive Parity.* Another method for setting the advertising budget, termed the **compet-**

cision Sequence Analysis of Developments in Marketing Communications," *Journal of Marketing* 37 (January 1973), pp. 29–38.

[3]Leo Bogart, *Strategy in Advertising,* 2d ed. (Chicago: Crain Books, 1984), p. 51.

itive parity method, is to base it on what competitors spend. If competitive spending rates can be determined, and industry averages are often available, the budget can be set to match competitive levels. Various rules of thumb might be used to generate the advertising budget, such as matching the advertising-to-sales ratio of competitors, matching the dollar weight of the largest competitor, or making the firm's share of product category advertising equivalent to their share of market. This approach is meant to ensure that the firm does not suffer any competitive disadvantage in advertising weight. In addition, if all competitors adhere to this approach, it may reduce the chance of an "advertising war." However, this method suffers from its reliance on a single consideration, competition, and there is no assurance that it does not lead to repeating blindly the mistakes of competitors.

- *Arbitrary and Affordable Budgeting.* Some firms are primarily concerned that the advertising budget be affordable. This leads to a number of rather **arbitrary budgeting** approaches. One approach, for example, is to budget for the coming year the same amount that was spent in the previous year. This might be adjusted for inflation or sales growth. Another approach is to allocate to advertising a proportion of what is projected to be "left over" after all expenses have been paid. And, of course, the budget might simply be arbitrarily set by the CEO. Although affordability is a valid concern, this method ignores market conditions and the role that advertising is expected to play. It seems to treat advertising as an unproductive expense that should be minimized.

Objective and Task Budgeting Method. The **objective and task** approach flows naturally from the **marketing planning process.** Following the **situation analysis,** objectives are set to provide direction to the marketing programs. Some of these objectives are directly applicable to the advertising program and become the advertising tasks. The advertising program then defines how each of these tasks will be accomplished. The budget is derived by determining the costs of each of the task-related programs.

The objective and task method follows what is termed a **zero-base budgeting** approach.[4] The budget is built from the ground up without reference to what was done last year. Each expenditure has to be justified based on the task to be accomplished. The budgeting process is as follows.

- *Define Tasks.* Using the marketing objectives, the tasks that advertising is to carry out are defined. These tasks (in zero-base budgeting they are called decision packages) must be separable projects. For example, developing a trade sales promotion to increase drug store distribution by 20 percent, would be a separable task.
- *Determine Costs.* Programs are next built to fulfill each task and the cost of each program is determined.
- *Rank Programs.* Programs are then ranked in terms of the importance of the objective that the program addresses.
- *Determine Budget.* The budget is determined by summing the costs of the various programs designed to accomplish the assigned tasks. The purpose of ranking the programs is to give guidance in cutting back the budget if, because of other considerations, a lower total budget is required. If the total budget has to be reduced, the least important programs are eliminated.

The task and objective approach offers several advantages. It is consistent with and carries out the direction established by the marketing planning process. Use of the zero-base means that errors are not blindly repeated from year to year. This approach is the only one that recognizes that the advertising budget is not made up of just advertising media, but contains a number of individual tasks, each of which requires a budget decision. The weakness of the approach is that it does not give explicit guidance in deciding what is an appropriate amount to spend in carrying out each task defined for advertising. This decision requires use of

[4]For more information on zero-base budgeting, see Peter A. Phyrr, "Zero-Base Budgeting," *Harvard Business Review* (November–December 1970), pp. 111–21, and James D. Suver and Ray L. Brown, "Where Does Zero-Base Budgeting Work?" *Harvard Business Review* (November–December 1977), pp. 76–84.

judgment, experience, and other budgeting methods.

Budgeting Using Quantitative Models. One of the deficiencies of the budgeting methods presented thus far is that none of them results in an optimum budget and none of them allows the marketer to answer the question, "What would happen if the budget were increased by *X* percent? decreased by *Y* percent?"

To formuate an optimum advertising budget, the response of sales to various levels of advertising must be known. This can be plotted as an advertising response curve, such as the one shown in Figure C.1–1. It is generally considered that advertising is subject to diminishing returns with the result, as shown in Figure C.1–1, that the increase in sales decreases as advertising expenditures are increased. (Some consider that the curve is S-shaped, increasing at an increasing rate until an awareness threshold is reached, then showing diminishing returns.) The optimum budget is the point at which a dollar added to the advertising budget would not increase sales enough to cover the increased cost of the advertising and other product costs. In other words, profits would not increase. Computer models are available or can be constructed that manipulate advertising response, costs, and other variables, providing suggested budgets and allowing the marketer to ask "what if" questions.

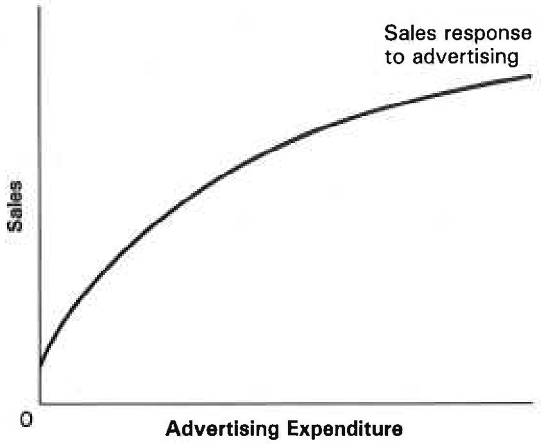

FIGURE C.1–1
Advertising Response to Sales

In practice, the quantitative model approach is much more complicated than the preceding description suggests. The principal complexity involves the data required by the model, particularly the sales response to advertising. Estimates of sales response can be made based on the experience of marketing executives, by regression analysis of historical sales and advertising results, or by market testing of various levels of advertising expenditure. Market testing is expensive, time consuming, and inexact, but is the preferred method nonetheless.

Despite the cost and the data difficulties, it appears that more firms are turning to quantitative budgeting methods. The method applies only to the advertising media expenditure portion of the budget, but this is likely to be the largest advertising expenditure, running into the millions of dollars for some products. While quantitative models can seldom develop a truly optimum budget, it can approach that ideal and allow the marketer to approximate the effect of other budget levels.

New Product Introduction Advertising Budgets. Setting the advertising budget for a **new product introduction** represents a different problem than for established products (see GLOSSARY entry C.18). For a new product, there is no last year's budget, no established advertising-to-sales ratio, and no history from which to extract advertising responsiveness data except through test markets. In addition to this, new products face special consumer, market, and competitive conditions. One result is that new product advertising expenditures, especially as a percent of sales, must be high to establish awareness of the product among consumers and to encourage channel members to stock the product.

With new products, the level of competitive spending plays an important role in determining the advertising budget. Although a new product will initially have very low

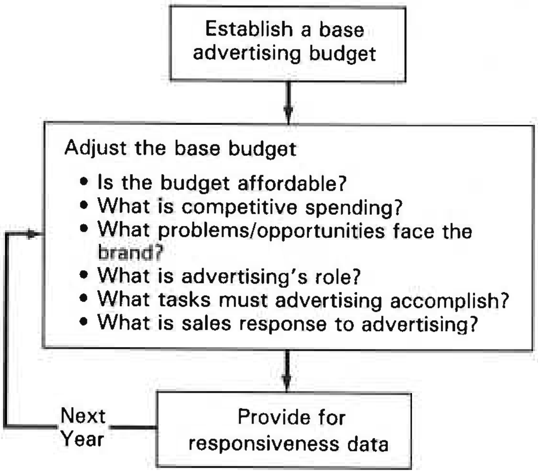

FIGURE C.1-2

Process for Advertising Budget Formulation

jected sales could be used, but the objective and task approach would be better because it makes it possible to establish multiple budgets directed to specific tasks assigned to the advertising.

- *Step 2: Adjust the Base Budget.* The other considerations affecting the budget, some of which were discussed above, should be listed. Data indicating their budget impact (much of which should be available from the **situation analysis**), should be gathered. Then, one consideration at a time, the budget should be adjusted up or down to reflect the influence of that variable. If, for example, the advertising spending of the major competitor had increased by 20 percent in the current year, this would be a factor arguing for an increase in budget. The adjustments should be only in those budget elements affected.
- *Step 3: Provide for Responsiveness Data.* If data on the responsiveness of sales to advertising expenditures are available, they should be used in step 2 to adjust the budget toward an optimum level. If such information is not available, provision should be made as part of the budgeting process for collecting such information. This may call for market testing of different levels of advertising expenditure. The cost of the testing and data-gathering effort should be included as one of the subbudgets or decision packages in the base budget. In the following year when sales responsiveness results become available, they should be used as an adjustment consideration in step 2 of the budgeting process.

SUGGESTIONS FOR FURTHER READING

BLASKO, VINCENT J., and CHARLES H. PATTI. "The Advertising Budgeting Practices of Industrial Marketers." *Journal of Marketing* 48 (Fall 1984), pp. 104–10.

BOGART, LEO. *Strategy in Advertising,* 2d ed. Chicago: Crain Books, 1984, pp. 37–61.

DHALLA, NARIMAN K. "How to Set Advertising Budgets." *Journal of Advertising Research* 17 (October 1977) pp. 11–17.

C.2 Advertising Copy

CREATION OF ADVERTISING MESSAGES

Advertising copy decisions determine the message that advertising will present to the target audience and how it will be presented. Advertising copy decisions are part of the promotion program. Two other interrelated advertising decisions, **advertising budget formulation** (GLOSSARY entry C.1) and **advertising media selection** (GLOSSARY entry C.4), are usually made simultaneously with creaion of advertising copy.

Sources of Direction for Advertising Copy Decisions. Advertising copy decisions are made as part of developing the **marketing mix.** In the **marketing planning process,** advertising copy decisions are made after the **situation analysis** has been conducted and the product's **positioning** determined. Both are important sources of direction and information for advertising copy.

Primary direction for advertising copy comes from the product's positioning (see GLOSSARY entry B.1). The positioning deci-