

An Enterprise Approach to Maximizing Promotion Effectiveness

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Executive Overview	3
Introduction	4
The Closed-Loop Promotion Planning Cycle.....	5
The Planning Phase.....	6
Collaboration Prevents Disjointed Plans	7
Supply Chain Synchronization Reduces Lost Sales	7
Close the Loop with Sophisticated Analytics	8
Design Promotions that Generate High Returns.....	9
The Execution Phase	10
Increase Sell-in by Offering Retailers More Profitable Promotions ...	10
Respond to Demand with Near Real-Time Monitoring.....	11
Leverage Retailer Point-of-Sale Data.....	11
Resolve Problems with Exception Management Tools	12
The Analysis Phase.....	12
Define the Right Effectiveness Metrics.....	12
Measure the Complex Impact of Promotions.....	13
Baseline Versus Lift	14
Cannibalization	15
Halo Effects	15
Prepromotion and Postpromotion Effects	15
Consumer Delayed Purchasing and Pantry Loading.....	15
Retailer Delayed Purchasing and Forward Buying.....	16
Diverting.....	16
Net Lift	16
Competitive Brand Switching Versus Category Growth.....	16
Example Net Lift Analysis	16
Harness the Power of On-the-Fly Analytics.....	18
Elasticity of Consumption	18
Conditioning of Consumer Response.....	19
Account-Level Profitability.....	19
Conclusion.....	20

An Enterprise Approach to Maximizing Promotion Effectiveness

Once a promotion goes into effect, real-time retail sales data should be monitored so plans can be updated and potential problems can be addressed. Once promotions are completed, their true effectiveness should be quantified. The resulting knowledge should be fed back into the planning process using predictive modeling tools. This way, marketers can learn from past experience and focus on those promotions that yield the greatest return on investment.

EXECUTIVE OVERVIEW

Spending on consumer and trade promotions by consumer goods manufacturers and retailers has grown steadily over the past two decades and now consumes the lion's share of their marketing budgets. Not surprisingly, consumer goods companies are increasingly attempting to measure and maximize the effectiveness and return on investment (ROI) of their promotional spending.

To do this, consumer goods companies are replacing simple spreadsheets with sophisticated new software packages that arm marketing and sales professionals with advanced planning and analytical capabilities. Such packages typically fall into one of two categories. In the first category is promotion management software, either standalone or modules of larger customer relationship management (CRM) and enterprise resource planning (ERP) suites. Although these applications automate promotions planning from a sales and marketing perspective, they offer very limited analytical capabilities and lack integration with supply chain systems. Applications in the second category, marketing analytics software, offer powerful analytical capabilities but are typically desktop or departmental systems for market research power users. They lack the enterprise collaboration and workflow capabilities needed to tie analytics into day-to-day marketing, sales, and supply chain planning.

To optimize promotion effectiveness at the enterprise level, consumer goods companies need to involve multiple departments and consider how promotions affect their overall business. A promotion that generates a large lift on a particular product, at a particular account, might appear quite effective to an account manager trying to meet a monthly volume quota. However such a promotion is not necessarily effective or profitable from an enterprise perspective. It might generate short-term results at the expense of long-term brand and corporate strategies. The lift might come at the expense of volume from other products, other accounts, and other time periods. Such a promotion might incur hidden supply chain costs, which erode corporate profitability.

Organizations must plan promotions collaboratively among brand management, marketing, sales, and external partners in a way that links tactical plans with strategic objectives. Supply chain operations must also be included in the planning

process so that supply matches demand. Once a promotion goes into effect, real-time retail sales data should be monitored so plans can be updated and potential problems can be addressed. Once promotions are completed, their true effectiveness should be quantified. The resulting knowledge should be fed back into the planning process using predictive modeling tools. This way, marketers can learn from past experience and focus on those promotions that yield the greatest return on investment.

INTRODUCTION

There is a growing industry consensus that consumer goods companies are not getting a good return on investment from their promotions dollars and that improving promotion effectiveness should be a priority.

Over the past two decades, a number of forces have compelled consumer goods manufacturers to increase spending on consumer and trade promotions. These forces include the growing negotiating power of retailers, the perceived commoditization of brands in many product categories, and concern over the potential reduction in advertising effectiveness resulting from media proliferation and “advertising clutter.” As a result, according to a widely referenced Accenture study, U.S. consumer packaged goods (CPG) manufacturers have doubled promotions spending from 9 percent of sales in 1978 to 19 percent in 2000, making promotions the second largest profit-and-loss item after cost of goods sold.¹ Not surprisingly, the effectiveness of consumer and trade promotions in the consumer goods industry has come under increased scrutiny in recent years as the amount of money spent on promotions has increased.

As a result of this increased scrutiny, there is a growing industry consensus that consumer goods companies are not getting a good return on investment from their promotions dollars and that improving promotion effectiveness should be a priority. In a survey conducted by Cannondale Associates, only 16 percent of manufacturers reported obtaining good value from their trade promotions spending.² In the same study, 92 percent of these manufacturers listed trade promotion inefficiency as an “extremely/very important” issue, second only to retail execution among a wide variety of issues facing consumer goods manufacturers.

The Accenture study referred to above also pointed out that improving promotion effectiveness is not simply a marketing and sales issue. The study reported:

Inefficiency causes excess hidden costs of up to US\$5.8 billion (in addition to the US\$25 billion spent on trade promotions in the grocery channel), fully 70 percent to 80 percent of it attributable to supply chain volatility (surge) and uncertainty.³

A recent AMR Research report reached a similar conclusion: “. . . synchronizing internal sales and marketing initiatives with demand management and supply chain

¹ “The Daunting Dilemma of Trade Promotion,” Accenture, 2001.

² “Trade Promotion Spending & Merchandising Industry Study,” Cannondale Associates, 2002.

³ “The Daunting Dilemma of Trade Promotion,” Accenture, 2001.

processes will reduce supply chain costs by as much as 15 percent.”⁴ The implication is that to optimize ROI on promotions, organizations must take an enterprise approach to measuring and improving promotion performance. They must extend their efforts beyond sales and marketing departments to include supply chain operations.

The potential payback from increasing promotion effectiveness is enormous. The Accenture study concluded that with a more intelligent approach to trade promotions, “. . . manufacturers could see return on sales increase by as much as 40 percent.”⁵ U.S. consumer packaged goods manufacturers account for about \$500 billion in sales and generate about \$50 billion in profits. Applying the 40 percent figure yields an additional \$20 billion in profits that could be generated by more effective promotions management. This figure addresses just trade promotions in the U.S. consumer packaged goods industry. While the precise numbers can be debated, few would disagree that the overall opportunity is huge.

Recent changes to Financial Accounting Standards Board (FASB) rules governing the accounting treatment of promotion spending have provided additional impetus to measure and improve promotion effectiveness. Promotion dollars that were once treated as expenses are now being deducted from revenues. The new rules affect neither cash flow nor accounting profit. But to the extent that companies run promotions to increase accounting revenue, the new rules will force companies to reconsider promotion tactics for which the impact on revenues has been neutralized.

The rationale for rethinking and redesigning trade promotion processes has never been greater. Today’s informal and disjointed processes are resulting in too much money spent for too little return. Consumer goods companies that embrace a new enterprise approach to maximizing promotion effectiveness will increase profits and gain competitive advantage.

THE CLOSED-LOOP PROMOTION PLANNING CYCLE

Effective promotions management requires a comprehensive and closed-loop approach throughout the promotion planning cycle, which consists of three overall phases:

- Prepromotion planning
- Execution
- Postpromotion analysis

⁴ “Count the Money When Sales and Marketing Work with Logistics,” AMR Research, 2001.

⁵ “The Daunting Dilemma of Trade Promotion,” Accenture, 2001.

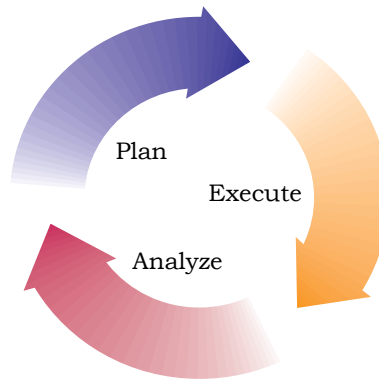


Figure 1: The closed-loop promotion planning cycle.

Within each phase, processes should be synchronized across the enterprise and with external partners. As illustrated in Figure 1 above, the overall process must be closed-loop. Postpromotion analysis must be tied into planning future promotions so that marketers can incorporate past experience in making future promotion plans.

THE PLANNING PHASE

Promotion planning involves establishing promotion goals and budgets and then specifying a schedule of promotion events to achieve those goals. In consumer goods manufacturing companies, planning takes place at multiple levels, from the strategic to the tactical, from broad guidelines at the brand, annual, and nationwide level to the level of specific deals on certain SKUs at specific accounts during precise time frames.

Unfortunately, promotions are often planned in a disjointed fashion and as a result are inefficient and ineffective. A number of problems are common, as illustrated in Table 1 below.

Common Problems	Possible Symptoms
Promotion tactics are not aligned with brand strategies	Promotions maximize current period account tonnage at expense of long-term price image, loyalty, and profitability
Promotion plans and supply chain plans are not coordinated	Out-of-stocks, overstocks, and high costs for expedited distribution erode promotion profits
Data on past promotion performance is not readily available or usable during the promotion planning process	Many promotions are unprofitable

Table 1: Common problems and possible symptoms of promotions.

Enterprise planning software can help overcome these problems by offering collaboration capabilities to align tactics with strategies and to synchronize promotion planning with supply chain planning. Tools to automate data analysis and predictive modeling can help tie past promotion performance into the planning process.

Collaboration Prevents Disjointed Plans

To plan promotions properly, consumer goods companies need software operating on a shared database and incorporating workflow, business rules, role security, and exception management capabilities. At the same time, such a system must accommodate various users having different priorities and operating with different constraints, data, metrics, and levels of granularity.

If consumer goods organizations use any software to facilitate their promotion planning processes, they typically use desktop spreadsheet applications. While providing a flexible and familiar user interface to schedule promotions, track budgets, and view performance to plan, such software creates a chaos of conflicting data and disjointed plans. To plan promotions properly, consumer goods companies need software operating on a shared database and incorporating workflow, business rules, role security, and exception management capabilities. At the same time, such a system must accommodate various users having different priorities and operating with different constraints, data, metrics, and levels of granularity.

Following is a hypothetical scenario for how promotions might be planned using collaborative planning software capabilities. This particular process is high level and is for illustrative purposes only, rather than an endorsement of a particular approach to planning promotions.

1. Brand manager establishes overall promotion guidelines: annual spending, revenue, volume, and profit targets for a brand; maximum temporary price reduction allowance per case in order to maintain price image of brand; and number of promotions per year that can be run.
2. Vice president of sales allocates target figures set by brand manager to each account.
3. Trade marketing manager creates specific promotion plans detailing product groups and promotion types by month and region. Plans are designed to maximize profits while meeting revenue and volume targets.
4. Account managers and individual accounts negotiate specific deals including details on timing, SKUs, and promotion elements. Plans are designed to maximize account profitability while meeting revenue and volume targets.

Using software with advanced collaboration capabilities, consumer goods companies can enable complex workflows like that outlined above and maximize promotion effectiveness by balancing the priorities across departments and users. The same software features can be used to collaborate with external partners such as customers, wholesalers, suppliers, and sales agencies.

Supply Chain Synchronization Reduces Lost Sales

The planning example above focuses on collaboration in a sales and marketing context. It is also critical to include supply chain operations in the promotion

planning process. Promotions cause great volatility in consumer demand, stressing even the most responsive supply chains. According to a 2002 report published by the Grocery Manufacturers of America (GMA), promoted products in the top 25 grocery categories are nearly twice as likely (13.1 percent of SKUs) to be out of stock at the retail shelf than nonpromoted items (7.4 percent).⁶ Such stock-outs lead to lost sales and wasted promotion dollars. Consumer goods manufacturers go to great lengths to avoid such stock-outs by increasing safety stock levels and expediting distribution. These activities lead to the hidden supply chain costs referenced earlier.

Lost sales and incremental supply chain costs result from a disconnect between marketing and supply chain operations. To minimize these effects and improve promotion ROI, sales and marketing departments must plan promotions with visibility to supply chain constraints. Supply chain departments must plan supply with visibility to promotion plans and their impact on demand. Synchronization among departments requires sharing a common view of demand, aligning planning processes, using compatible information technology (IT) systems, and breaking down organizational and cultural barriers.

Close the Loop with Sophisticated Analytics

Most consumer goods companies have extensive data on past promotion performance. CPG companies, in particular, typically have comprehensive syndicated retail sales data from ACNielsen or IRI, detailing weekly sales and merchandising activity by account, both for their and their competitors' products. This data, however, whether internal or syndicated, is not fully leveraged in the promotions planning process. Problems include

- Syndicated data is limited to raw product-movement information, and it is not readily accessible outside the marketing research department. Marketing and sales managers can request custom analyses from marketing research. But marketing research resources are limited and turnaround time can be considerable.
- Raw product-movement data is made widely available in electronic form, but users lack analytical tools to make sense of the data. Promotion lift cannot be distinguished from the impact of other causal factors such as weather, seasonality, and competitive activity. Quantifying effects such as cannibalization, halo, pantry loading, and forward buying is impossible.
- More sophisticated analysis can be obtained from syndicated data providers and consultants, but the cost is prohibitively high because of the custom software development and professional services required.

By automating the analytics process with software, analyses that might otherwise take days can be done “on the fly” as often as needed. Rather than having to

⁶ “Full-Shelf Satisfaction—Reducing Out-of-Stocks in the Grocery Channel,” Grocery Manufacturers of America, 2002.

submit requests to the marketing research department, managers can perform their own analyses as they need them, leaving marketing research to focus on the most strategic issues. With flexible modeling capabilities, marketing and sales users can focus on particular products, accounts, promotions, and time periods as appropriate. For example, a brand manager might want to look at the nationwide market share impact of trade promotions versus consumer promotions for a brand over the course of a year. On the opposite end of the granularity spectrum, an account manager might be interested in looking at the effectiveness with respect to case volume of a 20 percent temporary price reduction (TPR) on a specific set of SKUs at a particular account.

A key challenge in predictive modeling is avoiding “over-fit.” Many postpromotion analysis tools appear to do a very good job of explaining past data but break down when used to forecast the future. This problem results from confusing the noise inherent in retail sales data with real cause and effect.

Design Promotions that Generate High Returns

Analyzing past promotion effectiveness has some value for getting a general sense for what works and what doesn't. Marketing and sales professionals can observe how a particular promotion did in the past and feel comfortable that the exact same promotion will perform similarly in the future under the exact same conditions. But conditions change, and no two promotions are exactly the same. To accurately predict the impact of specific promotions under unique conditions, consumer goods companies need predictive modeling tools. With such tools, they can simulate the impact of hypothetical promotions and design promotions that generate the highest returns.

A key challenge in predictive modeling is avoiding “over-fit.” Many postpromotion analysis tools appear to do a very good job of explaining past data but break down when used to forecast the future. This problem results from confusing the noise inherent in retail sales data with real cause and effect. To properly model the complex retail environment, advanced stochastic (based on random trials) techniques are required to distinguish noise from cause and effect and to determine which of the dozens of possible causal factors drive demand. Figure 2 below highlights features of the Bayesian and Markov hybrid modeling used in Oracle's Demantra planning solutions. With predictive modeling tools, marketers can simulate various promotion tactics and strategies. They can then optimize promotion plans to maximize volume, revenue, profit, or whatever metric they are targeting.

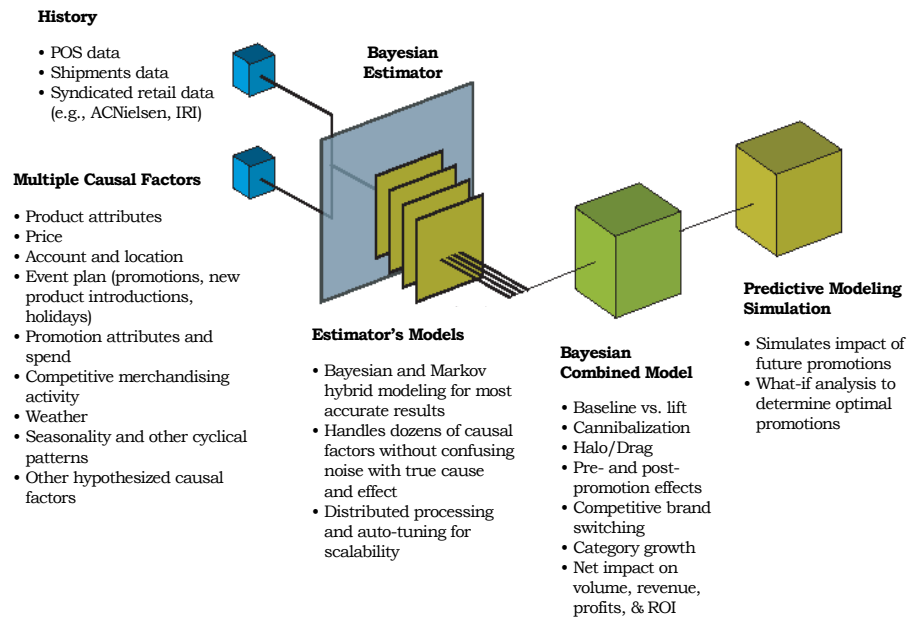


Figure 2: A comprehensive approach to analytics and predictive modeling.

THE EXECUTION PHASE

Promotion plans are only as good as their execution. Two issues are paramount in executing promotions. For trade promotions, a critical issue is whether retailers buy into a deal and use the promotion dollars as intended. For both consumer and trade promotion dollars, it is critical that the supply chain can actually deliver on the increased demand in a timely and profitable way.

Increase Sell-in by Offering Retailers More Profitable Promotions

Manufacturers are growing increasingly concerned that retailers are not fully executing trade promotions, at the expense of manufacturers' strategic marketing goals. Driving this trend is an increasing awareness among retailers that a promotion that might be good for a manufacturer is not necessarily good for a retailer. In fact, some analytics vendors focused on the retail sector are explicitly selling their capabilities to help retailers decide when to pass through promotion dollars and when to retain funds instead.

Analyzing promotion effectiveness allows manufacturers to design promotions that are more attractive to retailers and to communicate the resulting benefits to retailers. By offering retailers more profitable promotions, manufacturers can improve sell-in and increase the overall return on their promotion budgets. Manufacturers increase product sales through a mix of gaining share from competitors (getting a bigger piece of the pie) and driving incremental category volume (making the pie bigger). While both sources of lift are attractive to manufacturers, retailers much prefer the latter. A retailer has limited motivation to put up with the operational headaches of executing a promotion merely to shift volume from one manufacturer to another, unless the increase in overall consumer

traffic attributable to the promotion offsets execution costs. But if a promotion increases category volume, both the retailer and manufacturer benefit. Designing promotions that stimulate category growth, and sharing that supporting data with retailers, can thus help sell-in and increase pass-through rates.

Shape modeling assigns an overall demand curve shape based on past similar promotions. This allows a revised forecast for total promotion period demand to be accurately predicted based on just a day or two of POS data. With this near real-time intelligence, manufacturers and retailers can respond as soon as possible to unanticipated levels of demand.

Respond to Demand with Near Real-Time Monitoring

While sophisticating modeling techniques can significantly improve forecasts of promotional lift, there's always an unpredictable element to promotion demand. Variations in retail execution compound the problem. With stock-outs on promoted items twice the level for nonpromoted products, clearly there is an opportunity to improve sales of promoted product simply by making sure product is on the shelf. The alternative is lost sales and dissatisfied customers whose loyalties might go elsewhere.

To maximize the effectiveness of promotions, it is critical that manufacturers and retailers work together to monitor product movement in near real-time and respond to unexpected levels of demand. Options for responding include increasing or decreasing the duration of a promotion and shifting replenishment plans to better meet demand.

Leverage Retailer Point-of-Sale Data

The increasing availability of daily retail point-of-sale (POS) data is enabling near real-time visibility to consumer demand. With POS data from the first 24 to 48 hours of a promotion, retailers and manufacturers can much more accurately forecast promotion demand and refine plans accordingly.

Analyzing POS data properly and revising volume forecasts require special tools. POS data is notoriously messy as the result of mis-polling, mis-scanning, antiquated IT systems, and other factors. To interpret POS data correctly and avoid mistaking noise for real shifts in demand, data must be carefully cleansed.

Once clean POS data is available, revising promotion lift forecasts requires techniques like shape modeling. Shape modeling assigns an overall demand curve shape based on past similar promotions. This allows a revised forecast for total promotion period demand to be accurately predicted based on just a day or two of POS data. With this near real-time intelligence, manufacturers and retailers can respond as soon as possible to unanticipated levels of demand. Figure 3 below illustrates this concept.

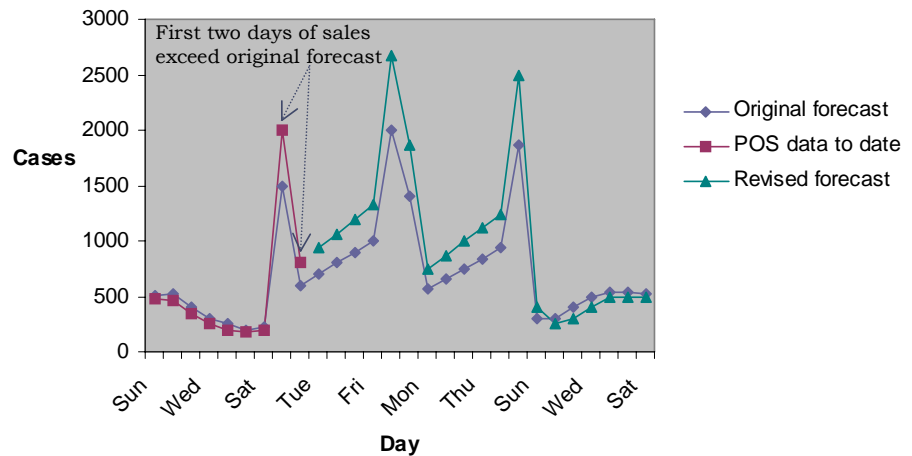


Figure 3: Near real-time forecast revision for a two-week promotion, Sunday to Saturday.

Resolve Problems with Exception Management Tools

Once POS data is analyzed and demand forecasts are revised, exception management and workflow tools play a critical role in quickly resolving problems. Exception management tools are needed to pinpoint problem areas from the potentially overwhelming streams of POS data. Efficient workflow software is critical in bringing together marketing, sales, supply chain operations, retailers, manufacturers, wholesalers, and sales agencies to respond to these potential problems.

External partners play a particularly important role in monitoring promotion performance and resolving issues. Including them in the process requires software specifically designed for remote, occasional users. User interfaces must be intuitive. Software must be thin client to minimize client support. It must also support the mobile devices used by field personnel, who can extend visibility and response capability to the retail shelf.

THE ANALYSIS PHASE

Define the Right Effectiveness Metrics

Before discussing the best way to analyze promotions performance, it is worth clarifying the meaning of effectiveness. The answer is not obvious, because promotions are often executed to achieve a wide variety of objectives, ranging from the tactical (such as moving excess stock or meeting this quarter's tonnage quota at an account) to the more strategic (such as generating trial or increasing brand share).

Today, few firms rigorously measure promotion effectiveness, let alone capture the data necessary to do so. As part of implementing software to measure and improve promotion effectiveness, consumer goods companies must determine which metrics they want to measure. Sophisticated enterprise software with workflow and

role security features gives consumer goods companies the luxury of rethinking the way they evaluate marketing performance, using a variety of metrics at the corporate, department, and individual levels. Companies can ask questions such as

- Should a promotion be considered effective if the lift it generates cannibalizes other product sales, or results in reduced volume in the future?
- Should account executives be measured on tonnage, revenue, profit, or other metrics?
- Should a promotion be considered effective if the incremental profits are offset by expedited distribution costs incurred to meet demand?

Measuring effectiveness requires quantifying the sources of lift resulting from complex interrelationships among products and accounts across time—phenomena like cannibalization, pantry loading, forward buying, and other effects that marketers intuitively know occur, but cannot easily quantify.

Once companies have defined the appropriate metrics and established targets for these metrics, they can determine whether the targets have been met and then measure the incremental benefit for each dollar of promotional spend. If case volume is a metric, then companies can also measure incremental cases generated per dollar of expense. If profit is a metric, incremental profit per dollar of expense can also be measured.

Measuring the ROI of promotional and other marketing spending is a hot topic in a number of industries. The metric of incremental profit per dollar of expense, mentioned above, is often used as a measure of ROI and results in a very useful “bang-for-the-buck” figure that can be used to compare the effectiveness of different promotions and maximize profitability. While this measure of ROI is technically not ROI from a financial perspective—and should not be compared with a corporation’s hurdle rate—it is nevertheless a good practical measure for evaluating promotion effectiveness.

Measure the Complex Impact of Promotions

The hardest part of measuring effectiveness is determining a promotion’s real impact on demand. Once companies understand the true impact on demand, calculating effectiveness is just a matter of arithmetic. Measuring true impact, on the other hand, requires powerful analytical techniques to make sense of huge streams of sales and causal data. The noisy nature of retail data complicates the task.

The first step is to separate lift from baseline volume. Syndicated market data and internal demand planning systems often break down volume data into baseline and lift. Many promotion management and customer relationship management (CRM) systems provide visibility to such data and stop there. But measuring effectiveness requires going a step further and quantifying the sources of lift resulting from complex interrelationships among products and accounts across time—phenomena like cannibalization, pantry loading, forward buying, and other effects that marketers intuitively know occur, but cannot easily quantify. Such phenomena can offset promotion lift and turn what appears to be a profitable promotion into a money loser.

Figure 4 below illustrates the three dimensions along which these interrelationships occur: products, accounts, and time—or the “influence range.” A promotion on Product A at Account A at Time zero on the chart affects demand of other product-account combinations throughout the three-dimensional Influence Range. Interaction among products results in product cannibalization, competitive brand switching, and halo effect. Interaction across accounts results in account cannibalization. Interaction across time leads to prepromotion and postpromotion effects, such as pantry loading.

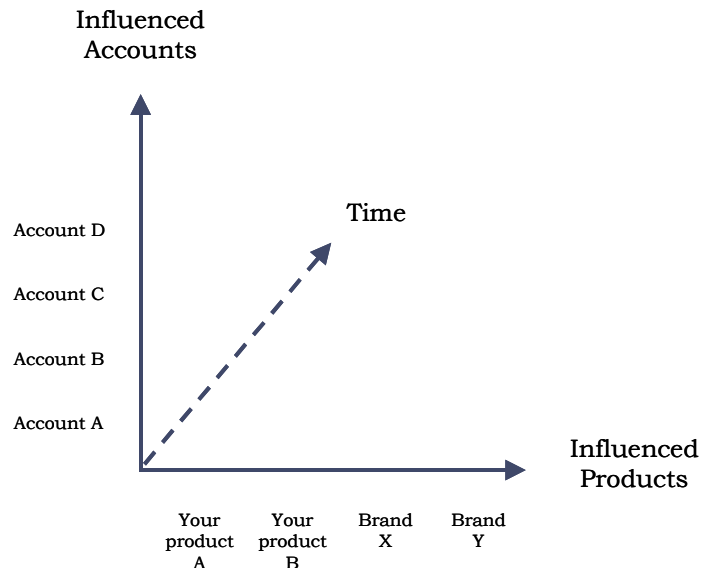


Figure 4: Complex demand interactions across products, accounts, and time.

Baseline Versus Lift

Before analyzing the components of lift, companies must first separate out promotion lift from baseline sales—the latter an estimate of what would have sold had the promotion not taken place. While baseline and lift data are commonly available, they should be validated. If changes to baseline volume are confused with lift, assessments of promotion impact will be erroneous. Sophisticated analytics are required to examine all the potential causal factors that could affect baseline volume, such as base price changes, weather, holidays, new product introductions, changes in distribution, competitive activity, seasonality, and other cyclical variations.

Special attention must be paid to avoid mistaking prepromotion and postpromotion effects with changes to baseline volume. Promotions often cause significant decreases in volume both before and after the actual promotion period. Simplistic analytical techniques that determine baseline volume by simply removing volume during promotion periods and smoothing out the remaining volume data will underestimate baseline demand and thus overestimate lift.

Cannibalization wastes promotion spending by simply shifting volume from one set of products to another while reducing margins, as full margin business is replaced with business at a discount.

Cannibalization

Product cannibalization—every brand manager, promotion manager, and account executive knows intuitively that promoting one SKU or group of SKUs often cannibalizes a company's similar products (for example, different sizes, flavors, packaging, forms of the promoted product, or even the company's other brands in the same category or related categories). Cannibalization wastes promotion spending by simply shifting volume from one set of products to another while reducing margins, as full margin business is replaced with business at a discount. But such cannibalization is not easy to measure given the potentially huge number of affected products and all the other factors that affect demand.

Account cannibalization—just as promoting one product can cannibalize the sales of others, promotions executed at one account can cannibalize sales at other accounts, even across channels (grocery, drug, mass merchandise, and so on). If account cannibalization were easier to measure, sales management could alter current incentive systems for sales representatives, which typically focus on sales for their accounts regardless of cannibalization of other accounts.

Halo Effects

The opposite of cannibalization is the halo effect, also called drag, in which promotion of one product has a positive rather than negative effect on the sales of other products. While relevant to manufacturers that make complementary products (for example, tortilla chips and salsa), it is of greatest interest to retailers, for whom the major objective of promotions is to drive store traffic and overall sales. As retailers often promote products at a loss (loss leaders) to drive traffic, clearly any measurement of the effectiveness of retail promotion must at minimum measure halo effects.

Prepromotion and Postpromotion Effects

Compounding the analytical challenge of measuring promotion impact is the fact that the impact is not limited to the duration of the promotion activity. Some promotions produce benefits beyond the promotion period. In other cases, promotions reduce volume both before and after the promotion period. These delayed purchasing and stockpiling effects can take place at both the consumer level and the account level.

Consumer Delayed Purchasing and Pantry Loading

Consumers will often stock up on nonperishable sale items, a phenomenon often called pantry loading. They might also delay purchasing until a product goes on promotion if they know that promotions are offered on a regular basis. If delayed purchasing and pantry loading are taking place, then the apparent lift during a promotion can be exaggerated. Some of the apparent lift represents a shift of demand in time rather than a real increase. As with cannibalization, there is also a shift from regular margin sales before and after the promotion to low margin sales during the promotion.

Retailer Delayed Purchasing and Forward Buying

Retailers exhibit the same behavior as consumers, delaying purchases in anticipation of upcoming deals, and then taking advantage of price breaks by buying (forward buying) huge quantities of product, well beyond what they plan to sell during the promotion period. Again, these sales result in low margin sales today at the expense of higher margins purchases at other times. By comparing shipment data with retail sales data, manufacturers can estimate the amount of delayed purchasing, forward buying, and the related phenomenon of diverting, described in the next section.

Diverting

Manufacturers can also take advantage of a promotion to buy large quantities of goods and then resell them to other retailers in regions where the promotion was not offered, leveraging excess warehouse and transportation capacity. If all the excess purchases are quickly diverted, the shipment volume for the diverting retailer should quickly resume baseline levels, but sales to other retailers will likely be lost.

Lift is the incremental volume over baseline for the promoted product during the promotion period at a specific account.

Net lift subtracts cannibalization and prepromotion and postpromotion effects to arrive at a measure of the real impact the promotion had on consumer consumption of a company's products.

Net Lift

Once companies have quantified all the above effects, they can arrive at a measure of net lift for a promotion. Lift is the incremental volume over baseline for the promoted product during the promotion period at a specific account. Net lift subtracts cannibalization and prepromotion and postpromotion effects to arrive at a measure of the real impact the promotion had on consumer consumption of a company's products. If a company's goal for a promotion is to reach a certain volume level for a particular product at a specific account in a given time period, regardless of the consequences, lift is an appropriate metric. But if a company's goal is financial ROI, net lift, or some variation of it, is more appropriate.

Competitive Brand Switching Versus Category Growth

Net lift consists of a mixture of volume gained by taking business away from competitive products (taking a bigger piece of the pie) and volume gained by growing overall category sales (making the pie bigger). As noted earlier, retailers find the latter much more attractive. Manufacturers should design promotions with this in mind and share supporting data with retailers to improve sell-in and pass-through.

Manufacturers might also be interested in measuring competitive brand switching versus category growth for other reasons. Depending on their strategies, they might want to grow category volume with minimal competitive brand switching to minimize competitive response. Or they might want to maximize competitive brand switching to gain category dominance.

Example Net Lift Analysis

Figures 5 and 6 below illustrate an analysis of the impact of two different promotions on the same product. The first figure shows raw movement data for a

product promoted with a TPR in week 3 and a display in week 9. At first glance, the two promotions appear to have had a similar impact. After analysis, it is clear that one was much more effective than the other. When cannibalization, forward buying, and pantry loading are taken into account, it turns out that the display promotion had a much larger impact on net lift. Further, a larger portion of the display promotion's lift resulted from category growth, making the promotion much more attractive to retailers.

From raw movement data . . .

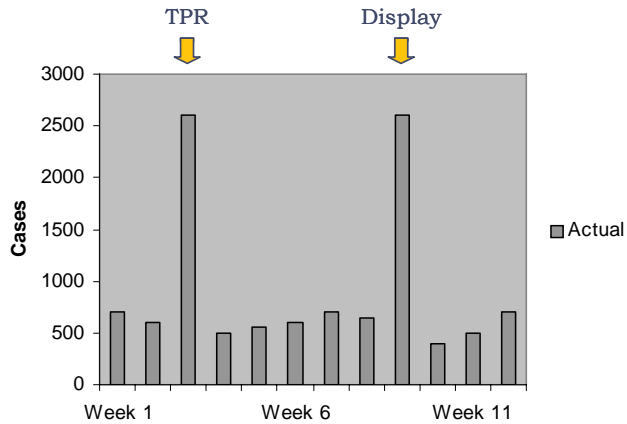


Figure 5: A temporary price reduction and display promotions appear to have similar results.

. . . to an understanding of the real impact on demand:

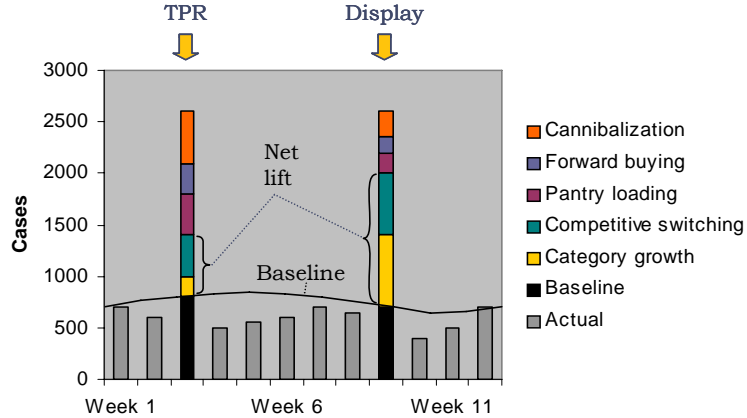


Figure 6: Analysis shows that the display promotion had a much greater impact on net lift.

Once consumer goods companies understand the true impact of promotions and capture promotion spending data during the planning process, measuring promotion effectiveness is straightforward. Table 2 below shows the incremental profits generated by the two hypothetical promotions and relates these to their costs. In this example, we see that the display generated greater profit. The TPR in fact lost money.

	TPR	Display
<i>Promotion spend</i>	\$400,000	\$250,000
<i>Incremental profit</i>	-\$20,000	\$50,000
<i>ROI (Incremental profit/spend)</i>	-5 percent	20 percent

Table 2: Incremental profits and costs of hypothetical promotions.

Harness the Power of On-the-Fly Analytics

Marketing and sales professionals intuitively know that different promotions have very different effects. Market research departments can explore these effects in detail, but on a day-to-day basis, marketing and sales managers usually have to rely on intuition rather than quantitative measures of such effects. With software offering on-the-fly analytical capabilities, marketing and sales managers can examine promotion issues quantitatively. Three examples are presented below.

Elasticity of Consumption

Promotions increase consumption and grow category sales for certain types of products, such as potato chips. Other products, such as paper towels, exhibit fairly inelastic consumption. If a manufacturer promotes paper towels, sales might surge, but it is likely that consumers are simply switching brands or stockpiling paper towels on their kitchen shelves. They are unlikely to increase paper towel consumption significantly. On the other hand, a promotion on potato chips could lead to a real increase in salty snacks category sales and consumption.

An analysis might show the different promotion impacts illustrated in Figure 7 below. The two products appear to have similar promotion lift. But the paper towel promotion generates less net lift, or less real increased demand for the promoted product. Further, most of that demand comes from competitive brand switching, rather than category growth, making the promotion unattractive to retailers.

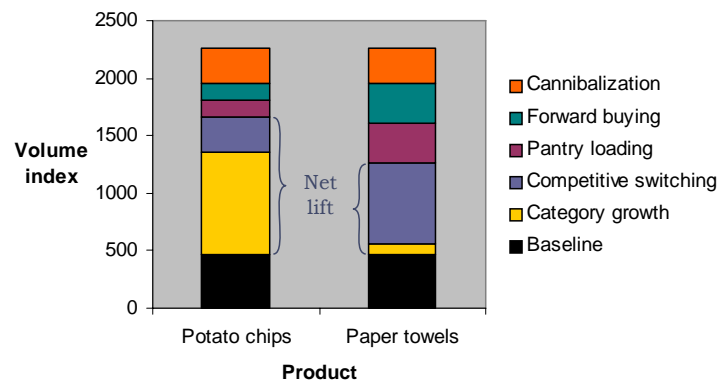


Figure 7: Analysis of promotion impact on net lift for potato chips and paper towels.

With on-the-fly promotion analytics, promotion planners can quantify such differences for all products and all circumstances.

Conditioning of Consumer Response

Research has shown that in certain heavily promoted categories, promotions which occur at frequent and predictable intervals can condition even the most loyal consumers to time their purchases to coincide with promotions. The result is that nearly all volume is sold on promotion, resulting in low margins. With promotion analytical capabilities, promotion planners could detect such conditioning (as evidenced by growing delayed purchasing and pantry loading over time) and take steps to avoid it.

Account-Level Profitability

Accounts vary tremendously in their ability and willingness to execute promotions. These differences affect promotion performance and profitability by account. Manufacturers need to quantify execution and manage profitability at the account level. A starting point is measuring promotion effectiveness by account, as illustrated in Figure 8 below, for three accounts.



Figure 8: Measurement of promotion effectiveness by account.

With on-the-fly analytics, sales and marketing personnel can conduct such analyses on a day-to-day basis at the level of individual SKUs, accounts, and promotions. Table 3 below illustrates additional analyses that could be performed on a regular basis by different users.

User	Typical Questions
Brand Management	<ul style="list-style-type: none"> • To what extent are promotions growing long-term brand sales and profits? • Are they growing the category or stealing competitive share? Is share growth coming from direct competitors or from other categories? Who are my main competitors? • How is promotion impact changing over time? • How much should I allocate next year towards trade promotions, consumer promotions, and advertising for a given brand?
Promotions Marketing	<ul style="list-style-type: none"> • Which SKUs should I promote? • What types of promotions should I run? • What should be the frequency and duration of a promotion? • In what regions and channels should I promote a product? • How much should I spend?
Sales	<ul style="list-style-type: none"> • For each account, what precise deal terms should I offer in terms of timing and other parameters? • How does my promotion compare with competitors' with respect to category growth effectiveness and profitability for the retailer? • Are there execution problems at certain accounts? How much of my promotions spend are retailers passing through? • How much forward buying and diverting are taking place?

Table 3: Example analyses that could be performed on a regular basis by different departments.

CONCLUSION

Improving promotion effectiveness has the potential to decrease promotion spending and related supply chain costs and to increase volume, revenue, market share, and profits. Additional benefits include enhanced relations with strategic trading partners and an improved understanding of consumer behavior and category dynamics.

The exact benefits of improved promotion effectiveness depend of course on a company's current level of performance. Estimates of the benefits from a sales and marketing perspective of more effective trade promotion management for consumer goods manufacturers yield savings figures as high as a 15 percent reduction in promotions spending. This would allow a manufacturer to maintain its current level of sales while increasing profits by the amount of savings.

Alternatively, a manufacturer could maintain the same level of promotion spending and increase both sales and profits. When companies synchronize marketing activities with supply chain operations, they could see up to an additional 15 percent savings on supply chain costs. These two effects together are consistent with the 40 percent increase in profits estimated by Accenture.⁷

⁷ "The Daunting Dilemma of Trade Promotion," Accenture, 2001.

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These numbers are estimates of maximum theoretical benefits, and the calculations are subject to debate. But because of the huge amount of money spent on promotions with little accounting for their impact, there is no doubt that consumer goods companies can achieve significant improvements in promotion effectiveness. If the actual benefits are even just a fraction of the above estimates, the incremental profits almost certainly justify the effort required to redesign promotion management processes. (Any such effort should of course be preceded by an assessment of current promotion performance and an estimate of potential improvements.)

In an environment characterized by decreasing margins and increasing promotion expenditures in the consumer goods industry, maximizing promotions effectiveness is a strategic imperative. To remain competitive, consumer goods companies can no longer afford to run promotions without an enterprise approach to planning, execution, and analysis. Consumer goods companies that embrace new processes and technologies for promotion management will increase profits and gain competitive advantage.



An Enterprise Approach to Maximizing Promotion Effectiveness
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