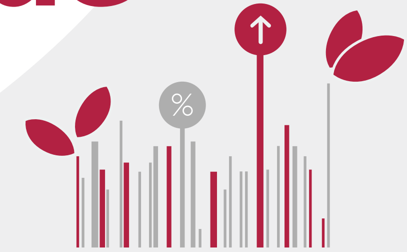
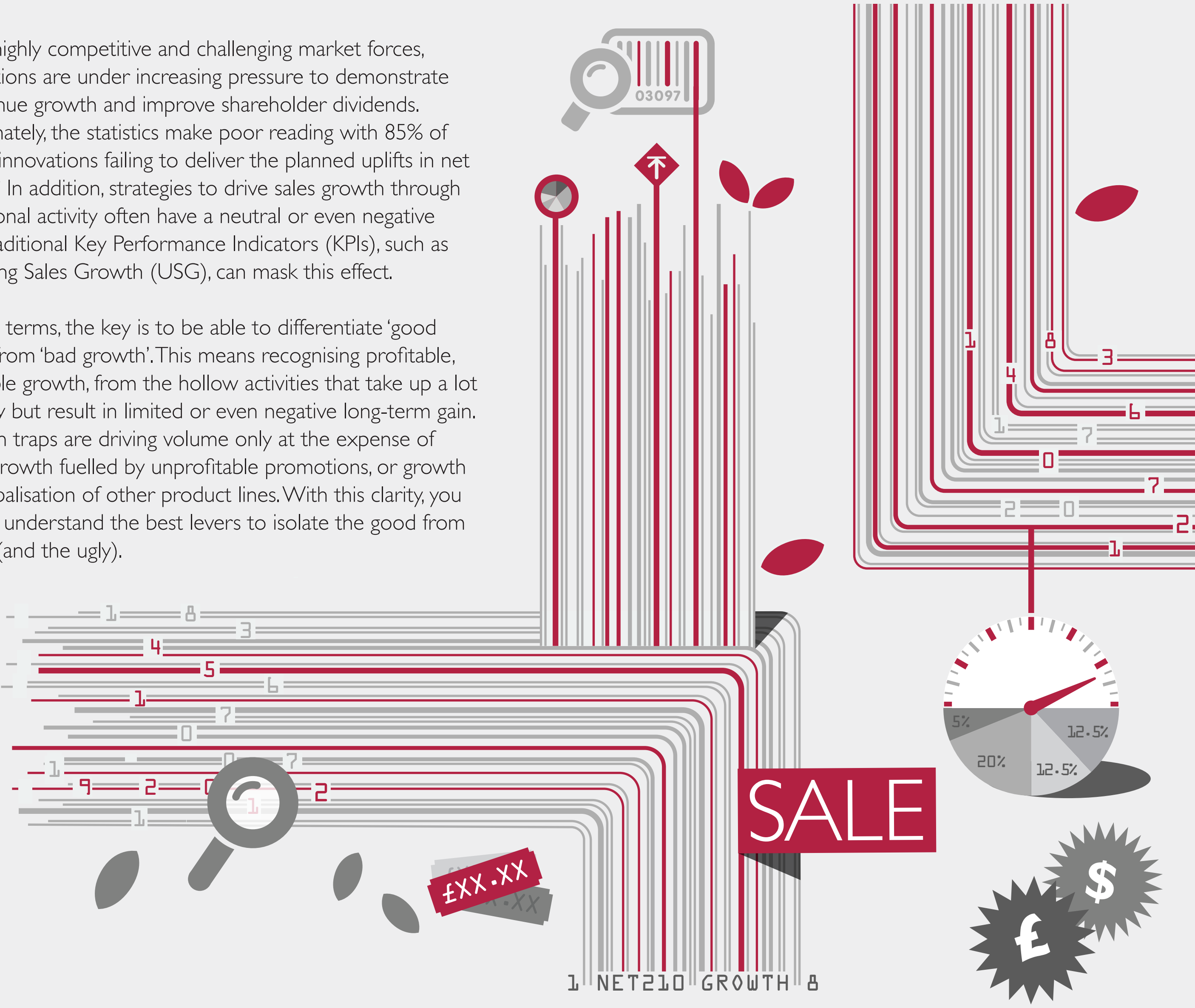
Secure "good growth" with Net Revenue Management



Net revenue growth should be at the heart of every business but too many organisations fail to deliver on their targets. Sales, productivity and volumes are up, but you're left scratching your head wondering what happened to expected corresponding profit gains. Nick Dawnay and Jon Bradbury look at the background and value of Net Revenue Management, and recommend six practical ways to help your organisation bring the focus back to profitable growth.

Due to highly competitive and challenging market forces, organisations are under increasing pressure to demonstrate net revenue growth and improve shareholder dividends. Unfortunately, the statistics make poor reading with 85% of product innovations failing to deliver the planned uplifts in net revenue.* In addition, strategies to drive sales growth through promotional activity often have a neutral or even negative effect. Traditional Key Performance Indicators (KPIs), such as Underlying Sales Growth (USG), can mask this effect.

In simple terms, the key is to be able to differentiate 'good growth' from 'bad growth'. This means recognising profitable, sustainable growth, from the hollow activities that take up a lot of energy but result in limited or even negative long-term gain. Common traps are driving volume only at the expense of margin, growth fuelled by unprofitable promotions, or growth by cannibalisation of other product lines. With this clarity, you can then understand the best levers to isolate the good from the bad (and the ugly).



*Nielsen 'The U.S. Breakthrough Innovation Report 2016'

What is NRM?

Net revenue management (NRM) provides organisations with the ability to effectively exploit the data available to them, identifying and leveraging opportunities for good growth – or, more precisely, net revenue growth. Originally conceived in the travel industry, NRM allowed airlines to use data to effectively price tickets based on fluctuating demand patterns. The automobile industry adapted this methodology to give manufacturers a better understanding of the optimal mix of their vehicle types. Following these early successes NRM has now been proven as a way of working that can, if applied correctly, drive real growth for organisations across all sectors. For the purpose of this article we have chosen to focus on the Consumer-Packaged Goods (CPG) sector. It provides a good case study due to the typically diverse nature of CPG product portfolios and the significant benefits that can be realised where this type of methodology is applied correctly in this environment.

NRM methodologies in practice – where is the value?

NRM introduces a new strategic Key Performance Indicator (KPI), which relates to change in net revenue (Turnover/ Unit of Volume) over time. The success or failure of brand strategies can be judged through whether corresponding targets are met.

NRM methodologies allow organisations to make informed, tactical decisions that drive real strategic success, reflected in positive net revenue changes. Specifically, this is achieved by analysing internal P&L and external market share data through a number of lenses.

NRM analysis helps you shed light on the following questions:

Portfolio Pricing – Are our products priced correctly against our competition? Are there any gaps in the market that we can exploit?

Pack Price Architecture – Do we have the optimum mix of product formats? Are these formats priced correctly?

Active mix – Is our product mix allocation optimised in a way that helps drive profitable growth?

As an example, a client in Latin America was looking to grow their share of the Mexican snack market. By conducting NRM pack price architecture analysis, they found that there was a culture for 'snacking in company'. As a result, the CPG successfully introduced a new shared snack in a different product category, which resulted in an uplift in net revenue.

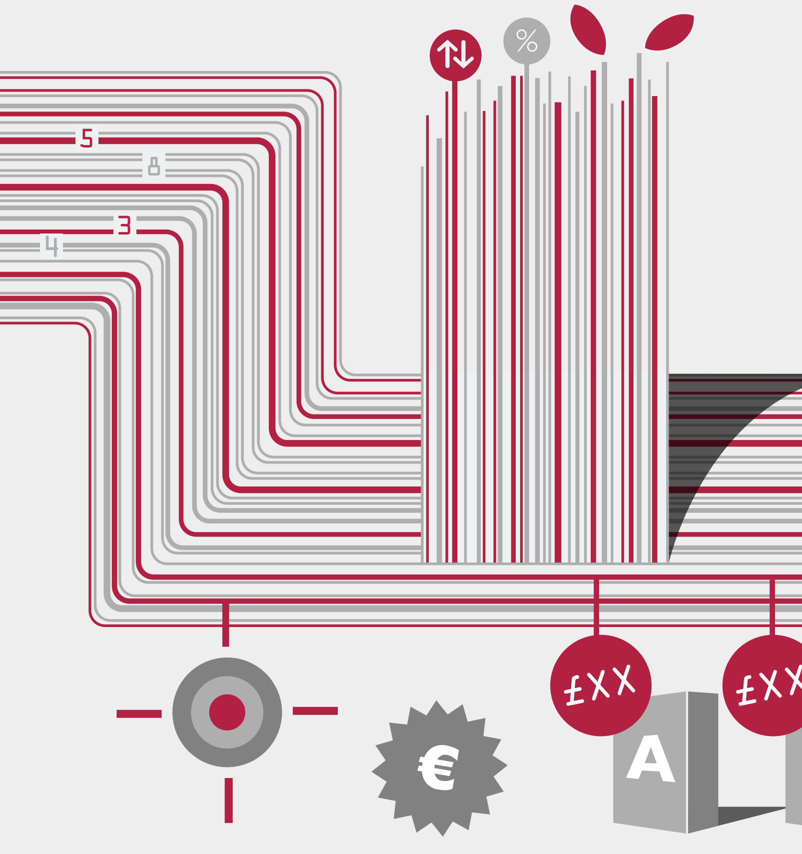
Promotion management – Are we promoting the right products in the right way to drive revenue growth?

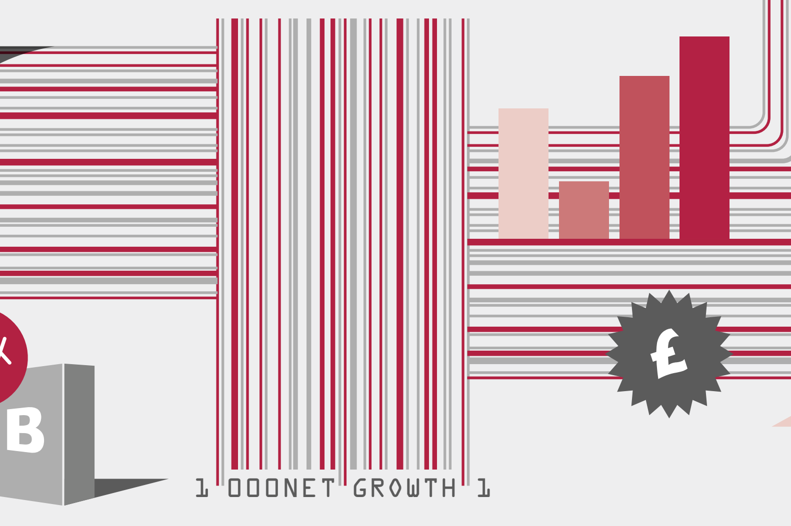
As an example, another client noticed that reported list price increases were not resulting in a corresponding uplift in net revenue. Following detailed NRM analysis, they recognised this was due to promotional activity offsetting these list price increases – and they were able to respond.

Trade Spend Translation – Are we getting the optimum return from our trade terms (which are the contracts CPG companies negotiate with retailers) and do we need to change our customer mix to drive revenue growth?

Innovations – Which innovations, and what types of innovation, are driving growth?

Using historical data to understand trends, NRM allows organisations to evaluate their product strategies over the long term. You can then properly maintain existing strategies and ensure new strategies are well-informed. NRM typically sits outside of the traditional remit of finance, marketing and supply chain, cutting across category or brand silos. Many organisations choose to establish new revenue management teams that



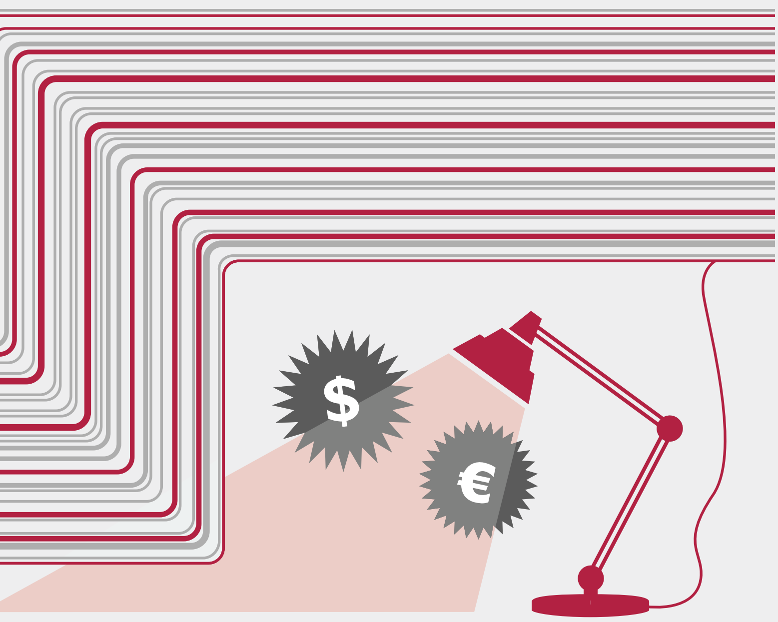


can easily draw information across these different business areas, building comprehensive strategies whilst strengthening working relationships.

NRM implementation – six steps to success

1. Business case and implementation structure – The level of investment and commitment required to successfully implement NRM is significant. A strong, detailed business case is required at the outset, clearly presenting both the benefits and what will be required to implement successful change. Due to the complex nature of NRM analysis a project will need to be set up to implement the methodology in a specific, pilot business area and it is recommended to start with this type of approach to prove the concept works. However, it is important for organisations to understand that NRM analysis is not a 'one off' exercise or project. NRM is a new way of doing business that will continue to drive revenue growth year on year and needs to be resourced accordingly.

2. Executive leadership and sponsorship – NRM introduces a new strategic KPI and a range of new metrics spanning the levers described above. These KPIs will complement the existing measures but may also expose gaps. For example, assessing performance through a net revenue lens could reveal a scenario where sales growth has been driven by increased promotional activity (the Marketing function is happy) but has not actually generated increases in turnover (so the Sales function is unhappy). As such, effective implementation requires total commitment throughout your organisation, to develop and deliver strategies aligned with net revenue targets, which may conflict with historical targets set against other KPIs. As with all strategic change initiatives, this type of commitment requires visible buy-in both from top leadership and throughout the organisation.



3. The right people, with the right skills and experience - In the short term, NRM expertise can be provided by consultancy organisations. However, you will need to consider investing in upskilling existing staff and/or recruiting new, experienced resources to ensure a cost-effective implementation that builds an enduring capability. Every organisation is unique, so naturally the NRM methodology application will need to be tailored to fit. For example, it can be hard to adapt NRM methodologies developed for companies with relatively few product categories, to one with a much wider range of different types of products in different sectors. By establishing an NRM Centre of Excellence (CoE), you can ensure your organisation forms a central group of senior executives to effectively develop and manage your NRM methodology and drive its implementation.

4. Integration with Business performance management and planning processes – Targets associated with traditional KPIs such as Underlying Sales or Volume Growth (USG / UVG) must be aligned with NRM KPIs. Without this, there is a serious risk that, at best, net revenue targets will not be achieved and, at worst, business performance as a whole will be threatened due to conflicting strategies.

5. Good quality data – the cornerstone of effective revenue management analysis. This means that:

   a. P&L data must be correct for the 'current' period but also well maintained allowing for effective historical analysis.
   b. Aligned or even common global product hierarchies are required. This makes it easier for senior executives and practitioners to compare performance across regions and for cost effective global IT tools to be developed.
   c. Common Units of Volume agreed across regions. As above, net revenue is defined as Turnover/ Unit of Volume. If standard Units of Volume are not agreed, net revenue will not be comparable across business units. For example, a global supplier of laundry detergents struggled to introduce a standardised Unit of Measure across regions, with many European countries using 'washes' and Asian markets only recognising 'tonnes' as the unit of measure (regardless of the level of concentration). By introducing a common global Unit of Measure the organisation was able to effectively compare performance across regions.

6. Strategic oversight of market share information – Organisations rely on a limited range of data providers (such as Nielsen and Kantar) for market share data and, in some cases, generate this data internally. NRM takes a standard approach to leveraging market share data, so you need to be prepared to renegotiate your existing provider contracts and seek improved data sources, with a view to securing the necessary data access. In addition, market share data providers may have little or no coverage of non-traditional, high growth channels (such as discounter and eCommerce channels) so you may need to look at innovative new approaches to ensure that you have the high-quality data required to make effective NRM business decisions in these channels.

IT as an NRM accelerator?

As above, NRM analysis can be a time-intensive, manual task requiring skilled resources who not only understand the methodology but are able to conduct the required financial modelling tasks. If good quality data is available, with the requisite standardised formats, hierarchies and taxonomies, then automation through technology tools can serve as a powerful NRM accelerator.

There are several 'standard' analytics tools available that can relatively easily be adapted to run NRM analysis, when good quality data is available. In addition, there is now a limited range of off-the-shelf NRM tools, although at this point these tools will only be cost effective for larger organisations (many of whom are also developing their own, bespoke NRM tools). Some organisations are looking to further enhance these tools with artificial intelligence and/or machine learning capabilities, which have the potential of providing your organisation with prescriptive and predictive analytics to help identify and action the real opportunities.

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How can Berkeley help?

To successfully implement NRM, organisations must commit to changing fundamentally how they operate. At Berkeley, we help our clients do exactly that. Working by their side, we shape and deliver transformational and lasting change, whether through a short-term project or a much longer commitment. We have helped clients both to define how NRM applies to their organisations and to design, build and deploy high impact NRM IT tools. Please get in touch if you would like to know more.