THE UPDATED AND REVISED 2ND EDITION OF
MARKETING DUE DILIGENCE

MARKETING AND FINANCE

CREATING SHAREHOLDER VALUE

MALCOLM **McDONALD** • BRIAN D. **SMITH** • KEITH **WARD**

CIMA
Chartered Institute of Management Accountants

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Contents

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Malcolm McDonald
Brian D. Smith
Keith Ward

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With thanks to all my friends and colleagues at Cranfield

— Malcolm

For Lindsay, Eleanor, Catherine and Rosalind

— Brian

For Angela, Sam and Rob

— Keith

Foreword

by Anne Godfrey, Chief Executive, CIM

'Marketers in the boardroom' has long been a call from those who see marketing as a strategic process rather than the tactical one that is often its fate. However, one glance at the boards of the FTSE 100 and it is clear that we are still some way from that being 'the norm'.

That said, I would be surprised if market*ing* wasn't in the board room, just in another guise. Many of the topics that marketers discuss are so important to an organization that it is hard to see boards not having them on their agenda. Worryingly however many of these processes are given to other areas of the business to manage. So, why is that?

Our experience has shown that there is a combination of forces that lead to professional marketers finding themselves out in the cold at Board level. The first is a fundamental misunderstanding of what marketing is, and the value it can bring to a company, by those in leadership positions. Communications and advertising is the first thing people associate with the 'm' word but those in the know understand that this is only part of what a professional marketer has to oversee; it's the visible tip of the marketing iceberg.

The second force is marketers themselves who are sometimes guilty of exacerbating this narrow view of our profession by focusing on the areas that people enjoy and shying away from the business language that their CEOs expect to hear. A sprinkling of buzz words and leaning on the intangible will quickly lead to business leaders confirming their thoughts on a profession they don’t fully understand.

So, should marketers have a strategic voice in an organization? Absolutely. Do they deserve this as a right? Not necessarily.

Marketers are in the unique position of being able to understand customers and translate that back into the business to influence how it operates and the products and services it develops. This ability to read customer sentiment is even more vital in an age where technology has made brands more accountable for their actions; an environment where mistakes are jumped upon and success creates a buzz, both of which can go viral at the touch of a button.

It is perhaps because of this that we have found Chief Marketing Officers increasingly welcomed at the top table to provide customer insight, with organizations fast realising that their customers are a vital part of their business; something we’ve all known for a long time. However, marketers must ensure that when they get their leader’s attention that they focus on talking the language of business rather than succumb to marketing jargon.

To say that marketers can’t speak the language of business is of course a sweeping generalisation. There are fantastic examples of leading marketers that have transformed organizations and driven up their profits; however they are often the exception rather than the rule.

We also have to ensure that this level of business acumen is present throughout the profession at every level. That’s why we view standards and related competencies as a key component of a professional marketer’s development.

This book outlines a pathway for marketers who want to ensure that their business plans not only take into consideration the intangible, such as brand, but also the tangible elements upon which boards and investors base their investment decisions.

I would urge marketers to read the pages that follow, take the lessons presented and ensure that marketing within your organization gets back to where it belongs, at the strategic hub of its operation.

Foreword

by Charles Tilley, Chief Executive, CIMA

A century ago John Wanamaker, considered by many, the father of traditional marketing said ‘half the money I spend on marketing is wasted; the trouble is I don’t know which half’.

Whilst there is more clarity on the costs of marketing, there is little understanding about the true value of marketing strategies, and other intangibles.

With intangible assets such as brand and reputation now constituting 80% and more of the market value of an organization, it is essential that that these too are measured and managed.

To achieve this finance and marketing must work together, right from the start, when marketing strategies and plans are being developed. They must understand how that strategy will create and preserve value in the short, medium and long term.

But the relationship between marketing and finance has not always been a smooth one. A previous research project, *Return on Ideas*, done in conjunction with the Chartered Institute of Marketing and the Direct Marketing Association in 2009, highlighted that finance and marketing often ask different questions and they answer them in different business languages. This must be overcome. The most successful businesses are those that are integrated.

Management accountants provide information and analysis – both financial and non financial – to support sustainable decision-making. They are therefore in an ideal position to partner with their marketing colleagues and apply rigour to the analysis of costs, risks and value from marketing strategies.

It is this blend of finance and marketing thinking that will ensure that marketing initiatives deliver sustainable value to the business.

This book outlines a useful framework that finance and marketing colleagues can use to encourage constructive dialogue and to put marketing plans through a ‘due diligence’ exercise. I urge both finance and marketing professions to read it.

Now, more than ever, executives must account for every penny spent. There needs to be a clear understanding of the value created – both tangible and intangible. With effective collaboration between marketers and management accountants this can be achieved.

Foreword from the First Edition by Sir Michael Perry, GBE

A few years back I was asked to address an Economist conference for senior marketing people on the questions – 'Why do so few CEOs of major UK companies come from a marketing background? Do marketing people make bad CEOs?'

To start with I was puzzled by the questions. I had spent thirty nine years working in a company, Unilever, where marketing was virtually the default background for the CEOs of successful operating companies. Every such subsidiary had a Marketing Director on its board as well, whose voice carried more weight than anyone's when it came to business strategy. Even at parent company level, of the ten Executive Chairmen of Unilever plc since the company was formed in 1929, four were marketing men – more than from any other discipline.

A little research soon revealed that this pattern did not by any means hold true for most FTSE 100 companies. Worse still, too many of them did not even have a marketing person on their executive boards. That really got me worrying. In such companies who represents the interests of customers? Where is the analysis of markets and market segmentation done? What about the detailed understanding of competitors and sustaining competitive advantage? Where does the prime responsibility lie for optimizing crucially important shareholder values such as intangible assets – like brands, or good-will? No wonder so many companies run into difficulties.

In the absence of a Marketing Director, it has to be the CEO himself who shoulders this prime responsibility, and since he or she typically comes from a financial, or perhaps a technical or operations background, he needs all the help he can get from his marketing specialists if he is to deliver sustained success. That's where the experience so skilfully displayed in this book comes in. It is precisely aimed at Chief Executives from non-marketing backgrounds, and it sets out simply and with great clarity what their marketing departments should be capable of delivering for them.

CEOs who have spent their entire earlier career in marketing would also do well to peruse these pages carefully. Shibboleths abound in the marketing trade, and most of us have been guilty at one time or another of keeping alive the myth that much of what we do is neither quantifiable nor expressible in the demanding terms of measured change in shareholder value. Scholarly attempts have been made in the past to find language and techniques for marketing metrics, most of which have helped improve marketing's accountability to some degree. But this book goes a step further, by insisting that the ultimate test of measurable impact on shareholder value is as relevant for marketing investment, in the widest sense, as for any other deployment of shareholders' funds.

All of this begs the questions I posed at the outset, of why there are so few marketing people on the boards of major UK companies. At the heart of the matter, sad to relate, is the fact that many companies either do not put the constant search for long-term competitive advantage at the centre of their thinking, or if they do, they do not believe their marketing departments have much to contribute. For many business leaders today, marketing is synonymous with advertising and sales promotion, and marketing people are caricatured as the flamboyant and not very numerate folk down the corridor who love to remind them, on impeccable historical authority, that half the money they spend is undoubtedly wasted. Not a very promising basis for a relationship grounded in mutual respect and trust.

The third group, therefore, who should take this book very seriously indeed are those Marketing Officers who understand the strategic elements of their role, and who need to break down the barriers that prevent their voices from being heard clearly enough in the boardroom. Marketing people typically do not speak the language of finance and investment, and this book makes a major contribution to the bridging of a gap that has become a major source of business under-performance in the increasingly competitive and globalized world in which we operate.

My advice to Chief Marketing Officers is very simple. You should be responsible for generating the value propositions that achieve sustained customer preference for your company's products or services. If your CEO does not recognize that, it is up to you to persuade him otherwise, or move somewhere else, where your proper role is fully understood.

The authors of this book rightly refer to the prime importance of measuring shareholder value creation. In recent times the concept of shareholder value has come to mean different things to different people and in different circumstances. The prime responsibility of boards is to secure and safeguard the longer-term prosperity of their business, for the benefit of its owners and its other stakeholders, most especially its customers and employees. Shareholders often see things differently. Owners of public companies, notably institutional investors, have less interest in the longer term than they publicly profess, or indeed demonstrate by their day-to-day trading behaviour on the world's exchanges. They also accept less of the responsibilities normally demanded by society in return for the benefits of legal ownership. Boards of public companies are therefore always obliged to bear the short-term needs of markets in mind, as they focus strategic thought on their wider responsibility of building longer term prosperity.

Marketing specialists are subject to the same pressures, and all too often they yield to the demand to sacrifice the long term interests of building brand equity, or other intangible asset values, to short term expedience. Careful examination of the contents of this book will remind them of the consequences of so doing. If they and their Chief Executive Officers are equally well informed, perhaps fewer businesses will be crippled by the inevitable results of the short-termism that we all profess to deplore.

A note for busy people: How to get the best out of this book

This book is written for directors and managers of firms operating in the real world. By definition, such readers will be busy people and may not have the luxury to read this book from start to finish before returning to review parts of the book that are especially relevant to their situation.

In recognition of this, we offer some suggestions as to how to gain an overview of the book and the subject of Marketing Due Diligence before attempting to understand and apply it in detail.

Each chapter begins with a short ‘fast track’ section which summarizes briefly its contents. These provide a succinct way to acquaint oneself with the content of each chapter before reading and when returning to it.

In addition, these ‘fast track’ sections are consolidated, with a little editing, into Chapter 10. This chapter therefore provides a good overview of the book and can be read before and/or after reading Chapters 1–9, depending on your learning style.

The main body of the book is split into three parts:

Part 1: What is Marketing Due Diligence?

This is intended for those who need an explanation of why this new process is needed, what it involves and what its implications are.

Part 2: The Marketing Due Diligence Diagnostic Process

This is intended for those who wish to assess the shareholder value creation of their marketing strategy.

Part 3: The Marketing Due Diligence Therapeutic Process

This is intended for those who wish to improve the shareholder value creation of their marketing strategy by acting on the outcomes of the diagnostic process.

By means of this structure, it is hoped readers will be able to understand the concept and process of Marketing Due Diligence as quickly as possible. Be warned, however, that Marketing Due Diligence is intended as a route to creating sustainable competitive advantage. Our readers will appreciate that it is naive to expect that outcome to be either quick or easy.

List of figures

List of tables

Part 1

What is Marketing Due Diligence?

Chapter 1

The Lessons of Experience

'Diligence is the mother of good fortune'

—Benjamin Disraeli

Fast track

Almost all businesses prepare a business plan and have it reviewed by senior executives. Whatever the business, the plan consists of a request for resources, some description of how they will be used and a promised outcome. Despite the large amount of effort put into preparing, reviewing and revising these plans, they often fail and, in doing so, they destroy shareholder value and waste precious resources. It is dangerous to draw simple conclusions from stories of business success and failure, but the rigorous study of enough cases reveals some useful general patterns. We can see common factors that lie behind success, such as making sure the market is really there and ensuring that the business has and uses a distinctive strength. Similarly, we can see patterns in business failures, such as the failure to identify the target customer correctly or to anticipate where the market is headed. Identifying these common factors is important because traditional metrics of firm performance and marketing accountability can be manipulated easily and, in most cases, look backwards rather than forwards. This chapter introduces a new way at looking at a business strategy and connecting it to firm performance. This approach, known as Marketing Due Diligence, is based on the fundamental factors that underlie almost all successful business strategies.

Introduction

There are few things in business life that are more universal or more ubiquitous than the business plan. From the entrepreneur trying to convince his backers, to the CEO of a multinational trying to assuage a room full of demanding investment analysts, the business plan occupies much of the attention of business leaders, their subordinates and those who invest in the enterprise. A strong business plan may not guarantee commercial success, but a weak one almost certainly guarantees failure, so the ability to craft a strong plan and to differentiate between weak and strong plans is, arguably, one of the core capabilities of any business executive. **This book is written for those people – owners, executives, investors – whose career and livelihood depends upon their business planning competence.** It does not, however, prescribe methodologies for preparing a plan; there are already many good books that do that. Instead, this book addresses a much more neglected question: How do we know if the business plan is likely to succeed? We think this question is important to every executive but, when we conceived the book, we did have two particular audiences and one particular context in mind; senior finance executives, senior marketers and the interface between them. For both, assessing and insuring the success of a business plan is an essential part of their job but, in our experience, the two professions look at this problem from very different perspectives, often leading to conflict where cooperation is, in fact, most needed. We've therefore written this book with the aim of encouraging a shared perspective between senior finance and marketing colleagues, one that combines the distinct value each brings to commercial management, with the intention that cooperation at the marketing/finance interface will lead to stronger business plans and better commercial outcomes.

Business plans appear to vary greatly between different types of company, but when one dissects them, they are in fact remarkably similar in their fundamentals. Whatever the nature of the enterprise, most business plans are, in essence, a request, a description and a promise. They request the allocation of some resources, describe how those resources will be used and promise to deliver an objective. Whether the plan is a two-pager for a small business or a 15Mb PowerPoint deck for a strategic business unit of a global multinational, it almost always boils down to that fundamental structure of a request, a description and a promise. This is no coincidence. It is an obvious and direct corollary of the simple reality that almost all businesses require investment in order to achieve their goals and almost all investors want to know how their money is going to be spent.

With well over a century of executive experience and academic research behind us, the three authors of this book have been involved in more business plans than we like to be reminded of. We’ve prepared them, presented them, analysed them and followed up on their outcomes. We have written them ourselves and been through the plan presentation and approval ritual many times; and we’ve coached hundreds, perhaps thousands, of executives through the process in industries ranging from consumer goods to pharmaceuticals and from high technology to incontinence products. By and large, we find the business plan review process, as it is practised in most companies, to be ineffective or at least inefficient. It is supposed to produce agreement on a plan that has a high probability of delivering its promises. In practice, it often does the opposite. Executives, operating in a highly uncertain environment, write plans that they think will work but in which the risks are poorly understood. They anticipate the challenges of their leaders and build in spare resources and soft targets. Their leaders, without their subordinates’ knowledge of the market environment but with long experience of how executives behave, counter these tactics by instinctively demanding better outcomes and less expenditure, whatever the initial proposal. Overall, the