Trade Promotion White Paper Outline

Today's trade promotion environment is filled with more questions than answers. Trade Promotion should have a very real objective in mind, however many companies field trade promotions that don't work, don't deliver a return on investment and provide little or no incremental lift over baseline. Why does an industry that spends $150 billion for trade promotion not know what is the end result of those expenditures? A leading consumer packaged goods company stopped promoting many of its brands a few years back because they knew their promotion expenditures were not productive, but within a year they were back in the "dialing for dollars" business. What are the forces that would drive one of the leading consumer package goods company to abandon such an innovative strategy as to abandon trade promotions on its brands?

Our reason for presenting this white paper is to provide a catalyst for self examination in your company's trade promotion strategy, promotional objectives and the process to measure success or failure against those objectives. We want to provide the reader a mechanism for measuring their company's promotional strategy effectiveness, and even to help the reader frame what an effective promotion is and how to use that definition as a benchmark for their company's promotion strategy.

The reader must engage in a self examination of their trade promotion strategy:

- Is my trade promotion strategy correct for my market situation?
- Do I have the processes and tools in place to determine the correct trade promotion strategy for each of my brands in the markets and accounts we sell through?
- Do I have robust trade promotion simulation tools in place to facilitate fact-based trade promotion planning by field sales?
- Do I have credible metrics, key performance indicators or scorecards in place to measure promotion effectiveness?
- Can I read the KPI results of my trade promotion strategy, and take action to refine my account level trade promotion tactics and execution?

Is my trade promotion strategy correct for my market situation?

Consumer Penetration	High (Penetration) /Low (Buying Rate) A lot of consumers buy your category or brand but don't tend to buy a lot of product. You need to sell them more. Promote larger sizes & multiples Related Items Displays/Scan Downs	High (Penetration)/High (Buying Rate) Field promotions that drive incremental consumption or steal share. Temp Price Reduction/Deep Discount Features/Displays
	Low (Penetration) /Low (Buying Rate) Understand where your consumers live that do buy your product and do niche or guerilla marketing.	Low (Penetration) /High (Buying Rate) Field promotions that bring consumers into the category/brand franchise. Displays/Features/Demos/Cross Rough Coupons

Consumer Buying Rate

Why do consumer packaged goods companies promote in the first place? An impactful trade promotion strategy must be consumer-centric, and will be designed to either increase consumer penetration or increase how much product your current consumers are buying. We will explore possible strategies, gains or pitfalls for each these broad strategies. In order to understand which tactics to employ against one or the other strategic approaches one must determine category consumption characteristics. Is your category a fixed consumption category or an expandable consumption category? Will promotions that simply load the consumer's pantry with no possible hope for increased consumption ever pay back a return on investment, or are these promotions simply the price of ante in the game of promotional poker? We will explore, in this paper why these promotions are fielded, how to predict and track their effectiveness and where the industry is heading regarding the retailer/manufacturer partnership surrounding this issue of trade promotion.

1. Grow Consumer Penetration – Promotion strategies and tactics should differ widely for brands with 10% consumer penetration versus brands & categories with 85% consumer penetration. Yet, the "go to market" strategy of many companies is exactly the same for both highly penetrated products and products with low consumer penetration. Are your company's promotions designed to attract your primary consumer with a loyalty reward or the secondary consumer that is on the outer fringe of your brand's consumer base?

   Categories with low consumer penetration will not respond well to certain store level promotional tactics. For example in a category such as Refrigerated Combination Lunches with a national penetration of 24% and a penetration no higher than 59% even in the highest penetrated consumer segments temporary price reductions (TPR) may be a tactic that drives little incremental lift when executed. Further, scattered pricing across 40+ SKU's contributes to consumer confusion regarding the price/value relationship equation. Promotional strategies that drive consumers into the category will tend to produce higher lifts with smaller price discounts, and these efforts will drive consumer penetration levels higher.

   Trade promotional strategies that grow consumer penetration would include any effort to bring consumers into the category franchise:

   - New market expansion
   - Displays
   - In-store demonstrations
   - Product tie-in programs that promote together complimentary products
   - Consumer programs geared to attract new consumers to your brand

   Risks associated with this approach might include:

   - Bringing consumers into the category that would switch to a competitor's product
   - Displays, Demos and Features are the more expensive trade promotion tactics and can strap a small brand's promotional budget, but that expenditure may pay back long term return on investment.

   The upside opportunities associated with a consumer penetration trade promotion strategy can be:

- Growing consumer penetration expands the category, and brings in new consumers that will buy full revenue product.
- While the trade promotion costs for tactics (Displays) to attract these new consumers may be higher than the costs of tactics to reward current consumers (TPR) these new category consumers are not trained to wait for a promotion to purchase the product.

2. Grow Consumer Consumption– A company can grow consumption by incenting the consumer to buy product more often (frequency) or more product quantity (buying rate) when they do purchase the brand. Knowing consumers' purchase cycles for a product/category and timing the consumer need with a promotional tactic such as a feature or display will drive more frequency while multiples i.e. 2/$3.00 will drive more product quantity purchases when consumers do purchase. Knowing consumer based promotional response will drive a more effective and efficient promotional strategy.

   Trade promotion strategies designed to increase consumer consumption should not be confused with promotional flights and timing that train your brand's consumers to purchase your product only it is being promoted. Some industries promote as much as 80% of its product on promotion, effectively reducing the consumer's perceived price/value relationship. An example of this is seen in the Orange Juice category where well over 60% of the category's premium product Not From Concentrate (NFC) is sold against some kind of promotional event (Feature, Display, Feature & Display, TPR). More NFC Orange Juice is sold on promotion than the lower price and lower perceived consumer value Reconstituted Orange Juice. NFC OJ consumers have been trained to buy their OJ only when it is being promoted at price discounts of 37%-50%. Therefore, a product that has a retail value of $2.99-$3.29 is perceived by the consumer to be valued at $2.00.

   Trade promotional strategies that grow consumer purchase quantities would include any effort to get consumers to buy and consume more product quantities:

   - Develop new product line extensions
   - Multiples pricing i.e. buy 2 get 1 free
   - Promote large size containers i.e. 96oz versus 64oz

   Risks associated with this approach might include:

   - The costs and efforts required to bring line extensions to market can be high, and consumer focused line extensions can take time to identify and develop
   - Cannibalization can occur when various sizes with a brand franchise are promoted, timing of promotions across the various sizes of a product need to be timed to coincide with consumption patterns for the target consumer segment. If 64oz & 96oz consumers are the same consumer promoting one size offering will cannibalize consumer from the other size offering. True incremental sales consideration will need to take into consideration this cannibalization.
   - If your category is a fixed consumption category i.e. dog food, toilet paper or detergents selling multiples or larger size product will only result in pantry loading

and can reward consumers for purchasing product they would have purchased anyway. This is called subsidized volume because promotional dollars are being spent to sell base volume product.

- If promotions are fielded too close together consumers tend to time their purchases to coincide with promotion timing thus selling minimal product at full revenue prices.

The upside opportunities associated with trade promotion strategy designed to increase consumer consumption can be:

- Products whose consumption is expandable respond well to consumption building trade promotion strategies. Categories such as beverages, snacks, frozen dinners & entrees and children's cereals respond well to consumption building promotions because their consumption patterns are interchangeable within these broader categories.
- Line extensions tend to reach out to new consumers as the new line extensions meet the consumer needs for additional target consumers. The Tea category is prime example of this point. Tea sales were declining rapidly until ready to serve offerings and flavored teas came to market, and boutique flavored tea manufacturers found a niche with exotic product offerings that delivered higher retail prices and margins. These higher margin niche products now dominate the category and do not depend on deep discounting trade promotions to move product.

Once an optimal promotional strategy is identified and the tactics are developed and set by marketing, those tactics will little impact unless they are communicated to field sales, planned, implemented and measured for success/failure. Without the proper information, tools and processes for control at the fields sales level the finest marketing strategy is destined to fail. Where does your organization fit along the continuum of efficient trade spending and out of control trade spending with increasing trade spending and decreasing sales?

Do I have the processes and tools in place to determine the correct product trade promotion strategy for each of my markets and accounts?

Most manufacturers do not have the systems in place to insure an efficient Most manufacturers do not have systems in place that help them analyze promotions over time to identify which promotions worked and which ones did not work and why. Does your sales organization know which retail customers are profitable and which ones are not, and does your organization alter its "go to market" strategy based on that knowledge?

What is the objective of an effective promotion?

- Incremental volume (volume above expected sales in the absence of a promotion)
- Incremental profit (is the profit from subsidized base volume more than the incremental profit realized from the promotion?)
- Increased Consumption from increased consumer penetration and/or increased product purchased on a buying trip
- Captured share that is maintained over time
- Minimal cannibalization within my brand – if we promote the 64oz item, what happens to sales on the 96oz item for the same product?

What key performance indicators (KPI's) are required to measure trade promotion quality?

- Promotional response rates (lift)
- Baseline volume
- Incremental volume
- Subsidized volume
- Cannibalization rates
- Cost per incremental unit
- Incremental profit
- Return on promotion spending investment

How does your organization manage trade promotion planning, tracking spending & volume through the life stages of the promotion, approval and settlement? Many companies exist somewhere along the continuum of a high degree of understanding of expected promotion spending by customer by product and by time period to simply placing a bundle of money in the hands of sales managers and hoping for a maximized return on promotion investment.

Manufacturers that have demonstrated successful trade promotion return on investment have been able to systematize a process of strategy development & communication, funds allocation, planning, approval, redirecting funds, settlement and post evaluation. Manufacturers can be segmented according to their ability into define an effective account/product strategy, plan & track spending & volume against that strategy, measure that strategy's effectiveness and adjust strategy quickly based on this knowledge. We will segment packaged goods manufacturers as crawlers, walkers and runners according to their level of sophistication. This paper will explore the differences between sophisticated and less sophisticated manufacturer approaches to this process.

Let's look at each of these elements of the process:
The best practices (top down & bottom up), what is the real world paradigm and what undiciplied companies are doing and what financial, organizational etc implications to taking the minimalist approach to each step. Run, walk crawl

1. Strategy Development & Communication – Strategy development must center on what the trade promotion is designed to do – drive penetration, drive buying rate, drive share etc. Aside from general trade spending economics, many companies promote for no other reason than to maintain a status quo (we spent $.50/case last year so we will spend $.45/case this year). Effective trade promotion strategies must revolve around which consumer(s) we are trying to reach, what incentive those consumers have to buy and which promotional tactics are likely to reach that target consumer. Some companies depend on brokers or account managers to "guestimate" baseline volume and the incremental volume a tactic will drive based on historic output. This approach does not consider evolving market trends, which consumers are buying the target product, why they are buying the target product and why they buy in retailer "A" versus retailer "B". Some companies do not know the level of compliance behind a certain strategy developed in the marketing department and fielded with the expectation that field sales will implement the strategy as developed. However, many companies have no way to track compliance, measure the effect or to insure funds designated to the strategy implementation were used as desired.

   Runners know the profitability of each their accounts and which trade promotion strategy worked based on results from specific promotion KPI benchmarks. Runner organizations can employ either a top-down or a bottom-up planning approach, but both approaches have trade promotion guidelines that are supported by KPI's and measurement tools to track gaps to those guidelines. Runners develop promotion strategies that have research to support the potential for success if when the specific tactics are properly executed. Successful promotions for runners are those promotions that increase consumer pull through the account. These runner organizations also have the tools to track compliance at the retail account level.

Crawlers tend to promote in patterns that are dictated by competition or past history and the success of the specific tactics used is considered based on sales to the account rather than consumer pull through the account. Crawler organizations seldom have comprehensive marketing plans that pull various elements of trade, consumer and media elements in a complementary program. Crawler organizations don't know the profitability of their retail customers, and this sets up a scenario of continuing expensive promotions that provide little lift and profit.

Manufacturers that know the most profitable trade promotion tactics by customer will field more profitable promotion strategies, avoid those tactic that hurt both retailer and manufacturer and field promotions are on strategy.

2. Funds Management – In organizations along the funds management continuum one will find a major decentralization of funds management to the field sales organization with little approval or accountability as to the spending by brand or the return on investment other than to drive a case volume objective. At the other end of the continuum organizations are using tight funding controls down to the promoted group level. The allocation of funds is a daunting task when the tool of choice is hundreds of spreadsheets that need to be disseminated down the sales hierarchy and managed at aggregated levels of the sales management hierarchy for evaluation. In a system driven approach checkbooks can be established at various levels such as product level, sales organization level and at an account level. Then distributions of these funds can be tracked as they are distributed down the sales hierarchy to the retail customer. Once a parent-child relationship is established these funds can be tracked using an audit trial, making the process of withdrawing funds and redistributing them to other sales opportunities much easier and controllable.

   Runner organizations set up checkbooks with product specific funding to insure Product A's funds are not spent on events for Product B etc. These organizations properly fund product groups within a brand, based on expected profitability of that specific product grouping. A product group is a subset of a brand that identifies multiple SKU's that are typically promoted together each time they are promoted i.e. all 12 oz Dinners or all Buffet Cat Foods within a brand.

   The funds management process is tracked via an audit trail from allocation through planning and to moving unused funds about the organization. At any given time the trade promotion group knows how much money is any stage of the promotion lifecycle, and can easily redirect unused funds to volume producing opportunities. In these organizations trade funds are not hidden in plans that have little probability for retailer commitment or execution.

Crawler organizations do not set up funds management systems and only allocate funds to the field sales level with no approval mechanism to insure the funds provide are used efficiently. These organizations allocate funds at very high levels and those funds are spent across all brands and products with no consideration for the P&L impact of under funded brands or over funded brands. In these organizations field sales has maximum control of trade promotion funds and these funds can be pigeon-holed into fictitious plans that prevent the organization from strategically moving funds across various opportunities that may have a higher payback that where those funds were originally allocated.

3. Event Planning – Along the planning continuum one finds various philosophies for trade promotion planning:

    a. Gain an understanding of expected volume quota attainment only
    b. Gain an understanding of volume achievement and understand the potential impact to product manufacturing & logistics
    c. Gain an understanding of volume achievement and understand the potential impact to product manufacturing & logistics accrue anticipated spending for accurate quarterly accounting purposes
    d. Gain an understanding of special pack planning, production & logistics

A systematized approach would provide a robust predictive modeling tool to evaluate the appropriate variables to predict consumption volume and return on promotion spending investment.

The predictive modeling tool would build several optimized scenarios based on minimal input by the account manager. The account manager would select an account, select a product and the system would deliver back three possible plans to select from, optimized for three different strategies i.e. optimized for maximum incremental volume attainment, maximized for retailer profit or maximized for trade promotion spending ROI. Upon selection of the desired plan strategy the system would enter the necessary rates, dates, trade dollars, baseline volume, incremental volume and other metrics customized to your company's needs.

A systematized approach to trade promotion planning provides for marketing/trade marketing built strategic promotions with elements such as consumer promotions, media and other marketing incentives to be communicated, planned and the results tracked. This tracking provides for tracking compliance for the national event across promotion life stage or phases i.e. Draft, Planned, Pending, Committed, Performed and Paid.

Runner organizations know which promotional vehicles deliver the maximum impact depending on the desired strategy. They use predictive modeling tools to forecast the volume impact when various tactics or combinations of tactics are used. Runners know the spending & volume totals for each lifestage of the promotion cycle, and know when & where unused/committed funds can be

Crawler organizations rely on unscientific forecasting of promotional baseline and incremental volume by account managers. Those volume estimates are based on historic sales results, but those sales results could include diversion, forward buys and profit taking by the retailer. There is no scientific approach to quantifying or predicting the volume impact of various combinations of tactics and discounts at many manufacturers. Some "crawler" organizations look to their account managers to predict baseline volume as well as incremental volume. This presents serious problem in post promotion evaluations, and the continuity of volume forecasting methodologies across account managers and for new account mangers just coming into an account.

4. Approvals and Oversight – We see manufacturers that run the spectrum from no promotion approval process to a micro-managed approach for approving and tracking planned spending and event plans. Many times those companies that are not approving planned field trade promotion spending have adopted that stance due to the lack of internal systems appropriate for approval and tracking. Other companies engage in such micro-managed approval processes that the field is strapped to get trade programs in front of their retailer partners in enough time to execute appropriately or the lead time for planning is so elongated that company cannot adequately react to competitive pressures. Manufacturers that have been successful in meeting the balance between trade funds accountability and management oversight of those funds have used a workflow mechanism to track plans through the approval loop. In a system driven solution to trade funds management senior management can have complete visibility to trade promotion plans well in advance of their execution and can drive adjustment of the account manager's planned execution strategy. In addition, by tracking the aggregated spending and volume numbers at any stage of the promotion lifecycle management can have a valuable tool to set expectation, adjust go-to-market strategies, manage logistics issues related to volume spikes and/or manage quarterly financial expectations.

5. Payments & Deduction management – Well planned and documented selling strategies that are entered into the order management system beget properly funded promotional executions that are settled quickly and efficiently and will stand the rigor of post audit scrutiny. Deductions occur when promotional elements communicated to the buyer are not well documented or are not in the seller's order management system to insure proper invoicing. To be sure, retailers use invoice deductions as a mechanism to settle outstanding promotional claims quickly, but those deductions are easily accounted for and cleared. In a manual or paper environment planned execution (if promotion planning is done at all) may or may not be entered into the order management system because of side deals and under the table dealings with the retailer b y the account manager. The results are deductions that are difficult to account for and clear off the books, and these types of deductions are more difficult to account for and clear in a post audit. When a system generated approach is employed:
    a. Account level event plans are sent by workflow rules through an approval process
    b. Adjustments are made through that approval process and/or in the account presentation process
    c. Upon retailer commitment to those plans, they are then interfaced into the order management system to insure exactly what was approved is what is invoiced from the order management system

The result of this system driven approach are fewer open deductions, faster accounting & closing of open deductions and a greatly reduced paperwork load stemming from the deduction management process.

6. Post Promotion Analysis – Bad promotions that are run each year because they were run a year ago only serve to continue poor promotion practices. Post promotion analysis is actually the first step in the planning process for next year, and begins the process of building the required data for the predictive modeling process for next year's promotion planning process. With all of the requisite data stored in one place – shipments, consumption, spending and actual performance detail – post promotion analysis is greatly simplified. Driven by the same algorithms that drive predictive modeling in the planning process, a robust trade promotion system will answer the age old question of which promotions worked and which ones did not work. The metrics required to evaluate promotion efficacy are common across most companies – incremental volume, ROI, lift, cost/incremental unit, subsidized volume etc but some can be customized to reflect cannibalization across SKU's in a brand, profitability and others specific to your business model.

   In a systematic approach lift coefficients can be modeled from account history or from history stored across all accounts in the database. A system could shift between historic account lift coefficients and historic coefficients across all accounts in the database using sales rates such as sales per $1 million ACV to equalize comparisons across all accounts in the database. Using this approach the system will show the account manager a more accurate forecast for the impact of tactic(s) and discount combinations.

   It is interesting to note that retailers are looking for the same type of information as they evaluate the thousands of promotions that are "pusher across the buyers table" to them every year. They want to know which promotions will generate the maximum volume and/or profit in the limited merchandising space available to each Category Manager. They want to know:
   - Which store clusters should be included or excluded in an ad plan?
   - Will a deep cut TPR deliver enough incremental volume to offset the lost revenue on a per unit basis?
   - When should I run the three competing products that just gave me their "hot" promotions?
   - Which display location provided the maximum lift on this product?

   If a manufacturer trade promotion system provides valuable predictive modeling insight into the best tactics and price discounts to drive volume, then the retailer is looking for similar guidance as each manufacturer pushes their promotional proposals across the Category Manager's desk.

What is the future of this promotional "blackjack game"? The retailer's Category Manager sits across the buying table from multiple manufacturer sales agents, and each sales agent is pushing their "best" deal to get the best ad space BUT there can only be one winner. The retailer needs a tool that will select the optimal item to promote at a specific time, and perhaps even when to promote the competing items at time frames that don't overlap consumption patterns for the product category. The future of trade promotion and trade promotion systems is to facilitate a collaboration between manufacturer centric trade promotion planning systems and retailer trade promotion evaluation systems. The retailer has the fuel to drive such a collaboration process – the POS data, and the manufacturer has the consumer data and market level syndicated data AND the promotional dollars.

If the two segments collaborate across the promotional "blackjack" table there will be significant cost reductions in the process as the planning process on the manufacturer side is driven by intimate knowledge of sales lifts store by store from the retailer POS data, electronic interface of proposed promotional plans, retailer system evaluation of all collected proposals, decision & scheduling of merchandising tactics, submission of promotional claims by the retailer and instant payment of those claims that meet agreed to spending & performance specifications. This process will be managed electronically through collaboration between manufacturer and retailer promotional planning systems.

The larger benefits of this future vision will be tighter logistics processes at the manufacturer by accurately predicting promotional spikes in manufacturing, facilitating efficient raw materials procurement, correct staging of finished goods at distribution centers to provide to eliminate short shipments fully support the planned performance at the retailer. The planning processes of the manufacturer and the retailer would be meshed together in a seamless flow facilitated by access to the retailer's POS data, predictive modeling engines, workflow engines and electronic data interfaces:

1. Pre-planning analyses – the planning system evaluates previous events' results for various product/account/tactic/discount combinations and benchmarks those results against national averages. The system will provide a ranking of "best" promotions based on multiple strategies i.e. profit driver, volume driver, consumer segmentation etc.
2. The manufacturer system evaluates retailer POS data to develop recommended plans to present to the account manager. Those plans will be across promoted groups and will recommend tactics, timing and discount levels for the account manager's consideration. These recommended plans will be developed based lift coefficients developed from the account's historic data & performances.
3. The account manager will review the proposed plans make any adjustments necessary in the planning screens and/or add additional events to the proposed list of events. The plans are in the draft status now, and those draft plans can be rolled to evaluate volume and spending estimates early in the planning process.
4. By workflow rules all completed plans are sent to approving authorities within the manufacturer. The plans are now in the approval status and are locked on the account manager's system.
5. Upon approval by the approving managers, all plans are eligible to be released to the account for consideration in accordance with preset workflow rules. This process is done electronically through an on-line collaboration site with connectivity between the retailer and the manufacturer. No deal sheets or new items sheets need to be completed as these will be done electronically in the retailer's own expected format. At this stage of the promotion life cycle the promotion is in the offer stage.
6. The retailer is receiving similar transmissions from competitors and the retailer system is evaluating a best fit merchandising plan based on strategy rules in the retailer software. These strategy rules may be based on the role this category or segment plays in the

retailer's stores, competitive pressures or profit objectives. The category manager will be presented with a recommended merchandising plan that can be overridden by him/her. Any manufacturer offerings that are accepted are so indicated and communicated by workflow rules, and any change requests are sent be workflow rules back to the respective manufacturer for consideration or rejection. The loop starts back over again for those change requests from the retailer.

7. For those plans accepted by the retailer ad, display and/or TPR tactics are setup in the retailer's system, recommended orders generated and timed to hit the retailer's distribution centers in time for cross-docking to the stores involved in the merchandising effort.
8. Those orders are interfaced to the manufacturer and logistics systems take over to insure finished goods are staged in the correct shipping distribution centers that serve the target retailer.
9. Performance is executed and compliance is indicated electronically by the retailer to the manufacturer through electronic interface between the two respective systems, and the compliance is flagged on the account manager's dashboard for authorization.
10. Upon authorization an electronic payment authorization is generated and paid in the same day, thus eliminating deduction paperwork.
11. A post performance scorecard is completed by both the retailer and the manufacturer systems and graded for success or failure versus expectations.

This is the vision of the future of trade promotion systems and the collaboration between both systems to drive waste and time lag out of the process and drive efficiency, accuracy and profit into the process.