L.E.K.

EXECUTIVE INSIGHTS

VOLUME XVI ISSUE 29

Passenger Transport Companies: How to Boost Profits When Revenue Falls – Invest in Marketing

Passenger transport companies (PTCs) spend millions on marketing. Every day we're surrounded by evidence of their activity: generic and route- or destination-specific adverts for airlines, train services, ferry operators and coach lines can be seen on national television, on billboards and poster sites, and in national newspapers and consumer titles.

And being the 21st century, those adverts are also visible online, appearing on dedicated travel portals or a wide array of B2C and B2B websites, social media platforms and search engines. Adverts are supported by on- and off-line promotions with media and tourism partners.

The name of the marketing game is obvious: to attract new customers to use a PTC's travel services, either to grow the overall travel market or to improve an operator's market share, to motivate occasional customers towards more frequent use, and to cement the loyalty of high frequency or high value customers.

> ***Marketing spend is a highly controllable item of expenditure. As such, it is often an early victim of cost-cutting in tough economic times.***

The strategic purpose of marketing is also clear: to generate revenue. As PTCs invariably have high fixed operating costs, any revenue increase makes itself felt straight on the bottom line.

Proving the Case for Marketing

In good times, when PTC customer numbers are steady or rising, marketing budgets are usually secure and funding for advertising campaigns and promotional activities, whether digital, broadcast or print can continue. But in tougher economic times, as have been experienced over the past few years, marketing expenditure has often been an early victim of the cost-cutting guillotine because it is a highly controllable item of expenditure.

Henry Ford, founder of the eponymous motor company, once said: "A man who stops advertising to save money is like a man who stops a clock to save time." Mr. Ford may be right, but time and time again marketing budgets are axed because marketers struggle to demonstrate the effectiveness and business value of the investment. If they can't make a convincing case for maintaining or increasing marketing spend, they have little chance of persuading financial controllers to leave their budget alone.

Are the money men right to target marketing budgets when the going gets tough? Not necessarily. There is evidence that cutting marketing spend may be absolutely the wrong thing to do when a PTC is fighting for business.

Unsurprisingly, the marketing industry has long proclaimed that companies maintaining or increasing their marketing spend

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during tough times tend to be better positioned, even stronger, when economies pick up. L.E.K.'s analysis suggests this is a valid point of view and project experience has shown that some PTCs under-invested in marketing during the recent hard years and so lost the opportunity to generate additional revenue. In a recent case, L.E.K. was able to demonstrate that companies that cut marketing significantly saw a related fall in revenue, while others who invested in marketing achieved a marketing expenditure ROI of more than 500%.

Being Smarter

By applying robust analytical techniques, L.E.K. has proved the relationship between marketing expenditure and rates of return, addressing fundamental questions such as: What did marketing deliver in terms of customer volumes? What positive effect did marketing have on business revenue? Where was this greatest?

These are seemingly simple questions, but they are difficult to answer accurately. If the challenge for PTC marketers is measuring the impact and ROI of marketing expenditure with more precision, why has it been so hard to do so?

Quantifying marketing ROI is not straightforward, nor is it necessarily independent or unbiased, with marketers accused of bending the truth to show their campaigns in a better light. It can be hard to identify, let alone analyze, suitable campaigns that might help benchmark marketing ROI. Indeed, assessments of apparently similar campaigns might generate wildly differing returns, further clouding meaningful measurement and interpretation.

In our experience, this difficulty in accurately evaluating the business return of marketing stems from an inability to separate non-marketing growth drivers – such as economic conditions, employment and pay, inflation, and service performance – from marketing-derived drivers.

The problem is that analysts tend to use common simple measurement techniques for assessing marketing ROI, and these tend to comprise both marketing and non-marketing drivers. If the non-marketing factors are not separated out, they can dominate the data, skew the result, and misinform the analysis. A further problem may arise where the analysis tries to be too specific. Attempting to identify and measure the returns from individual campaigns runs the risk of confusing the results where these are not independent of the influences of other activities. A holistic approach can be more effective when assessing the overall returns achieved by the marketing budget as a whole.

L.E.K. has developed a method of filtering out the non-marketing factors, deploying a high degree of analytical rigor in the ROI calculation to show a clear relationship between marketing expenditure and revenue generation. Amongst the

Project Example 1: Assessing the Revenue Impact of National Television Advertising

L.E.K. worked with a UK PTC engaged in travel ticket sales across multiple travel providers. The project assessed the revenue impact of national television advertising, examining the direct ROI for the client, and the impact of its advertising on PTCs in the wider sector. Reliable benchmarks were very hard to find, but the analysis showed the client was getting a modest return of about 100%, considerably below the industry average of around 500%. But by raising awareness of the overall travel proposition, the campaign delivered big benefits to the travel sector as a whole. L.E.K. found that £1 of marketing spend was generating about £12 of incremental journeys – an ROI of 1,100%. The question arose: with such a big potential prize from raising awareness and consideration of the travel options, why not initiate more cross industry marketing programmes?

cacophony of events and influences, it identifies the small but significant signals that provide true insight into marketing spend effectiveness.

This approach involves looking at period-on-period changes in revenue generation and marketing spend, typically by week or month, and adjusts for seasonal factors that might skew the results. Industry growth attributable to non-marketing factors is also considered and assessed, together with the impact of other structural one-off effects, such as the impact of calendar changes in year-on-year holiday periods such as Easter.

Figure 1 gives an example of our approach to understanding the factors affecting period-on-period changes in revenue and their relative impact. The process started by considering the whole business, then progressed to focus on more specific sub-elements such as individual markets or sales channels. In each case a number of factors were explored in the search for statistically robust performance indicators, where each factor was a necessary and significant element of the final answer. Factors passing these robustness tests were retained (the green check marks), and the others dropped (those check marks shown in grey).

Too Little or Too Much?

L.E.K.'s methodology helps to generate business-beneficial insights by addressing fundamental marketing questions including: Where is too little too little and where is too much too much? Is marketing paying off? How much is it paying off? How long should I keep paying? The approach determines the optimum point for marketing expenditure by analyzing a range of comprehensive data inputs, such as:

- Passenger revenues segmented by customer type or journey purpose and by sales channel
- Marketing expenditure, segmented in a variety of ways:
  - Type of marketing activity
  - Other third party marketing activity which might either help or hinder performance, for example by industry partners or competitors

Ideally, there should be five years' worth of history, split by month

Figure 1

Variables Tested and Included in Marketing ROI Calculation (Example)

Dependent revenue variables		Independent variables									
		PTC marketing			Competitor/ other marketing		Temporal			Inflation	
		Advertizing spend	Lagged advertizing spend	Cumulative advertizing spend	Advertizing spend	Lagged advertizing spend	Seasonality	Days per period or other one-off impacts	Time trend growth	GDP	Inflation
Increasing specificity of marketing effects	Total company (or industry)	✔	✓	✓	✓	✓	✔	✔	✔	✓	✓
	Individual markets or routes	✔	✓				✔	✔	✔		
	Sales channels	✔	✓	✓			✔	✔	✔	✓	

Key: ✔ Included ✓ Excluded. Variables were excluded due to a lack of statistical significance and/or limitations associated with the scope of data.

Source: L.E.K. Consulting analysis

or four week period, so that the data can be sliced, diced and interpreted, and then used to generate marketing ROI evidence that is both unimpeachable and simple to understand.

Project examples illustrate how this new approach to analyzing marketing ROI for PTC clients helped irrevocably demonstrate the impact of marketing. In both cases, analyses showed that revenue was clearly linked to marketing spend and that cut-backs had an adverse effect, with revenue either remaining flat or falling. As a result, these insights informed decisions to

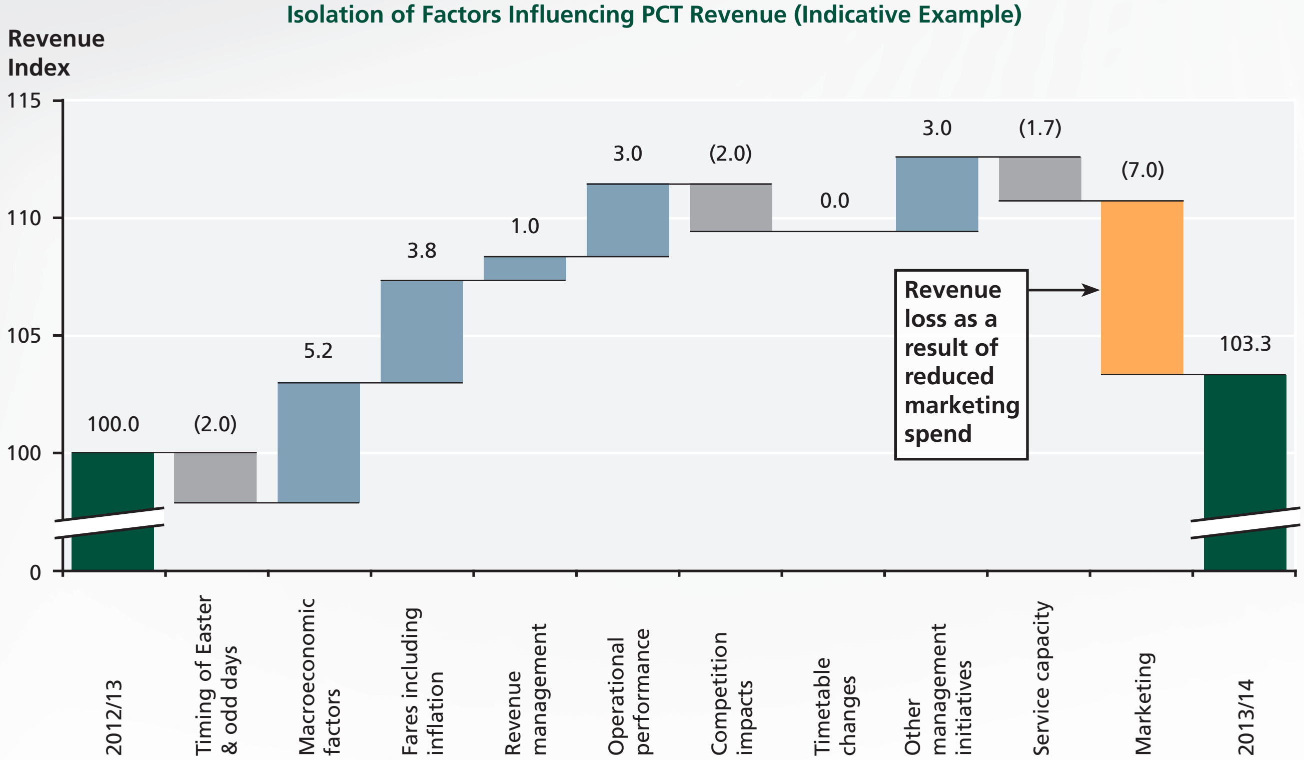
Project Example 2: Identifying the Root Cause of Revenue Decline

L.E.K. was engaged by a UK PTC to investigate why its revenues had unexpectedly declined. Company managers advanced various hypotheses for this fall, believing that it was due to operational issues (service disruption, crowding, etc) but did not consider the role and effect of marketing. L.E.K.'s investigation found that the company had cut its marketing expenditure and activity at the wrong time. Historical ROI methods had initially showed marketing was not delivering a sufficient return – but L.E.K. established that this conclusion was not accurate and cutting marketing budgets was the core reason for the under-performance – despite this not even being considered a possibility by the client at the start of the project. Figure 2 shows how individual revenue drivers were isolated to reveal the true impact of marketing.

Faced with this insight, L.E.K.'s recommendations to the client were clear: reinstate marketing and spend more, not less.

Figure 2

Isolation of Factors Influencing PCT Revenue (Indicative Example)



Source: L.E.K. Consulting analysis

maintain or increase marketing spend to stimulate more ticket purchases and therefore revenue.

What distinguishes L.E.K.'s approach is its heritage as a strategy consulting firm, with extensive expertise in revenue forecasting and analysis, and in employing sophisticated statistical techniques to ensure the results delivered are robust and true. This means that L.E.K. can be both highly effective and credible in isolating pure marketing impact. Typically, the regression results we have achieved explain 98% of period-on-period changes in revenue.

Proof of the Pudding

We believe that this approach generates more valuable insights than many commonly-used analytical methodologies, insights that can help sow confidence amongst PTC executives. Armed with this confidence, business managers and marketers can make more informed decisions about the optimum size, shape and timing of marketing budgets so that properly-funded marketing activities can contribute to revenue and profitability growth.

So the answer to the eternal question of how to boost profits even when revenues are falling may well be this: invest in marketing.

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