FRAMEWORK FOR TRADE PROMOTION OPTIMIZATION

In the super-competitive consumer goods marketplace, profitable trade promotions require the right framework and the right tools.

Exceedra, Europe

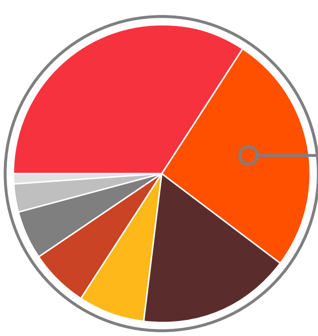
There is no doubt about it. The consumer goods (CG) industry with its complex supply chain, shifting consumer behavior and massive competition is a precarious marketplace. Increasing market share—or protecting the portion you already have—can be tricky business. And with the continuous evolution of the retail landscape, manufacturers have to be at the top of their game to make sure their product ends up in the shopping basket.

Trade promotions have a long-established history in the CG sector. For decades, they have been the modus operandi when manufacturers want to promote a new product, increase demand for an existing one or gain some ground in a specific category. They have also been a fairly effective way to build good relationships with retailers. The manufacturer offers bonuses and allowances for certain products and the retailer reciprocates by rewarding more shelf space or in-store displays, for example. In the end, everyone wins because more product moves off the shelf.

Unfortunately, there's a problem. Despite that fact that trade promotion spend is one of the largest line items on the P&L—generally 20-30 percent of sales revenue and growing—very few promotions result in profit. In fact, most barely break even. Despite this, they seem to be a mandatory element of the CG sales cycle. In other words, they have become a necessary evil. But as the CG marketplace expands and changes, most manufacturers will be scrutinizing their P&Ls. Sooner rather than later, trade promotions are going to have to prove their worth.

The truth is that optimizing the efficiency and effectiveness of trade promotions is a fairly straightforward task. Having the right framework and the right tools will ensure your promotions are meeting their objectives every time.

THE HIGH COST OF TRADE PROMOTION:



+20%

Trade promotion spend is one of the largest line items on the P&L—generally 20-30 percent of sales revenue and growing.

Pre-Promotion Planning

Today, though the economy may be making a comeback, disposable income is still in short supply and there is incredible price transparency across channels.

Before diving into the optimization framework, there is a step that would seem self-evident, but is too often ignored. Structured pre-promotion planning is an essential exercise when thinking about any trade promotion event. This is the strategy session when you set your goals, get to know your shoppers and customers, check out the competition and ensure consistent measurement of promotion success.

Defining the objective of the promotion is the first step. Do you want to win new customers (gain market share)? Turn inconsistent customers into brand loyalists (increase rate of sale)? Or entice steadfast customers to stock their shelves (increase purchase volume)? It is critical that you decide exactly what you want to achieve because that will dictate how you move forward.

Next, you should think about the shoppers—who they are, what they're looking for, how they pick their products, what pressures they are facing. Today, though the economy may be making a comeback, disposable income is still in short supply and there is incredible price transparency across channels. This means price is king and brand loyalty is at risk if your category rival is offering equal value at lower cost. And most shoppers are fickle and will eventually start looking elsewhere for exciting new products if your brand doesn't innovate. For your promotion to succeed, you must focus on meeting the needs of the people buying your products.

Knowing your customers is also key. What is their trading strategy? Can this facilitate your objectives? What will be the cost to meet your goals? You should be sure your customers are in a position to facilitate your strategy efficiently and effectively.

In addition, you will benefit from knowing what your competition is up to. Being aware of marketplace activity and tracking competitive promotions will help you make better decisions. Ask yourself if it would be better to go head to head with competitive products or wait until the category is quiet. And consider your price index threshold. Can you match your competition's price cut without compromising profits? Or should you risk being at the top of a competitive price gap? The answers to these questions will help drive your promotion decision making.

Finally, the consistent measurement of promotion success is paramount. Measuring efficiency and effectiveness in a uniform manner will equip you to evaluate your promotion strategy and ensure that you are achieving the established objective. For many CG companies, formulating ROI Efficiency percentage and ROI Effectiveness percentage are proven methods.

ROI EFFICIENCY % = INCREMENTAL PROFIT / INCREMENTAL PROMOTIONAL SPEND

ROI EFFECTIVENESS % = INCREMENTAL NET REVENUE / INCREMENTAL PROMOTIONAL SPEND

Run the Right Promotion

This is all about choosing the right promotional mechanic—an easy job if you've done your planning homework. There are three elements driving rate of sale—penetration, frequency and weight of sale—and each lends itself to a specific objective. Determining which of these elements you want to drive will help ensure you run the right mechanic.

Penetration: Penetration promotions are best suited to market share capture—winning new customers. Distinguished by trial prices with deep reductions of 33 percent or greater, penetration promotions give shoppers good reason to abandon their competitive loyalties and experiment with something new. This type of promotion is particularly useful when introducing a new product to a category.

EXAMPLE: HALF-PRICE or BOGOF

Frequency: Frequency promotions are a good choice if you want to increase rate of sale—solidify brand loyalty. With price reductions of 20-33 percent, frequency promotions encourage shoppers who occasionally use your product to make it their primary choice and purchase it more often.

EXAMPLE: $2.69 TO $2 PRICE REDUCTION

Weight of Purchase: Weight of purchase promotions are designed to increase weight of sale—incentivize purchases in larger quantities. This promotion gives shoppers two-for-one, extra free pack and other multi-buy offers. The idea is to make sure your customers have a back-up supply on hand so when one box, bottle or can is empty there's another right in the cupboard.

EXAMPLE: 3 FOR THE PRICE OF 2 or 2 FOR $3

Keep in mind, no matter what type of promotion you choose to run, if you want it to succeed you need keep it simple. If a deal requires any effort from your customer—whether it is tricky math or mail-in rebates—you have lost them.

RATE OF SALE EQUATION:

PENETRATION + FREQUENCY + WEIGHT OF PURCHASE = SALES VOLUME

The goal is to make the product highly visible within retail environment so shoppers have multiple opportunities to put it in their shopping basket.

Run the Promotion in the Right Place

Location. Location. Location. Matching the right place to the right promotion can be the difference between profit and loss.

Penetration: Penetration promotions are most successful when they include feature and display support at the store. Gondola ends, extra pallets and front-of-store displays are prime locations to grab shoppers' attention. Additional marketing efforts like television, radio or coupon campaigns are also an important aspect of a penetration promotion. They make shoppers familiar with the product before they get to the store. This way they recognize it when they see it and have less to think about when deciding to buy or not.

Frequency: Similar to penetration promotions, frequency promotions require the product to have various displays and secondary locations within the retail environment. The goal is to make the product highly visible within retail environment so shoppers have multiple opportunities to put it in their shopping basket.

Weight of Purchase: Unlike the first two promotion types, weight of purchase promotions can get the job done using only the product's existing shelf space. The added volume is an unexpected bonus on something the shopper was already prepared to buy. The idea is that shoppers will take advantage of the good deal while it lasts with bigger purchases.

Run the Promotion at the Right Time

Like so many things in life, when it comes to trade promotions, timing is everything. To get the most out of every promotion event, you need to know your business calendar, the calendar of your retailers and you need to think about holidays and seasons. By tying promotions to your business initiatives and those of your retailers, you will support KPIs and have a greater chance of increasing profits. By planning promotions around seasonal events that coincide with your product, you will see greater uplift.

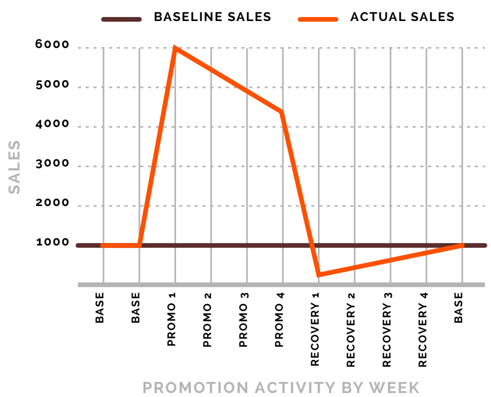
To get the most out of every promotion event, you need to know your business calendar, the calendar of your retailers and you need to think about holidays and seasons.

Run Promotions for the Right Length of Time

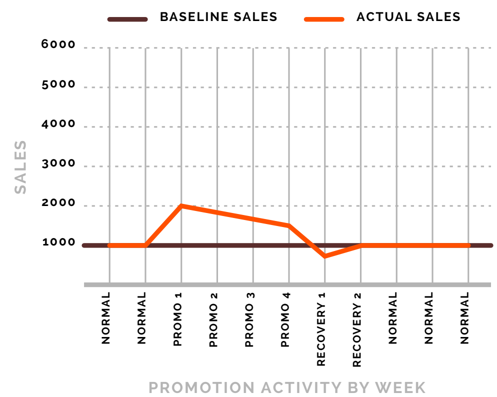
If you are in a quandary about how long is too long, you're not alone. Determining the best length of time is a crucial decision that relies, once again, on the objective of the promotion as well as past promotion performance. The diagram below illustrates how plotting the historical margin, volume and uplift data from similar promotions will help project how promotion length will impact profits.

PROFITABILITY BASED ON PROMOTION LENGTH:

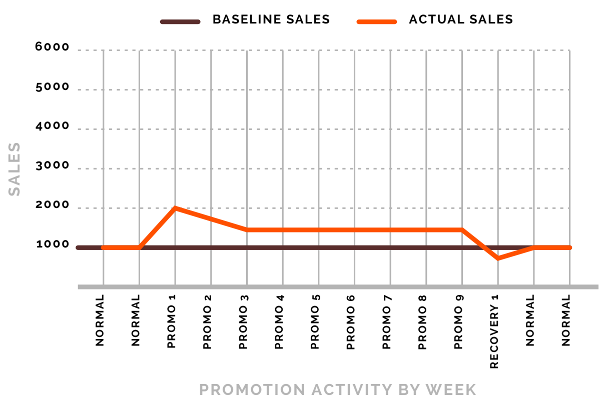
SHORT PROMOTION



MEDIUM PROMOTION



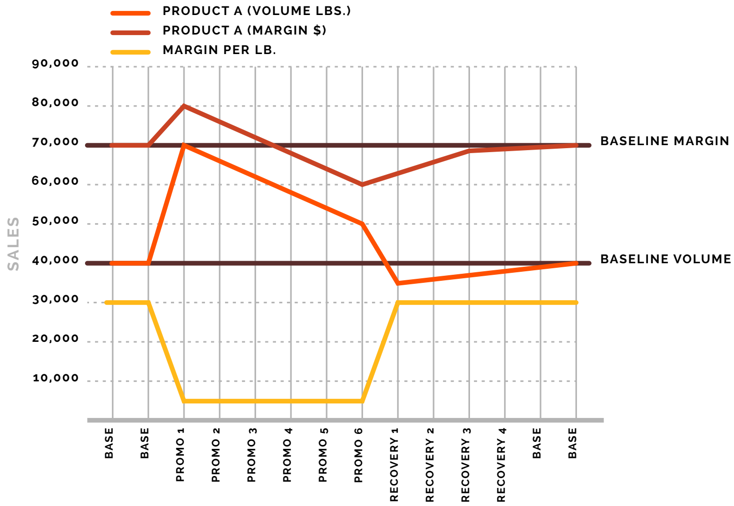
LONG PROMOTION



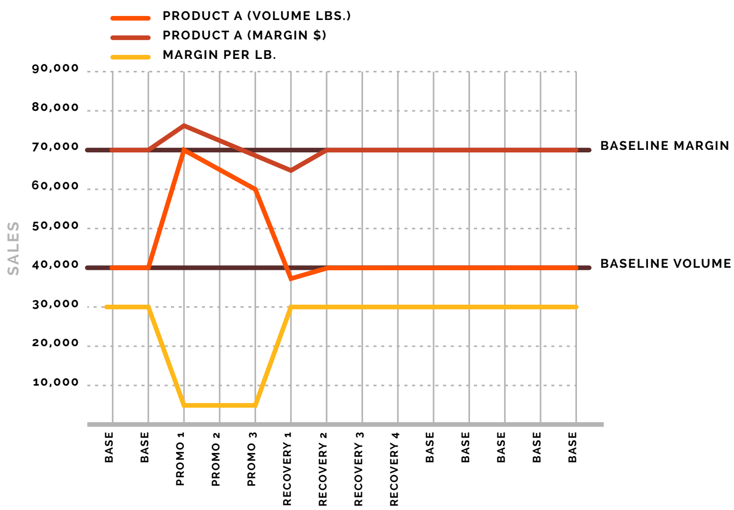
Generally, it is safer to err on the shorter side before margins risk dipping into the negative threatening the bottom line of a promotion. The diagrams below illustrate how shortening a promotion by two weeks can transform overall performance.

TRANSFORMATION BASED ON PROMOTION LENGTH:

BEFORE OPTIMIZATION BY LENGTH



AFTER OPTIMIZATION BY LENGTH



By introducing a new promotion right on the heels of another you are investing trade promotion funds during a time of recovery when margins may not be able to make up for the additional cost.

Short: A 1-3 week timeframe is designed specifically to draw shoppers away from other category products and capture market share. This is a great tactic when introducing a new product. Offering price cuts of up to 50 percent for a short time tends to generate huge initial uplift because shoppers are excited by the deep discounts. However, interest generally wanes quickly and the recovery time tends to be deep and long, sometimes 3-5 weeks.

Medium: A promotion lasting 3-6 weeks is effective for all three promotion types and objectives. Whether you offer discounts, multi-buys or extra volume, a moderate time frame should give you significant initial uplift and an extended period of interest. But, it is important to bear in mind that once the promotion ends, it may take a long time to return to baseline sales volume—perhaps 2-3 weeks. This tactic will impact other category products to a certain degree.

Long: Extended promotions tend to be most effective when frequency or weight of sale is the objective. Promotions lasting 6 weeks or longer usually generate good uplift over a longer period of time then level out with little to no recovery time. Generally, the impact of these promotions on other category products is insignificant.

Find the Right Promotion Balance

Striking the right balance for repeating promotions is every bit as important as choosing the right promotion, place, time and length. By promoting too little, you might be threatening your rate of sale. In essence, by not reminding shoppers to buy your product you are encouraging them to buy someone else's. In the end, this may end up in distribution losses. If you promote too often, shoppers may believe the promotion deal is permanent and feel cheated when price and volume return to business as usual. Now you run the risk of customers forsaking brand loyalty for price loyalty. You should also avoid running promotions back to back even if they are different deals. By introducing a new promotion right on the heels of another—particularly if the first was a deep discount—you are investing trade promotion funds during a time of recovery when margins may not be able to make up for the additional cost.

Finding the right balance is often a case of common sense. But by carefully tracking promotion history, the most effective promotion patterns will become clear.

To get the most impact, you need a tool that will reveal the right promotion parameters based on measurable results.

Sticking to the Rules

Following the rules of promotion optimization is the first step toward more profitable promotions. But guess work and intuition are not enough to show you the best promotion type, place, time, length and frequency. To get the most impact, you need a tool that will reveal the right promotion parameters based on measurable results. Drawing on real industry knowledge, Exceedra has developed a trade promotion management and optimization (TPM/O) solution built specifically on CG best practices and this framework.

Using historical data, the Exceedra solution lets you study the performance of past promotions from various perspectives. This gives you the information you need to run planned promotions through a set of performance scenarios before they are launched. The solution applies the framework of optimization by comparing baseline results of past promotions with those achieved after simple changes to promotion parameters. It is easy to evaluate the mechanics of type, place, time, length and frequency to see how different promotional structures can impact performance. You can measure the effect of attributes like mechanics, feature and display support, promotion timing, length of promotion and frequency to find optimal ROI efficiency and effectiveness. Analyzing the outcomes of various funding models—margin percentage, free goods, profit sharing, off-invoice—will give you insight to negotiate better deals with retailers.

OPTIMIZATION FLAGS:

SKU's	NO
PROMOTION	YES
PLACE	YES
TIME	YES
LENGTH	NO
FREQUENCY	YES

Color-coding and optimization flags make it easy to see which aspects of a promotion achieved optimal efficiency and effectiveness. Hyper-links give access to relevant reports so you know what changes need to be made.

P&L CHART BY WEEK:

	WEEK 1	WEEK 2	WEEK 3
VOLUME (CASES)			
VOLUME (LBS.)			
VOLUME (UPLIFT)			
NET SALES			
NET SALES			
PROFIT			
MARGIN %			
ROI (PROFIT)			
ROI (VOLUME)			

P&L tables by week show you exactly when a promotion moved from positive to negative efficiency so you can avoid negative margins.

IMPACT OF CHANGES:

	BFRE	AFTER	VAR	%
SPEND	$	$	$	%
INCREMENTAL NNSV	$	$	$	%
INCREMENTAL PROFIT	$	$	$	%
ROI (EFFICIENCY)	%	%	%	%
ROI (EFFECTIVE)	%	%	%	%
MARGIN %	%	%	%	%

Easy-to-read tables show you how optimization changes impacted promotion spend, profit, margins and ROI for more accurate promotion projections.

PROMOTIONAL SUMMARIES REPORT:

DEAL CODE	DEPTH	PROMO_STATUS	LENGTH	FORECAST	POST PROMOTION	NET	ROI EFFECTIVENESS	ROI EFFICIENCY	MARGIN %
JM-505	20%	FRONT STORE	5 WKS						
JM-539	20%	GONDOLA END	3 WKS						
JM-550	20%	GONDOLA END	3 WKS						
JM-622	20%	GONDOLA END	4 WKS						
JM-647	50%	GONDOLA END	3 WKS						
JM-649	24%	EVENT	3 WKS						

OPTIMIZATION CHANGES

Promo	Changed JM-539 from 'Half Price' Deal to '$2' Deal
Promo	Changed JM-649 from '$2 or 3 for $5' Deal to $2 Deal
Place	Changed JM-505 from 'Front of Store' Deal to 'Gondola End' Deal
Place	Changed JM-550 from 'Gondola End Gold' Deal to 'Gondola End' Deal
Length	Changed JM-622 from $2 '4 Week' Deal to $2 '3 Week' Deal

Promotion evaluations demonstrate the total impact of changes made to mechanics, attributes and funding so you have the most accurate overall view of promotion optimization.

Sticking to the framework, this comprehensive solution has helped Exceedra's TMP/O customers reduce trade spend by 1-2 percent, improve trade investment ROI by 2-10 percent, increase forecast accuracy and service levels, and decrease inventory levels, bias and accounts receivables. The final result is reduced effort, increased visibility and agility, and enhanced planning and insight. The Exceedra TPM/O solution gives consumer goods companies the proper insight and tools to analyze past promotions in order to fine tune future strategies.

To find our more about trade promotion optimization and how the Exceedra solution can help make your promotions more profitable, contact Michael Creasey at Michael.Creasey@exceedra.com.

About Exceedra

At Exceedra, our mission is to provide Integrated Business Planning Solutions for Consumer Goods companies across the globe to help our clients be more agile in planning and make better business decisions managing their trade budget. Our market leading solutions enable greater control and return on investment for our clients and our service has been recognized as a distinct advantage.

Our solutions support business in the area of Trade Promotions Management and Optimization, Customer Planning, Sales and Operational Planning, Demand Planning, and can be deployed in the Cloud or on premise. We are a global company, based in the UK, with offices in the US and in Australia. For more information, please visit us at **www.exceedra.com**.