

# Margin Improvement Best Practices in a Downturn

Illinois Institute of Technology (IIT)  
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## **Price and Margin Improvement: Best Practices in Difficult Economic Times**

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# Introduction: The forgotten component of the profit equation during an economic downturn

- At the onset of an economic downturn, a company's traditional reaction is to focus on controlling costs, retaining their largest customers, and hoping to ride out the storm.
- But Companies that focus on revenue, pricing and overall profitability can survive and even thrive during a recession, but only if they go about it in an effective way



- A *foundational understanding* of the way the business operates, including visibility into transaction-level margin performance is required to make the right decisions
- **Transactional Price Analysis** can help a business address the immediate issues presented during a recession, and position the company for long term, profit growth

## **Five Common Approaches to a Downturn**

- **Focus on Core Competency and Cash Flow**
- **Cut Costs**
- **Downsize Production and People**
- **Keep “Best” Customers**
- **Do What it Takes to Protect Earnings**

What Is The Common Challenge With These Strategies?

## **Enhanced Strategy Through Transactional Analysis**

- **Understand Business Competence**
- **Cut The “Right” Costs**
- **Redeploy Assets to the Drivers of Profitability**
- **Identify Who Your Best Customer Really Are**
- **Establish a Framework for Near Term and Long Term Earnings**

Without transaction level precision, traditional strategies are often ineffective, and can actually destroy short term profits and long term growth



## ■ The Downturn

### A. Identify Low/Negative Margin Business

- Root cause
- Corrective action

### B. The Customer Playbook

- Define Discount Concession Strategy
- Monitor Changing Customer Needs
- Reduce Unwarranted Services Costs

## ■ Don't Forget the Sales Force



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**Uh oh....**

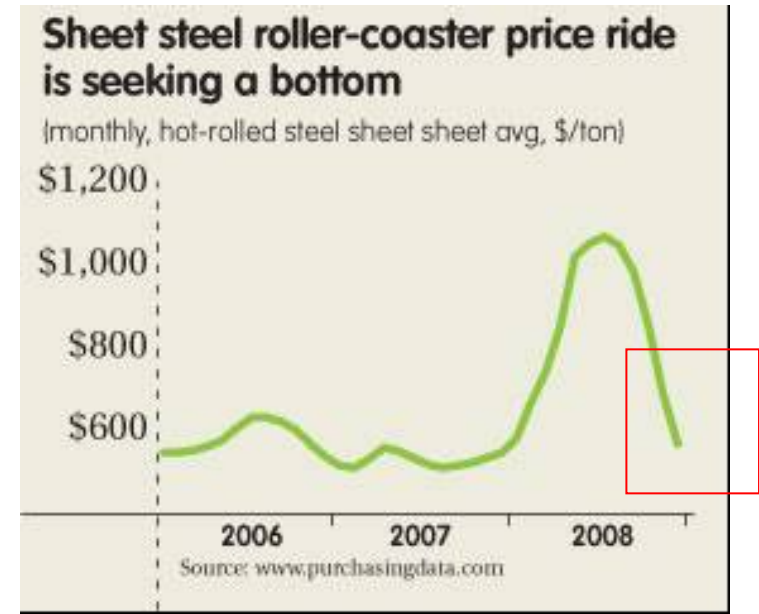
- Volume and revenue down
- Excess capacity
- Downward pricing pressure

**First.....**

- Curtail or slow production
- Postpone expansion
- Cut costs where possible

**But not...**

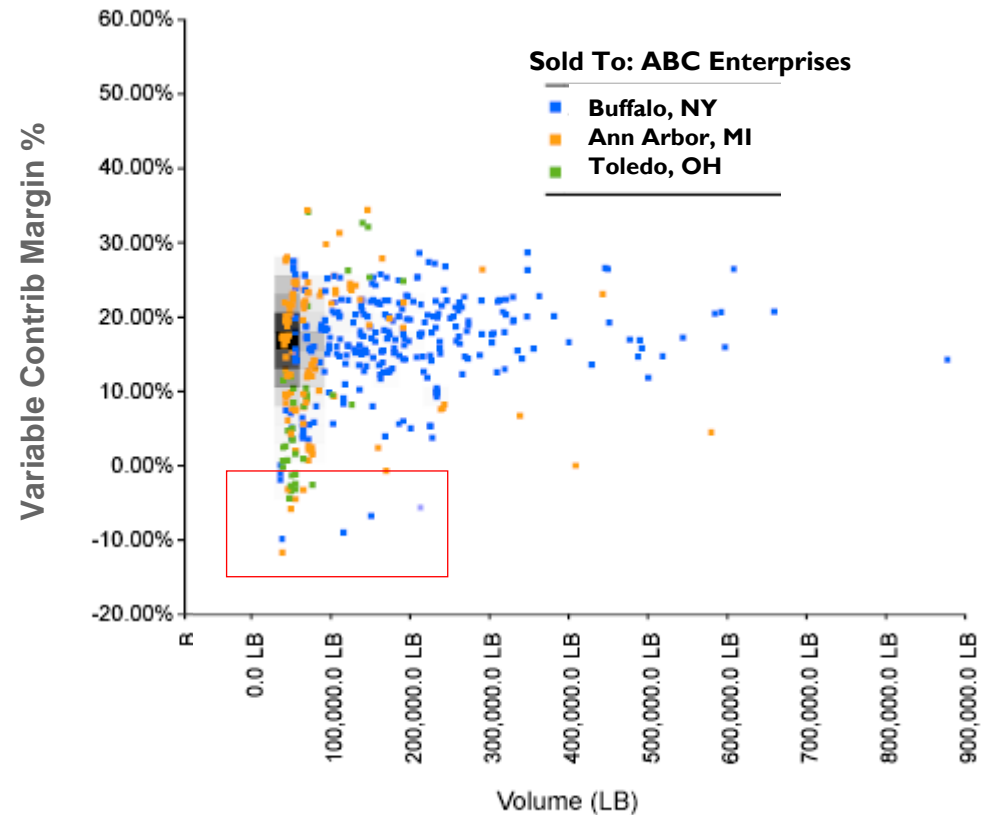
- Across the board price reductions
- To lower prices in an ad-hoc fashion



# Measurement of Customer Profitability is the Key to Successful Navigation during a Downturn



- Need to manage margins at the customer and product level
- Averages drive poor decisions
- Measure performance
  - Not just Averages
  - Measure Customer - Product
  - Measure Product - Ship To





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# Playbook A: Identify your Most Expensive Volume

## Step 1: Identify Low and Negative Margin Business



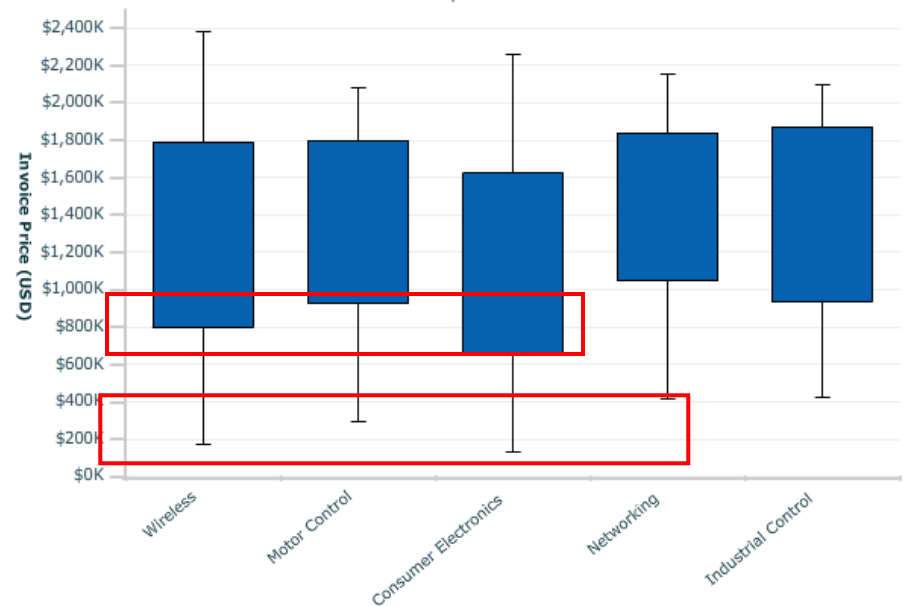
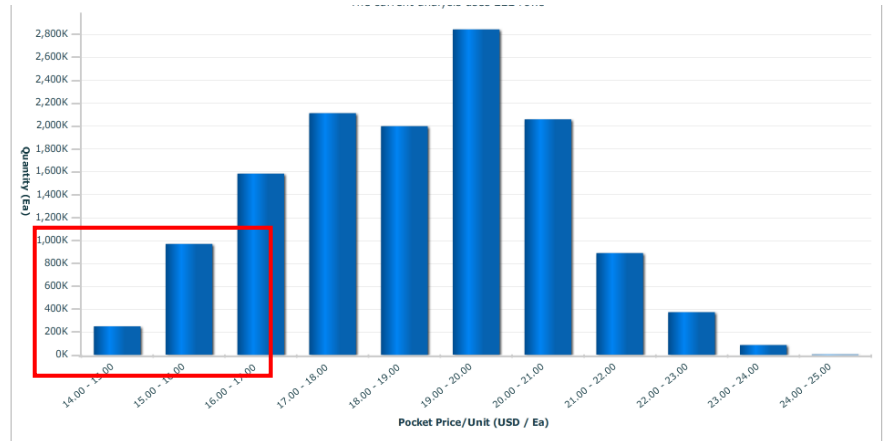
### ■ Define outliers

- What constitutes an outlier?
  - Is it bottom quartile?
  - Pocket Margin < 12%?
  - Revenue < \$1mm and PM % < 12%?

### ■ Identify who they are

- Analytical tool and competency
- Automated if possible

### ■ Now what?



# Playbook A: Identify your Most Expensive Volume

## Step 2: Root Cause Analysis

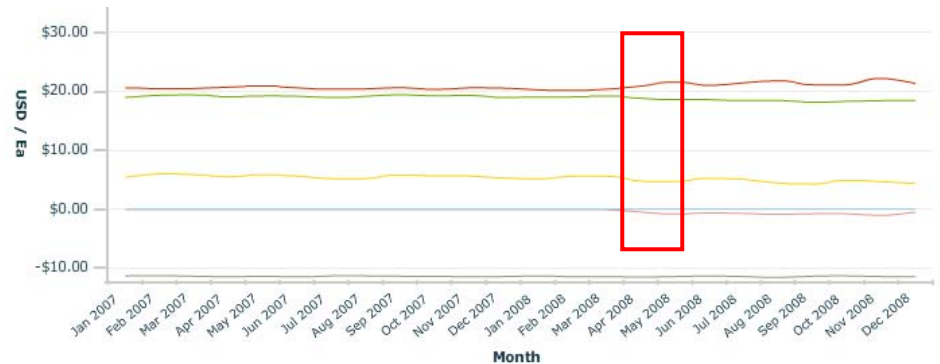
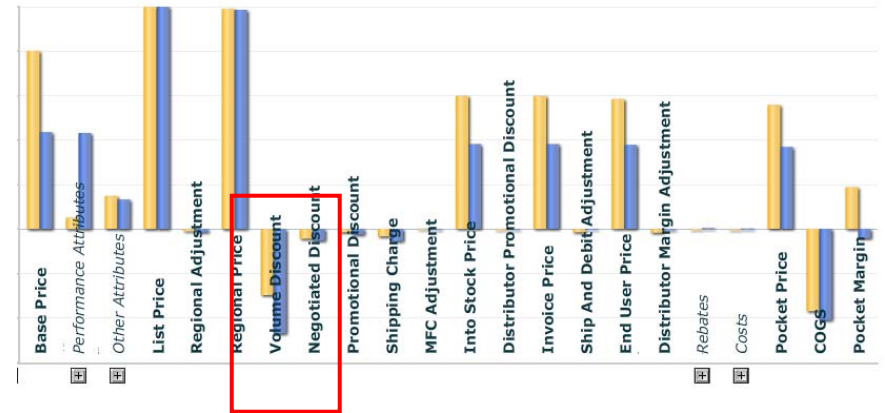


### ■ For Low Margin Customers...

- Compare to peer group
- Identify the cause

### ■ Identify Root Cause(s)

- Low Invoice Price?
- High rebate?
- High fulfillment costs?
- Product issue?
- Ship To Issue?



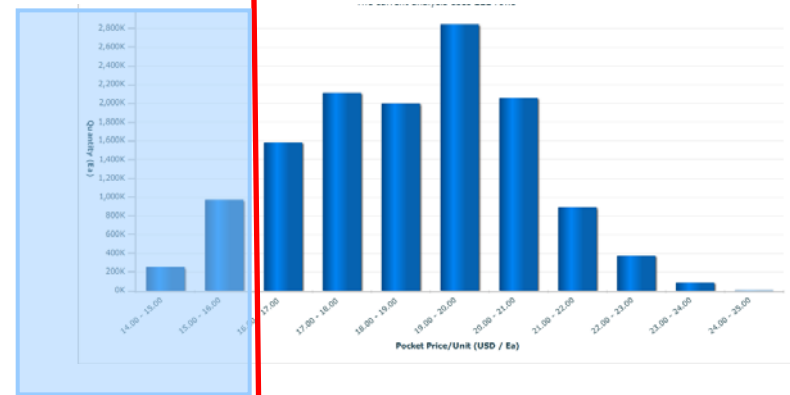
# Playbook A: Identify your Most Expensive Volume

## Step 3: Execute Corrective Action



### ■ Prioritized Action Plan for Each Root Cause

- Low Invoice Price?
  - Increase Price
  - Increase volume
  - Move discount to a volume rebate
- High rebate?
  - Change volume and mix targets
  - Increase Invoice Price
  - Reduce service costs
- High fulfillment costs?
  - Reduce service costs/freight allowance
  - Increase Invoice Price
- Product issue?
- Ship To issue?
  - Address mix within customer
- Exit opportunistically





## ■ The Price Waterfall – Do You Know Yours?

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# Playbook B: The Customer Playbook

## Step 1: The Customer Upgrade Process

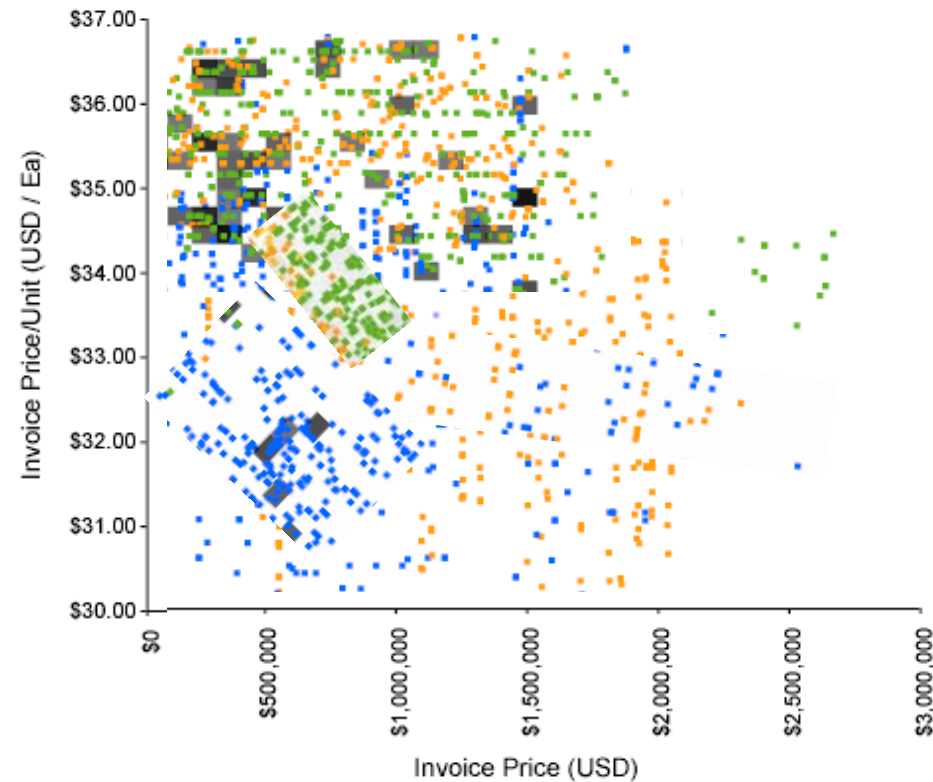


### ■ How do you Rate your customers?

- Define 'best' customers
- Define 'worst' customers

### ■ Can be multi-dimensional

- Volume
- Margins
- Logos
- Geography
- Capacity/Mix

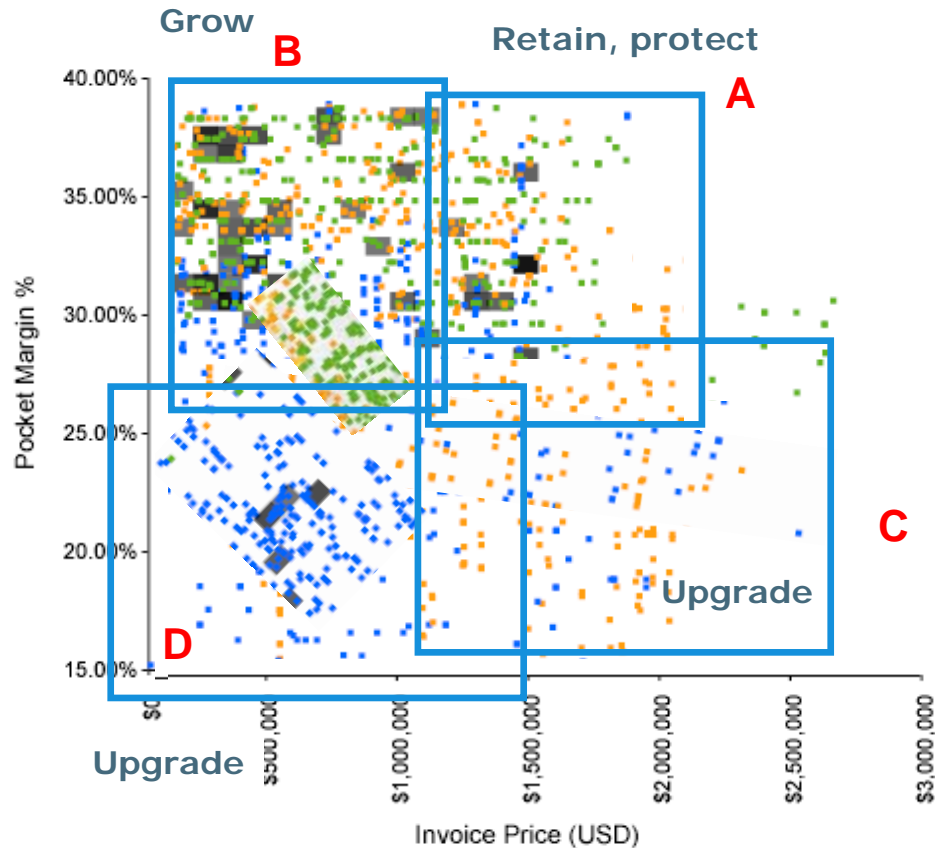


# Playbook B: The Customer Playbook

## Step 2: The Customer Upgrade Process



- Do a simple, actionable segmentation model
- Determine what business you need to keep



# Playbook B: The Customer Playbook

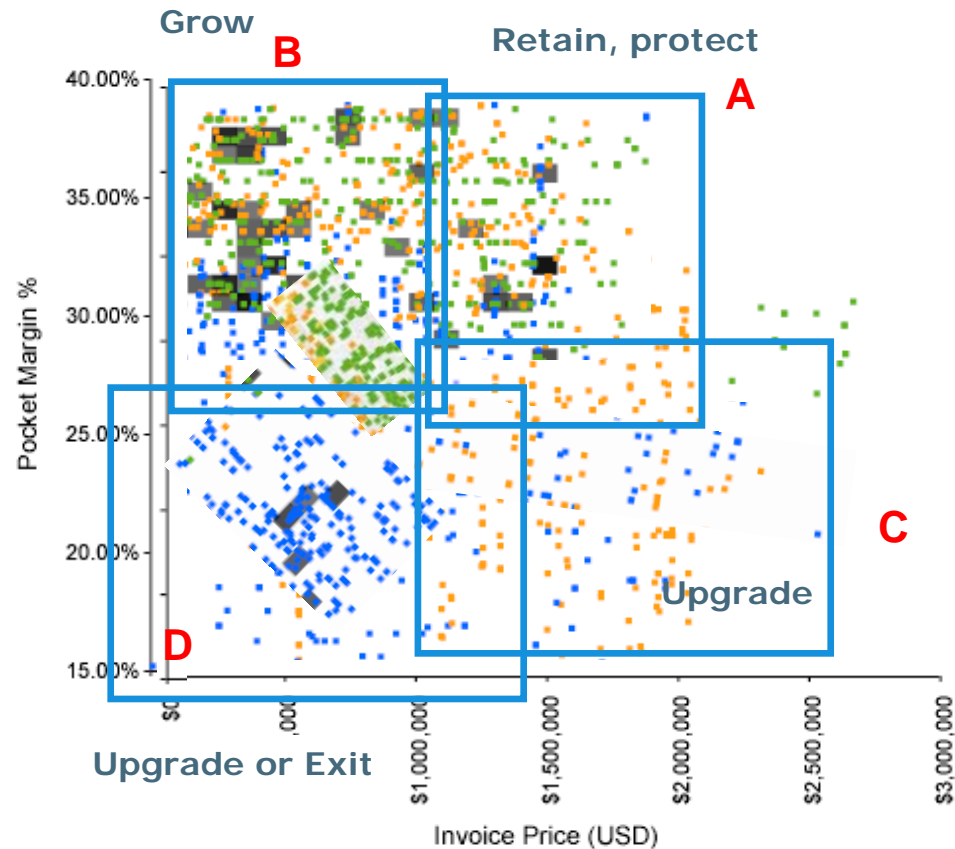
## Step 3: The Customer Upgrade Process



### Define policies to treat A and D differently

- Cost to serve policies
  - E.g. Delivery surcharge
- Pricing policies
  - E.g. Price Increases
- Service policies
  - E.g. Overnight delivery
  - E.g. Special Packaging

How much price erosion will you accept and where will you accept it?



# Playbook B: The Customer Playbook

## Step 5: Define Discount Concession Strategy



How much price erosion will you accept?

*New discount request.....*

### ■ Retain and Protect

- Offer increased service offering
- Position value
- Concede to floor

### ■ Grow

- Offer increased service offering
- Bundles based on value?
- Rebate on mix and volume?
- Service wildcard?

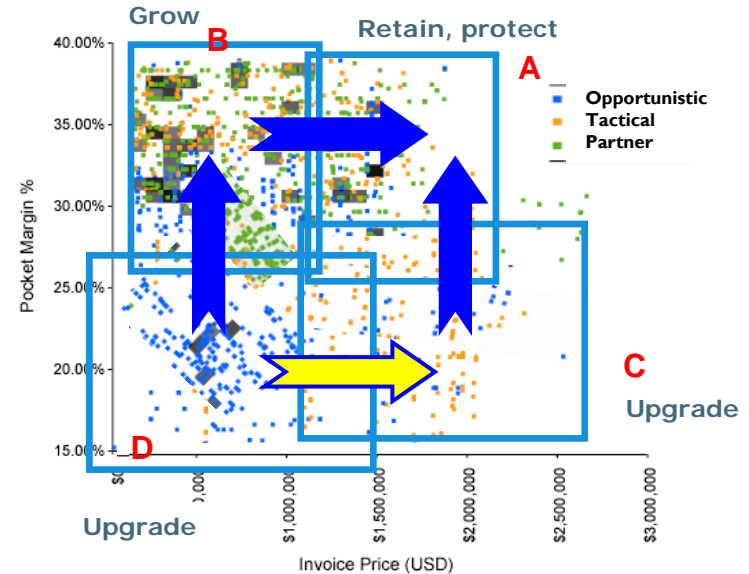
### ■ Upgrade C

- Reduce service costs

### ■ Upgrade D

- Price buyer discount and service package
- No allocation rights?

### ■ Define targets and floors for each segment





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## ■ Last year...

- Price increases killing our customers
- Long backlogs, not much available to sell

## ■ This year...

- Crazy competitors
- Price, price, price

## ■ Chin up: body language matters

- Less likely to defend price in this market, with volume king
- Focus on value! Focus on value!

## ■ Give Sales Targets and Floors – Pay Attention and They Will Too

- Measure and manage

## ■ Track policy enforcement

## ■ Great opportunity: lots of product to sell

- Good opportunity to differentiate yourself



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