Cahners Advertising Research Report

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Media Advertising When Your Market Is In A Recession

by
Dr. Valerie Kijewski
Strategic Planning Institute
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THE STRATEGIC PLANNING INSTITUTE

THE PIMS PROGRAM

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PIMS—THE MAJOR PROGRAM OF SPI

The Strategic Planning Institute (SPI) of Cambridge, Mass., is a non-profit membership organization dedicated to the advancement of strategic business management. SPI manages the PIMS (Profit Impact of Marketing Strategies) data base which consists of over 200 corporate members. These firms provide specific information on their individual businesses, now totaling nearly 2000. A majority of these businesses produce industrial products or services.

By analyzing these business experiences, the PIMS staff discovers the general "laws" that determine what marketing strategies, in what kind of competitive environment, produce what profit results.

PIMS began as an internal project of the General Electric Company to assist corporate and division level planning. From 1972 to 1974, the PIMS program was established as a development project at the Harvard Business School, and then eventually organized as an autonomous institute, SPI.

In 1980, SPI completed a major research project with Cahners Publishing Company evaluating the relationship between brand awareness/preference, market share and profitability, and the impact advertising has on this relationship. This report, "Brand Awareness as a Tool for Profitability," provided an analysis of advertising accountability for industrial businesses. For more information on this material, telephone SPI (617) 491-9200, or Cahners Publishing Company (708) 635-8800.

TECHNICAL NOTES

The sample for this research was selected from the PIMS data base which contains the actual experiences of over 1,000 industrial businesses. These include businesses described as: Capital Goods Manufacturing, Raw or Semi-Finished Materials Manufacturing, Components for Finished Products Manufacturing, Supplies or Consumable Products Manufacturing. The annual data describing each business covers a minimum of four years to a maximum of 10 years (from 1970 to 1981). The sample included only businesses with non-zero media advertising expenditures, over 500 businesses in all. Through the technique of "pooling," the sample was expanded to slightly more than 1,000 total experiences.

Definitions of Market Conditions

Recession Stage in Served Market: Short-term Growth Minus Long-term Growth ≤ -4

Expansion Stage in Served Market: Short-term Growth Minus Long-term Growth $\geq +4$

MEDIA ADVERTISING WHEN YOUR MARKET IS IN A RECESSION

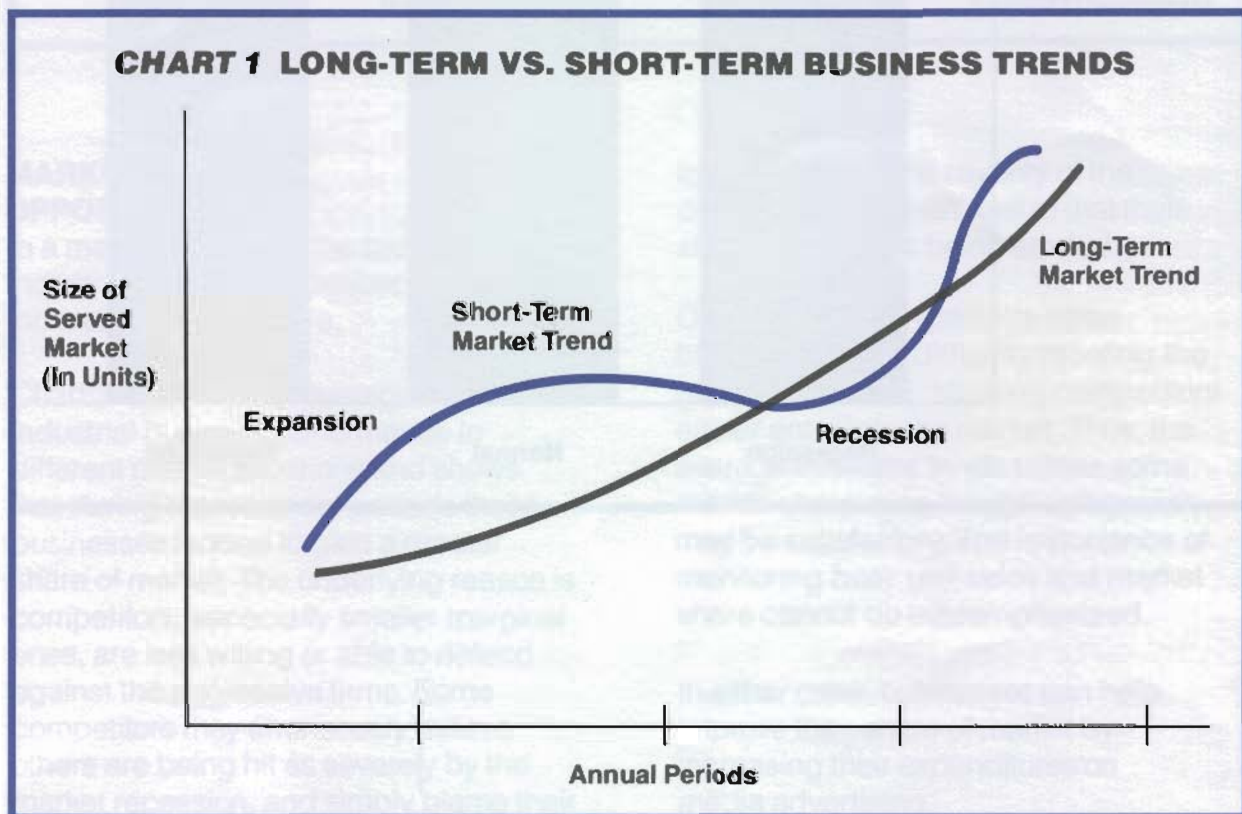
by Dr. Valerie Kijewski

We commonly think of recession in a national framework, the U.S. economy is either doing well or it is not. Yet some businesses are counter-cyclical and thus defy general recession periods.

To better understand periodic business behavior, an alternative definition of recession is needed which is not dependent on national economic behavior. If we establish that every business serves a particular market, then we can define "recession" as being a condition in which the market you serve, at one point in time, is growing at a rate substantially slower than the market's long-term trend.

Chart 1 illustrates this concept. The black time-series line is the long-term market trend based on a four year average. The blue line represents the short-term (one year) recession and expansion stages.

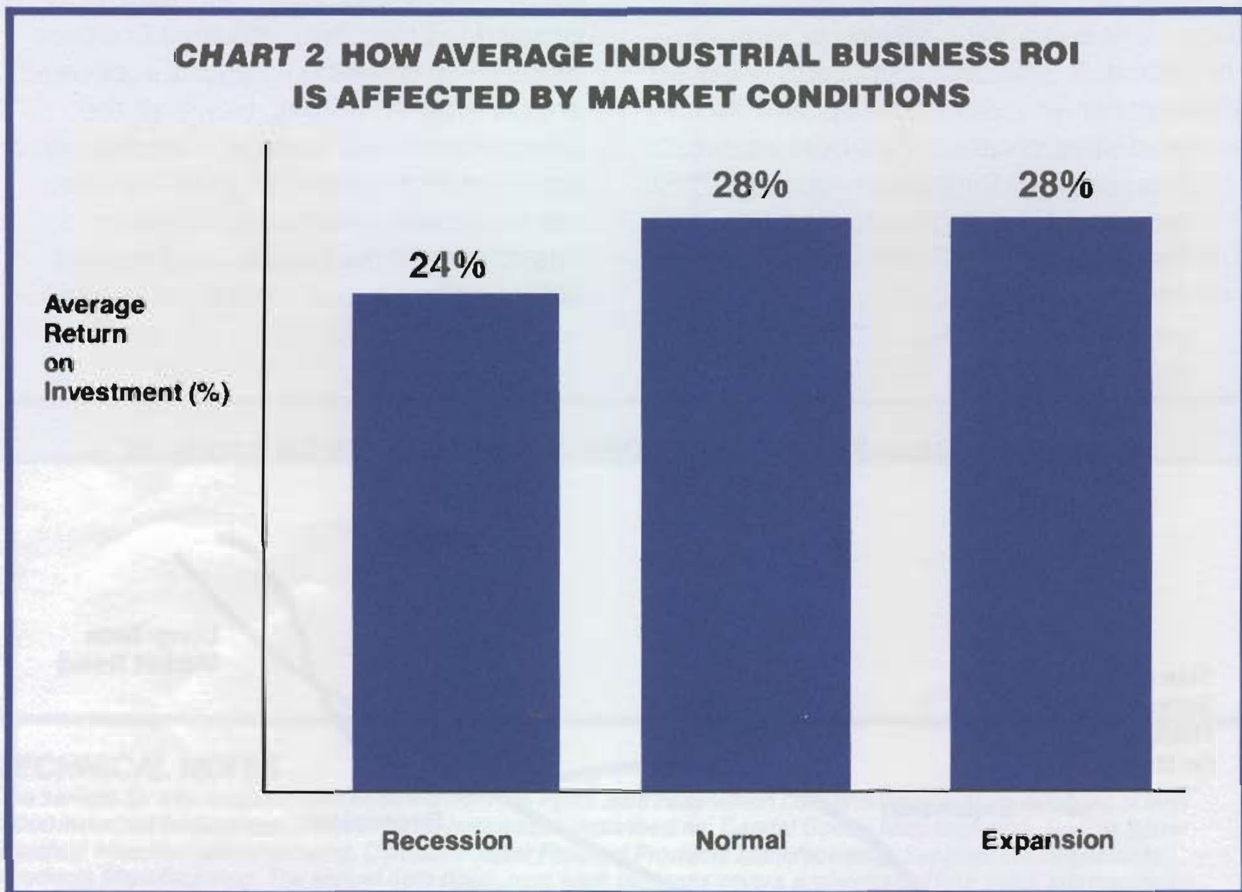
We can now compare these two trend lines. When the short-term growth exceeds the long-term growth by 4 percentage points, we consider the market to be in an expansion period. When short-term growth lags long-term growth 4 points or more, it is a recession. Periods in between are considered normal. However, the determination of the stage in the business cycle is entirely dependent on served market growth and has no direct relationship to the national economy or other traditional measures of recession.

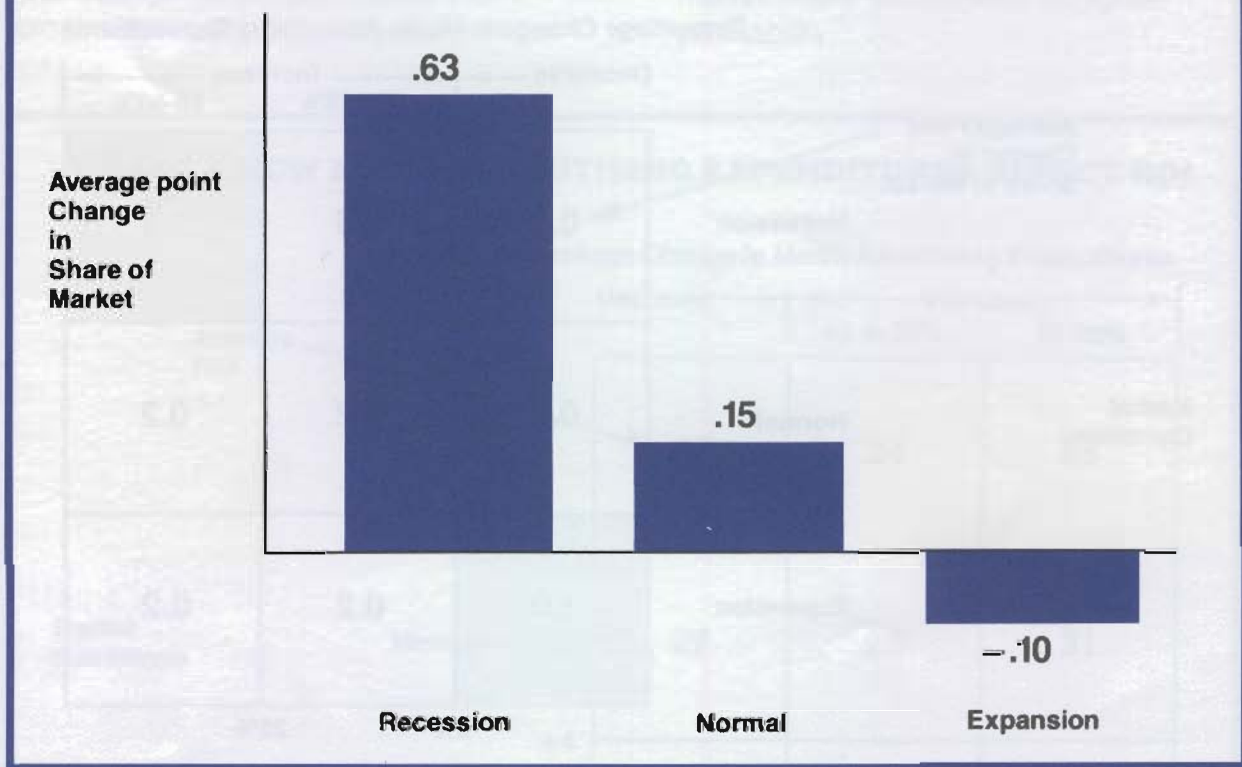


IMPACT ON PROFITABILITY

Utilizing the PIMS data base, we can examine the impact of served market expansion or recession periods on the pre-tax, pre-interest return on investment of over 1,000 industrial business experiences which constituted the sample for this report.

Chart 2 shows the impact on ROI during different stages of the business cycle. During a recessionary period, average businesses do experience a slightly lower rate of return relative to normal times. However, expansion times do not generate a higher level of profits than normal periods as might be expected. The explanation of this phenomenon involves an analysis of market share changes, which follows.





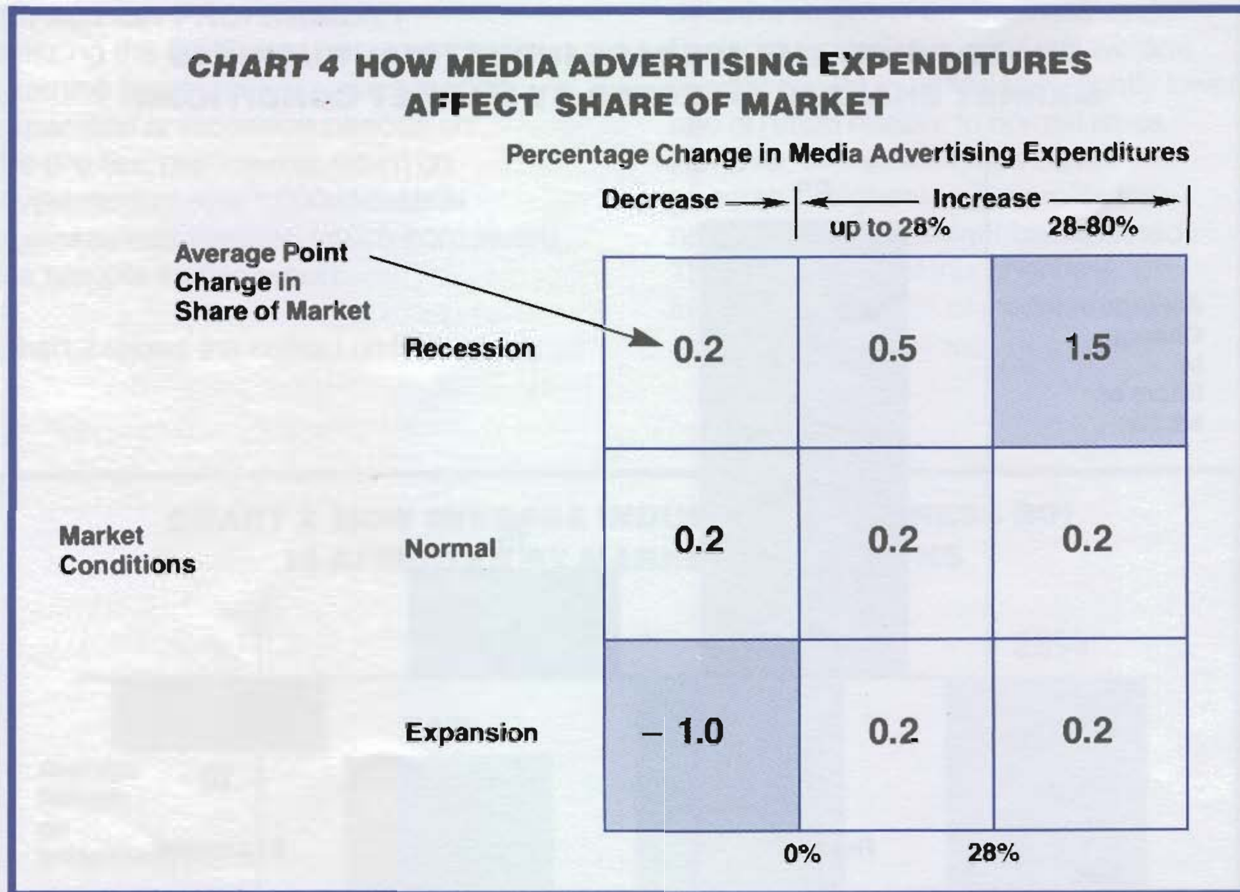
MARKET SHARE OPPORTUNITIES

In a market downturn, the average industrial business experiences increased market share.

Chart 3 illustrates the average PIMS industrial business performance in different market situations and shows that during recessionary periods these businesses tended to gain a greater share of market. The underlying reason is competitors, especially smaller marginal ones, are less willing or able to defend against the aggressive firms. Some competitors may erroneously believe others are being hit as severely by the market recession, and simply blame their loss of sales on the severity of the downturn rather than realize that their share of market is being eroded.

During expansion periods some businesses have difficulty meeting the growing demand, allowing competitors easier entry into the market. Thus, the average business tends to lose some market share even though unit growth may be satisfactory. The importance of monitoring *both* unit sales and market share cannot be overemphasized.

In either case, businesses can help improve their share of market by increasing their expenditures on media advertising.



MEDIA ADVERTISING IMPROVES MARKET SHARE

Chart 4 shows that businesses making major increases in media advertising expenditures during the recessionary period gained an average of 1.5 points of market share. This level of aggressiveness was displayed by only 25% of the businesses. Thus, by being aggressive, these businesses outperformed the average business which, as we saw earlier, gained only 0.63 points of share during market recession.

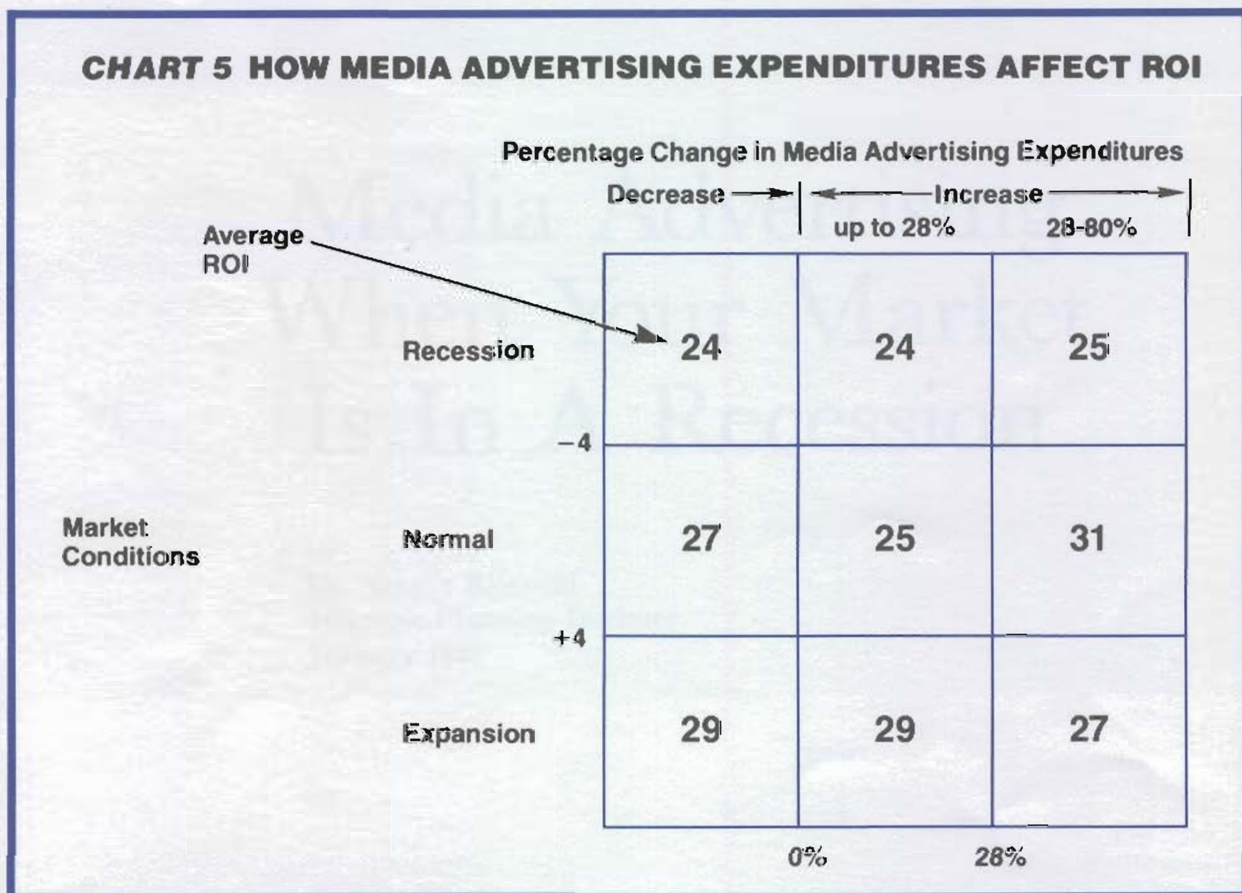
During market expansion periods, over 80% of the businesses increased media advertising expenditures. The problem, however, is that no particular share gain was achieved, on average, because most firms take the same action. Thus, the consistency of ROI levels between normal and expansion periods is maintained.

We do see the danger of falling behind in media advertising. Those businesses that reduced their media advertising during the expansion lost one point of share. We cannot say, without additional information, whether the pulling back of media advertising caused a loss of share or whether it was caused by the lack of production capacity to serve the growing market. However, any program of increased media advertising should be a part of your marketing *and* business strategies.

ROI NOT AFFECTED

What price, in terms of ROI, was paid for being aggressive with media advertising? There was no statistically significant difference in the level of profitability for aggressive media spenders. Chart No. 5 indicates ROI remains consistent regardless of media advertising expenditures even when media expenditures are substantially increased! For this analysis ROI is measured in the same period as the increase in expenditures.

However, over the long term increased market share should lead to higher profitability.[1]



CONCLUSION

A recessionary market condition can provide an opportunity for an industrial business to break from traditional budget-cutting patterns, and build a greater share of market through aggressive media advertising.

In fact, the study indicated that businesses which are aggressive media spenders can increase their share of market more than the average business during market downturns. Correspondingly, businesses that reduce media expenditures in expansion times suffer loss of market share. It was demonstrated that aggressive businesses may be able to accomplish these gains through greater expenditures without reducing short-term profitability.

1. See "Market Share—A Key to Profitability," by Robert D. Buzzell, et al. (Harvard Business Review, Jan.-Feb., 1975)

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