ADVERTISING EXPENDITURE, FIRM PERFORMANCE, AND MODERATING IMPACT OF HUMAN CAPITAL AND FIRM SIZE IN INDIAN HOSPITALITY SECTOR: AN EMPIRICAL NOTE

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ABSTRACT

This empirical note investigates the impact of advertising expense on the firm performance, and moderating impact of human capital and firm size on this relationship for the 69 Indian hospitality firms during the period 2012 - 2022. We employ panel fixed effect regression to analyse the relationship. Empirical results suggest that advertising spendings significantly boost firm performance measured through net sales, asset turnover ratio and return on assets. Further, human capital and size positively and significantly moderates the advertising spending – firm performance relationship only in case of net sales as performance measure. Thus, hospitality firms should continue to develop long term advertising policy to have better performance.

Keywords: Advertising expenditure, Firm performance, Human Capital, Indian Hospitality firms, Panel Data.

INTRODUCTION

Advertising being widely adopted marketing strategy among firms primarily intended to enhance consumers' product awareness and facilitate informed purchase decisions; increase consumer demand and profitability; and a competitive edge over competitors (Park and Jang, 2012). Therefore, firms have significantly increased the advertising spending significantly. In India, firm's annual gross advertising spendings has reached INR 1,26,818 crores from INR 35,117 crores during 2012 – 2022 period (GroupM TYNY 2023 report). Furthermore, this advertising spending is primarily dominated by digital (54%), and followed by television (31%), print (11%), OOH (2%), radio (1%) and cinema (1%) media and originates mainly telecom, retail, media, gaming, fintech, travel & tourism sector (GroupM TYNY 2023 report).

Therefore, the dynamics between advertising spendings and firm performance have been extensively examined by marketing and finance researchers from developed and developing economy perspective. However, the empirical outcomes on this issue remain mixed and inconclusive. We briefly discuss the related literature in the context of hospitality sector here. Kim et al. (2013) evaluated how advertising affected consumer behaviour and corporate performance in 119 US restaurant firms from 1991 to 2012. They found advertising increased sales immediately but not profit. Assaf et al. (2015) evaluated how advertising spending affects financial performance in Slovenian and Croatian hotel. They confirmed that advertising boosts hotel sales, and this linkage becomes stronger for larger hotels and hotels having higher star ratings. Later, Assaf et al. (2017) examined the moderating impact of corporate social responsibility (hereafter CSR) on the link between advertising spending - firm performance (proxied by sales and market value added) relationship in US hotels and restaurants during the period 2001 -2012. They found that firms with a higher level of CSR resulted into higher returns on their advertising investments. Acar and Hüseyin (2017) demonstrated that advertising spendings positively impact Turkish bank performance over the period 2007 to 2015. They also revealed that advertising spending had long-term financial benefits for these banks. Similarly, Tackx et al. (2017) examined the advertising spending - financial performance dynamics among the world's top 500 brands of established companies for the year 2008

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– 2015. They found that brand value and R&D spending boost profitability, but advertising does not. Further, they confirmed advertising and R&D spending interact positively, while brand value and R&D spending interact negatively with profitability. Thus, Advertising only boosts profitability when it fosters consumer value development through R&D. or advertising doesn't make a business more profitable. It only does so when it helps create customer value through research and development.

Hughes et al. 2018 examined the linkage between marketing investment intensity and Tobin's Q (as measure of shareholder's value creation), and moderating impact of human capital productivity on this linkage among US firms during 2004 – 2014. They found a U-shaped relationship between marketing investment intensity and Tobin's Q. Further, human capital productivity positively impacts Tobin's Q and positively moderates the relationship. Later, Sardo (2018) examined how intellectual capital sub-components impact financial performance of 934 Portuguese hotels over the period 2007 - 2015. Their findings revealed that all intellectual capital sub-components including human capital have positive impact on their performance.

Jaisinghani and Kanjilal (2019) used panel threshold regression to study how marketing spending affected Chinese manufacturing enterprises from 2008 to 2017. Their findings showed that marketing expenditure benefits smaller enterprises below the threshold size value. Firm performance is adversely impacted by advertising in case of upper regime firms having size greater than threshold. Later, using a sample of 589 listed South Korean firms from 2012 to 2016, Xu et al. (2019) observed that advertisement positively affects financial performance for large companies but negatively affects smaller ones. Similarly, Manala and Atienza (2020) analysed advertising spending - firm performance nexus in 57 Philippine Stock Exchange-listed companies from 2008 - 2017. Their findings revealed that advertising spending improves sales but diminishes net profitability. Later, Farooq and Pashayev (2020) evaluated how product market competition influence advertising spending on company performance among non-financial firms in India over the period 2009 to 2018. Firms operating with high rivalries benefit more from advertising spending rather than those firms operating in low competitive sectors. Hua (2020) studied how human capital affected operating performance (measured through total revenue and earnings before interests, taxes, depreciation and amortization (EBITDA)) among 1,471 US hotels between 2010 - 2017. Their finding indicates that human capital strengthens operating performance measured through operating profit and total revenue.

Semenov and Randrianasolo (2022) examine how firm age and cultural style moderate the association between advertisement intensity and performance for 262 enterprises from 13 countries. Their findings revealed that firm age significantly and positively the relationship only in high context cultures but not in low-context cultures firms. Similarly, Kamal and Singh (2023) found the advertisement improved the market value of 680 Indian firms across 41 industries over 2003-04 to 2017-18. Similarly, Lee et al. (2023) studied the interactive impact of CSR and advertising spending on financial performance of 2431 listed Chinese enterprises from 2011 to 2019. Their findings confirmed that advertising investments significantly improve financial performance and CSR positively moderates. Later Akorede (2023) explored moderating effects of firm age and size on advertisement expenditure - firm performance linkage for 28 Nigerian listed firms 2014 to 2019. Their findings revealed that advertising spending increases sales but not return on asset for the sample firms. Further, advertisements also enhance sales more for larger companies than the smaller firms. Thus, literature review clearly suggests that empirical outcome on the advertising – firm performance and moderating role of contextual variables remain mixed and ambiguous.

This study contributes to the hospitality literature in two ways. Firstly, following organizational adaptive learning theory, we analyse the dynamics between advertising spending and firm performance for the 69 hospitality firms from the market and financial impact perspectives over the period 2012 – 2022 in an emerging economy i.e. India. We measure firm performance through both accounting and market performance measures through net sales, asset turnover ratio, and return on

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assets to have robust inferences in hospitality firms. Secondly, literature suggests that dynamics between advertising spending and firm performance is highly intricate and assessing it directly might be deceptive. Therefore, we follow the contingency approach suggested by Luo and de Jong (2012) and employ two firm specific contextual parameters namely human capital and firm size as moderating variables which might affect the advertising – firm performance dynamics.
The subsequent outline of this study continues as follows. Section 2 provides empirical framework and data used in the study and followed by empirical results in Section 4. Finally, we conclude our study in Section 5.

METHODOLOGY AND DATA

Model specification

To access the effect of advertising spending on firm performance, we specify the basic model as follows:

$$Y_{it} = \beta_0 + \beta_1 Adv.Spending_{it} + \sum_k \beta_k Control_{kit} + \varepsilon_{it} \quad (1)$$

where Y denotes firm performance measures. *i* indicates individual firms. *t* represents year. Adv. Spending is main regressor i.e. firm's advertising spending. Control denotes the firm specific and macroeconomic control variables used in the study. β_0 and ε_{it} represent a constant and the error term respectively.

Moderating Role of Human Capital and Size on the Advertising Spending on Firm Performance Dynamics

Firm's advertising spending tends to be critical determinants of firm performance (Abdel-Khalik, 1975; Assaf et al., 2015; 2017), which might be impacted by some variables like firm size, human capital (Assaf 2017; Adesina, 2019; Akorede, 2023; Jabbouri et al., 2023). To analyse these dynamics, we specify following model:

$$Y_{it} = \beta_0 + \beta_1 Adv.\ Spending_{it} + \beta_2 Adv.Spending * Human\ Capital_{it} + \beta_3 Human\ Capital_{it} + \sum_k \beta_k Control_{kit} + \varepsilon_{it} \quad (2)$$

$$Y_{it} = \beta_0 + \beta_1 Adv.\ Spending_{it} + \beta_2 Adv.Spending * Size_{it} + \beta_3 Size_{it} + \sum_k \beta_k Control_{kit} + \varepsilon_{it} \quad (3)$$

where Y denotes firm performance measures. *i* indicates individual firms. *t* represents year. Adv. Spending is main regressor i.e. firm's advertising spending. Human capital, and size are two moderating variables used in the study. Control denotes the firm specific and macroeconomic control variables used in the study. β_0 and ε_{it} represent a constant and the error term respectively.
The coefficient of interaction term and its magnitude (i.e. *Adv.Spending * Human Capital; and Adv.Spending * Size;*) will indicate whether moderating variables (Human capital, size and economic policy uncertainty) positively impact the advertising spending – firm performance dynamics and vice versa.

Variables and their Measurement

Following related literature, this study uses three dependent variables namely Net Sales, Asset Turnover Ratio (ATO) and Return on Assets (ROA) as performance measures (Acar and Temiz, 2017; Akorede, 2023; Assaf et al., 2017; Kamath, 2019; Kim et al., 2018; Molla and Rahman, 2022; Smriti and Das, 2018; Xu et al., 2019). Net sales are annual sales values nett of indirect taxes, whereas asset turnover ratio assesses a firm's asset efficiency. Return on assets shows how well a

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company uses its assets to generate net income. We measure the advertising spending using the log of the annual advertising spending and log of sales and distribution cost of the firm for the robust inference (Akorede, 2023; Chen, 2020).

Firm specific human capital is computed using the widely used value added intellectual capital (VAIC™) framework developed by Pulic (2004). This approach employs annual financial data to compute human capital (Adesina, 2021; Kamath, 2019; Vidyarthi, 2019). Human capital is value added (summation of operating profit, employee compensation and depreciation) divided by gross employees' compensation. Higher human capital is always preferable at the firm level as it shows superior contribution of each unit of human capital employed to the firm's value added. We incorporate three firm specific factors namely natural logarithm of firm's total assets (Size) to control firm size, ratio of debt to total asset ratio (leverage) to control the capital structure, sales growth rate (calculated as annual growth in net sales). Further, we consider GDP growth rate and Inflation to control for the overall economic climate that may affect hospitality firm's performance. Since, our dataset coverage includes Covid pandemic timings as well, during which Government regulations (like complete and partial lockdown, and restriction of group gatherings) were imposed. These regulations might have impacted the financial performance of the hospitality firms as well. Therefore, we have used dummy variable for the pandemic year 2020 – 2022 to ascertain the impact of Covid pandemic on the firm performance in the hospitality sector.

Data

This study employs the Centre for Monitoring Indian Economy (CMIE) - PROWESSIQ database, i.e. most prominent data sources for Indian incorporations. Our sample consists of balanced panel data comprising of 69 hospitality firms having minimum INR 10 Crores as annual sales / revenue over the year 2012-2022. Further, macroeconomic variables have been extracted from the World Development Indicator (WDI) – 2023. We present descriptive statistics and correlation matrices of the variables employed in the study in Table 1. The correlation among the independent variables clearly indicates that our empirical models don't have multicollinearity problems.

Table 1
DESCRIPTIVE STATISTICS AND CORRELATION MATRICES OF VARIABLES EMPLOYED IN THE STUDY

	Obs	Mean	Std. Dev.	lnSales	ATO	ROA	AD1	AD2	Size	VAHC	Leverage	Sales Growth Rate	GDP Growth Rate	Inflation
lnSales	759	6.437	1.217	1										
ATO	759	0.429	0.35	0.089*	1									
ROA	759	0	0.103	0.044	0.230*	1								
AD1	759	2.074	1.689	0.748*	-0.096*	0.169*	1							
AD2	759	2.717	1.56	0.735*	-0.172*	0.150*	0.874*	1						
Size	759	7.566	1.364	0.818*	-0.409*	-0.103*	0.676*	0.702*	1					
VAHC	759	2.291	1.173	0.164*	-0.176*	0.275*	0.198*	0.275*	0.228*	1				
Leverage	759	0.573	0.501	-0.04	-0.036	-0.642*	-0.195*	-0.120*	-0.008	-0.068	1			
Sales Growth Rate	759	-0.109	0.698	0.223*	0.220*	0.245*	0.140*	0.135*	-0.009	0.233*	-0.034	1		
GDP Growth Rate	759	0.056	0.039	0.185*	0.192*	0.226*	0.125*	0.112*	-0.012	0.168*	-0.028	0.842*	1	
Inflation	759	0.062	0.023	-0.100*	-0.048	0.012	0.002	-0.06	-0.051	0.06	-0.037	-0.073*	-0.141*	1

Note: * represent statistical significance at 5 % respectively.

Empirical Results

The empirical results presented in Table 2 shows that advertising spending has positive and significantly associated with the firm net sales, asset turnover ratio (ATO), and return on assets (ROA) values at 10% significance level. However, impact is much stronger in case of Net Sales as dependent variable and followed by asset turnover ratio and return on asset respectively. The overall

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findings are in line with the previous studies (i.e. see Adeola, 2016; Akorede, 2023; Assaf et al., 2015; Assaf et al., 2017; Kim et al., 2019, Lee at al., 2023; Laing et al., 2010; Rahman et al., 2020).

In line with existing literature (see i.e. Adesina, 2020; Sardo et al., 2018; Vidyarthi, 2019; Tiwari et al. 2023) positive and significant impact of human capital on firm performance, either measured through net sales, asset turnover ratio or return on asset, clearly indicate the critical role played by human capital through their skills, knowledge, and experience in hospitality sector.

Table 2
SELECTED REGRESSION RESULTS ON ADVERTISING SPENDING – FIRM PERFORMANCE DYNAMICS FOR INDIAN HOSPITALITY FIRMS DURING 2012 – 2022 PERIOD

Variables ↓	lnSales		ATO		ROA	
AD1	.1301***		.0348***		.0035*	
AD2		.1096***		.0285***		.0093**
Size	.2139***	.2247***	-.3349***	-.3327***	.0115	.0085
VAHC	.0634***	.0653***	.0238***	.0237***	.0331***	.0322***
Leverage	-.1545***	-.1336***	-.0577***	-.0544***	-.1006***	-.1009***
Sales Growth Rate	.2539***	.25***	.034***	.0331***	-.0014	-.0035
Covid	-.1057***	-.135***	-.0434***	-.0501***	-.0021	-.0013
GDP Growth Rate	.0621	.1375	.3971**	.4269***	.3958***	.413***
Inflation	-4.1667***	-4.078***	-1.6585***	-1.6232***	-.1531	-.1203
Constant	4.7977***	4.6656***	2.9649***	2.9375***	-.1272	-.1239
Observations	690	690	690	690	690	690
R^2	0.8288	0.8148	0.5834	0.5776	0.2992	0.3036

Note: *, ** and *** represent statistical significance at 1, 5 and 10% respectively.
Source: Author's estimation

Among control variables, Leverage is significantly and negatively associated with all performance measures at 10% significance level suggesting that firms with higher proportion of debts in capital structure seems to detrimental impact on the performance measures (Hall and Weiss,1967; Fazzari et al.,1988; Stulz,1990). Firm size is positively associated with the net sales. It indicates that larger firms have economy of scale particularly through higher sales. However, negative relationship between size and asset turnover ratio indicates the presence of agency costs (Canarella and Miller, 2022). Secondly, insignificant impact of size on return on asset indicates more complex structures of management contributing to a diminished efficiency as well as financial performance and under reporting of profit despite higher sales mainly by larger hotels (Chen, 2009; Kim and Lee, 2013; Zeglat and Zigan, 2014). Sales growth rate is having positive impact on sales and asset turnover ratio but insignificantly associated with return on asset (Jang and Park, 2011). Similarly, covid pandemic had significant and negative association with the sales and asset turnover ratio but insignificantly associated with return on asset (Hu and Zhang, 2021). GDP growth rate is positively associated with performance measures except return on asset, in line with previous findings (Domowitz et al., 1986; Egbunike and Okerekeoti, 2018; Otambo, 2016). Inflation is having negative impact on the firm performance.

Table 3
SELECTED REGRESSION RESULTS ON MODERATING IMPACT OF HUMAN CAPITAL ON ADVERTISING SPENDING – FIRM PERFORMANCE DYNAMICS FOR INDIAN HOSPITALITY FIRMS DURING 2012 – 2022 PERIOD

Variables ↓	lnSales		ATO		ROA	
AD1	.0983***		.0405***		.0031	
AD2		.0818***		.0373***		.015**
AD1VAHC	.0145**		-.0026		.0002	
AD2VAHC		.0127**		-.004		-.0025
VAHC	.0348**	.0342*	.029***	.0335***	.0327***	.039***

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Size	.2192***	.2281***	-.336***	-.3338***	.0115	.0076
Leverage	-.1543***	-.1336***	-.0578***	-.0543***	-.1006***	-.1009***
Sales Growth Rate	.2589***	.2539***	.0331***	.0318***	-.0013	-.0042
Covid	-.1079***	-.1344***	-.043***	-.0503***	-.0021	-.0016
GDP Growth Rate	-.0045	.0841	.4093***	.4429***	.3952***	.4179***
Inflation	-4.1769***	-4.0473***	-1.6558***	-1.6329***	-.1533	-.128
Constant	4.8202***	4.7027***	2.9615***	2.9257***	-.1268	-.131
R^2	0.8304	0.8160	0.5838	0.5787	0.2992	0.3051
Note: *, ** and *** represent statistical significance at 1, 5 and 10% respectively. **Source:** Author's estimation						

Table 4
SELECTED REGRESSION RESULTS ON MODERATING IMPACT OF FIRM SIZE ON ADVERTISING SPENDING – FIRM PERFORMANCE DYNAMICS FOR INDIAN HOSPITALITY FIRMS DURING 2012 – 2022 PERIOD

Variables ↓	lnSales		ATO		ROA	
AD1	.0311		.1516***		.0703***	
AD2		-.0685		.1175***		.0666***
AD1Size	.0132		-.0155***		-.0089***	
AD2Size		.024***		-.012***		-.0077**
VAHC	.0639***	.0649***	.0233***	.0241***	.0325***	.0326***
Size	.1886***	.1665***	-.3052***	-.3033***	.028**	.0267*
Leverage	-.1548***	-.1332***	-.0565***	-.0537***	-.1***	-.1003***
Sales Growth Rate	.254***	.2528***	.034***	.0317***	-.0008	-.0037
Covid	-.1069***	-.1377***	-.0429***	-.0496***	-.0024	-.0016
GDP Growth Rate	.0487	.0622	.4061***	.4585***	.3891***	.4173***
Inflation	-4.1892***	-4.1337***	-1.6331***	-1.5971***	-.14	-.1047
Constant	4.9688***	5.07***	2.7628***	2.7321***	-.2374***	-.2506***
R^2	0.8289	0.8162	0.5917	0.5830	0.3087	0.3114
Note: *, ** and *** represent statistical significance at 1, 5 and 10% respectively. **Source:** Author's estimation.						

Moderating Regression Results

We present the moderating impact of human capital and size on the relationship between advertising spending and firm performance in Indian hospitality firms in Table 3 and 4 respectively. In Table 3, human capital significantly moderates the relationship between advertising spending and firm performance, measured by net sales only at 5% significance level. Other moderations (in case of asset turnover ratio and return on asset as dependent variable) remain insignificant. As presented in Table 1, average annual human capital for the entire sample is very low (2.291 with a very high standard deviation of 1.173) with respect to other economies. This indicates that these firms generate only ₹ 2.291 rupee for every ₹ 1 of investment in human capital. Therefore, these firms need to further augment in the human capital investment through training and development and retaining the experienced employees in order to realise the full potential of human capital.

Secondly, In Table 4, firm size partially but significantly moderates the relationship between advertising spending and firm performance, measured by net sales at 10% significance level (Akorede, 2023; Assaf et al., 2017; Rahman et al., 2021). Other moderations (in case of asset turnover ratio and return on asset as dependent variable) are significant and negatively moderated. It indicates that as the firm size increases, there is diseconomies of scale are applicable in case of asset turnover ratio or return on asset as dependent variable.

CONCLUSION

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This study examines impact of advertising expenditure on financial performance among 69 hospitality firms operating in India during the period 2012 – 2022. Also, we examine how human capital and size is moderating this relationship. Our panel fixed effect regression indicates that advertising spending positively and significantly impact all three performance measures, namely net sales, asset turnover ratio, and return on asset, used in the study. Thus, advertising spending not only enhances customers' positive perceptions, but also financial performance. Secondly, we also found positive impact of human capital on all three performance measures, indicating the critical role played by human capital in the success of these firms. However, moderating impact of human capital and size is positive only when net sales as dependent variable. Thus, better human capital and firm size further strengthens the advertising spending – firm performance nexus. Thus, hospitality firms should simultaneously consider advertising spending and human capital investment as these firm's success lies on human capital. However, the same is not reflected in case of asset turnover ratio and return on asset as dependent variable. We also found the recent Covid pandemic has adversely impacted the performance as widely perceived. Future research should consider the optimal level of advertising spending, internal composition of advertising spendings and their features, and their association with the performance measures.

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