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Net Revenue Management - Are You Leaving Money On The Table?

by Tom Gallen

Consumer health players risk missing deserved revenue and profits by failing to take a holistic approach to net revenue management. In this exclusive interview, Simon-Kucher & Partners' Josh Goodman explains how effective NRM can have a big impact on sales and profits by ensuring full capture of willingness to pay, maximizing promotion ROI, incentivizing beneficial trade terms, prioritizing appropriate channel presence, and capturing all relevant customer purchase occasions. Goodman offers his top tips for small NRM hygiene factors that can make a big difference.

Increasingly price sensitive consumers, savvier retailers and competitive new market entrants are eroding the already tight margins of consumer health manufacturers.

With instant access to product comparisons and ongoing promotions, consumers are better informed and more price sensitive in their pursuit of their desired products. Retailers also have greater access to more data on consumer purchasing habits, and can utilize data analytics to ensure that their product mix, promotions, and prices are revenue or profit optimal. Furthermore, the growth of the online channel has made it easier than ever before for start-ups to enter the market.

Faced with these challenges, prioritizing net revenue management (NRM) is more important than ever before for consumer health players to ensure full revenue and profit capture, says Josh Goodman, head of US Consumer Healthcare at strategy and marketing consultants Simon-Kucher & Partners.

NRM consists of five key elements:

- Pricing

- Promotion
- Trade terms
- Channel strategy
- Portfolio strategy

Speaking exclusively to *HBW Insight*, Goodman notes that while firms may be familiar with NRM, and may have even trialled it in one or two markets, the full benefits can only be felt by embracing it as a company-wide strategy.



SIMON-KUCHER & PARTNERS' JOSH GOODMAN

“There are a lot of consumer health companies implementing NRM, but they might only be doing it in one country, or not taking a holistic approach by focusing on only one facet,” Goodman explains. “We often see companies that don’t have the full process laid out for how to go about achieving their goals, whether it’s pricing excellence or promotion excellence.”

Goodman insists that a half-baked approach to NRM, or worse, ignoring it entirely, can have

significant negative consequences for manufacturers' sales and earnings. "If you're mismanaging any one of the key elements of NRM, whether it's pricing, promotion, trade terms, channel strategy or your overarching portfolio strategy, that means your products could be overpriced and not getting the volume that you really could get if you had an overarching strategy that is reflective of the value."

While firms may recognize the rewards effective NRM can bring, Goodman admits that for some manufacturers the prospect of company-wide implementation can seem daunting. "Some companies look at this whole topic and they can get overwhelmed, but a good start is to just put a framework together to identify an objective they want to achieve, such as more effective promotions. They then define how they're going to achieve that objective and go and actually monitor and measure the outcomes of those activities."

"Just putting that together can help manufacturers as then they will better understand how the actions they're taking impact their bottom line."

"You don't need to have these huge complex systems," Goodman insists, "Simple changes can make a big difference."

Pricing: Capitalize On Consumers' Willingness To Pay

For firms looking to implement NRM, pricing is a great place to start, says Goodman, as it is one of the strongest levers for revenue and profit impact.

"In an increasingly globalized market, maintaining a global pricing strategy is key," he points out. "By properly positioning products both within the brand portfolio and against the relevant competitive products, consumer health manufacturers can capitalize on end consumers' full

NRM Action Items

Simon-Kucher & Partners' top tips for effectively implementing NRM:

Pricing: Price position portfolio products in relation to consumers' willingness to pay for benefit sets that each product offers

Promotions: Ensure that every promotion planned is designed to achieve a specific objective

Trade terms: Leverage mutually beneficial pay-for-performance trade terms to forge a true partnership with your trade partners

Channel: Design your channel offerings around your consumers' purchasing preferences for each product type

Portfolio: Determine key purchase occasions for your portfolio and ensure your pack sizes, product types, and assortment capture each of them

willingness-to-pay while simultaneously building a global brand position.”

Companies must have an overarching strategy for how they want to price position their products, Goodman insists. “Do they want to be the premium player? Or the discount player?”

The growth of e-commerce makes it more important than ever for firms to think globally about pricing. “Once you can buy something online it becomes a global product,” he notes, “so you really need to have a global strategy, because your pricing gets out there across numerous markets, not just one.”

“Firms should set up guidance that each country manager can leverage to do their work at a local level around the price-positioning of a product,” he suggests.

Drawing up a value ladder is a great place to start, Goodman advises

For consumer health players unsure where to begin, Goodman advises drawing up a value ladder. “If you have a portfolio of products that build on top of each other, you can set up a formal value ladder so that all of the different product managers on a global and country level know a certain product should always have a certain premium over another product, or at least a premium range.”

“With a value ladder, you know that your products are going to be similarly positioned on a global basis,” he explains.

Asked how firms can determine the best price for their individual products, Goodman says it’s all about understanding their value to consumers. Ideally, this should be top of mind during the new product development stage.

“Design the product outside in, not inside out,” Goodman recommends. “It should be built to deliver a benefit to a consumer that’s going to be valuable for them. You don’t want to add features to a product just because you can.”

For both new and established products, the “gold standard” for determining value and what consumers are willing to pay is conducting market research, he notes. “This approach allows you to present consumers with products that are in their consideration set and really understand

what's driving the value of each of the products relative to competitors in the market."

"Understanding where the customer sees the different value components of a product, or portfolio, is really important," Goodman says. "What are consumers willing to pay extra for?"

"If you have a product where you know the willingness to pay is inherently higher, but you have it priced at parity, or even worse at a discount, you're leaving money on the table."

Giving the example of toothpaste, Goodman notes that parents tend to be willing to spend more money on oral-care products for their children as they want to make sure they brush their teeth. Furthermore, a toothpaste promising teeth whitening might also command a higher price among consumers with a perception that they need whiter teeth, he suggests.

"If as a manufacturer you don't understand what the value drivers are in a given category, you're not going to be able to price position your product portfolio the right way to reach your revenue and profit potential," Goodman observes.

Promotions: What Are You Trying To Achieve?

With a global pricing strategy in place, the next key element of NRM for consumer health players to consider is promotions. While effective promotions can have a positive impact on sales and brand perception, Goodman says getting it wrong can undermine or cause irreparable damage to a brand's image and price positioning.

"The majority of promotions don't generate incremental value for the manufacturer," he explains. "If you're discounting your price [to drive volumes and revenue] you need to gain enough incremental volume to counteract the lower margin, but some firms fail to even make that simple calculation. If you're spending money on a promotion, are you even recouping that spend by achieving the goals for conducting the promotion in the first place?"

According to Simon-Kucher's research, almost 70% of promotions are value destroying. By implementing a proper promotion management system, the firm estimates that most manufacturers could significantly decrease the share of promotions that lose marketing spend.



'ALMOST 70% OF PROMOTIONS ARE VALUE DESTROYING'

Goodman advises that it is crucial to understand the role of a promotion in order for it to be successful. “There’s all sorts of promotions that help you achieve the different goals that you have, but not all promotions are created equal.”

Firms need to think about the end goal they’re looking to achieve with a promotion, Goodman says. “Is it to increase your penetration in the market, or to increase purchase frequency, or do you want consumers to trade up to a more premium product?”

Without a promotion strategy, manufacturers risk discounting the wrong product and selling it too cheaply to consumers that were willing to pay full price, he explains. “If you’re looking to entice new consumers to try your product, it’s not a good idea to discount a bulk pack as you’re essentially discounting the product to the people that are already sold on it. By discounting the single pack, you’re allowing non-existing customers try the product on a small unit basis.”

Getting promotions wrong can lead to a change in consumer behavior, Goodman notes. “If you run promotions too frequently then you’re training consumers to buy only when you’re running promotions. Selling via promotions only is OK, if this is the intended strategy, however we have seen companies unintentionally train customers to buy only during promotion periods.”

Trade Terms: Incentivize Retailers To Promote Your Products

Not only can consumers come to expect discounts, but so can retailers, he points out, which is why it's vital for consumer health firms to have a clear promotion strategy in place. "When sitting down with retailers talking about different trade terms it's really important to make sure you have flexibility. Do you have to run a certain number of promotions during certain times? Or can you work with them to develop a schedule for what makes sense for both you and their business?"

It's in the retailer's interest to work with manufacturers and offer them flexibility on discounts, Goodman argues, as effective promotions benefit both parties.

As well as being important in their own right, promotions play a crucial role in trade terms, the third element of NRM.

Goodman points out that while trade term spends are among the largest investments for consumer health manufacturers, they often lack transparency and effectiveness.

Ongoing channel-partner consolidation and increasingly transparent global pricing are further intensifying the importance for firms to offer consistent trade term systems across channels, trade partners, and countries, Goodman notes. Not only does this reduce the confusion that trade partners may have from inconsistent terms, but it also allows the manufacturer to develop performance-based terms that incentivizes partners to behave in a manner beneficial to the manufacturer.

"Avoid having a one-sided relationship with a retailer, be a good partner to them as well." - Josh Goodman, Simon-Kucher & Partners

The starting point for negotiating trade terms is good preparation, Goodman advises. "Oftentimes the manufacturer has the goal – especially if they're a start-up or single product company – of just getting the product through the channel. So they just have that one objective and they haven't necessarily properly prepared for the negotiation."

"There's lots of different mechanisms as part of these negotiations so it's important to know what your objective is," Goodman insists. "Are you trying to include product training for store associates to better communicate the value of your products over competitors or would better

positioning on the shelf be more valuable for your products?

It's important for manufacturers to put the proper incentives in the contract for the retailer to get them to act favorably, according to Goodman. "You should try and avoid having a one-sided relationship, so you're a good partner to them as well," he advises.

"Making sure the retailer is getting a really good margin could be a way to really help with the competitive positioning of your products in their stores. If they're getting great margin from you, they won't accept a lower margin from a competitor, because that doesn't help them, in fact it hurts the retailer every time they sell that competitor versus your product," he explains.

Channel Strategy: Not All Consumers Are Created Equal

With effective trade terms secured, a global pricing strategy in place and promotions that increase profits rather than cannibalize them, consumer health firms must next think about implementing a coherent channel strategy, Goodman advises.

Traditionally, understanding the consumer journey or path to purchase within a specific channel was a key element of any sound channel strategy, Goodman says. However, today's increasingly connected consumers not only expect a seamless omni-channel experience, but also cross-reference information across all channels before making a purchase decision.

"Consumers are so experience driven that some would even refrain from a purchase if their expectations are not met when moving from one channel to another," Goodman points out, "which makes channel strategies an essential tool for capturing a consumer's business."

For Goodman, understanding consumer segmentation is key for manufacturers. "Firms should think about who their consumers are and why they are buying their products. Not all consumers are created equal, they fall into different segments, whether it's behavioral or otherwise."

It's also crucial to understand why a consumer is buying a product at that time and in that location, Goodman says. "In

NRM Success Stories

Examples of how effective NRM has helped Simon-Kucher & Partners' clients:

- A leading consumer health manufacturer experienced an annual profit impact of more than \$4m by redefining their pricing structure to better capture consumer willingness-to-pay based on product value drivers
- A leading consumer health generics manufacturer experienced a 23% increase in profits by enhancing their trade terms with improved comprehension and implementation of a

consumer health, there tends to be a specific need for why a consumer is going to buy a product. If someone has an acute need they're not going to go to the web, but to a store. It's also unlikely they're going to want to buy a huge bulk quantity – they want to buy a product to solve their problem and be done with it.”

“Knowing that, it makes no sense as a manufacturer to only offer bulk products in a bricks-and-mortar convenience store,” he explains, “or to only offer single unit packaging in a club store, for example.”

“It's important to understand what the need is for the product and why the consumer would be buying it in pharmacy versus online. Then you must think about how to position the product, the packaging and the pricing to take advantage of that purchase situation.”

Once consumer health firms know who their consumers are and what motivates them, they can then leverage that knowledge when in discussions with retail partners, Goodman points out.

“You can say to the retailer, ‘look here's the pricing you could get, here's what we anticipate from a market share perspective and this is why you should have our products in your store.’”

Portfolio Strategy: Don't Paralyze Consumers With Too Much Choice

Once firms have identified who their consumers are and where they want to buy, it is crucial to make sure the product offering is available in the right place at the right time. Central to this is portfolio strategy. A well-managed portfolio can not only help a consumer manufacturer better utilize the other four levers for NRM, but also be utilized as a lever itself, Goodman argues.

By optimizing the product offering – the pack size, type and assortment – within each channel, companies can improve conversion rates by meeting consumer purchase occasion needs, at the time of purchase, he says.

“If you don't have the right strategy across the board for your portfolio you can undo all of your good work. You can end up promoting a more premium product below the basic product,” he points out. “You might have the right pricing strategy in place, but because you've discounted your premium product below the base you've just destroyed your value ladder.”

In some cases portfolios can get too large, Goodman says, with so many pack sizes available for

pay for performance scheme

- An established OTC player achieved 17% volume growth by initiating a proactive e-commerce strategy across multiple categories
- A large consumer health manufacturer uncovered an estimated 4-18% incremental profit upside by optimizing pricing and pack sizes across four brands

an individual product consumers get confused.

“When there are too many options it paralyzes the consumer and they can’t make a decision because they don’t know which product they should be buying. In that situation, manufacturers must work to really understand the role of the products within their portfolio and how they should really play in the market. Part of that is identifying which products to discontinue and which to maintain.”

Immediate Impact On Top Line

Without a complete NRM strategy embracing all five key elements, it’s clear consumer health players will struggle to fully maximize sales and profits. Indeed, companies risk overpricing, or potentially worse, under-pricing their products, effectively leaving money on the table.

Goodman advises companies, “Single hygiene factors can have immediate impact on a company’s top line. While approaching NRM in a comprehensive holistic manner is ideal, not all companies are positioned to address all facets of NRM at once.”

“Simon-Kucher has clients who have seen profits increase just by optimizing single levers within NRM,” he notes, “identifying one or two areas for improvement helps internal buy-in and sets the company in the correct direction.”

Josh Goodman is a Partner in the Boston office of Simon-Kucher. He helped establish the firm’s Global Medical Technology Practice in the US, and he leads the US operations of the Global Consumer Healthcare Practice. His focus is on price setting and price execution activities, targeting product or portfolio launch and lifecycle strategies.

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