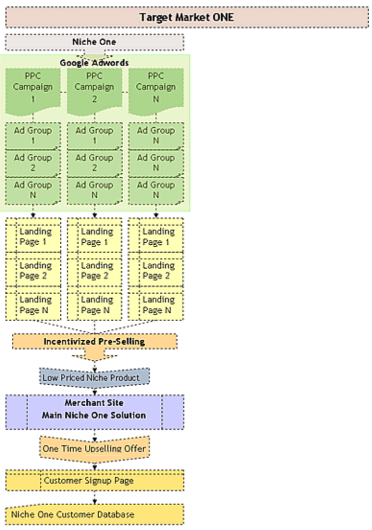
europartnership consulting

EUROPARTNERSHIP WHITE PAPER DIGEST

Using performance drivers

within scenario based models



Underpinning business growth strategies
with analytical business models

SSC101D

Contents

Summary

Organisations face relentless pressure on prices and markets. At the same time financial return has to be balanced with managing risk and corporate governance as a requirement from stakeholders. Traditional analytical approaches – such as market research – have limited value for identifying and exploiting new growth opportunities. We need an approach that integrates the technology and market insights with customer demand, cost and capability for informed decision-making.

For instance, in the 1990s high-growth businesses appeared offering a range of software applications hosting, management, and infrastructure services. These Application Service Providers were the darlings of investors. The initial value proposition "lower cost enterprise applications and infrastructure" ran out of steam as many ASPs focused on large-scale, low-cost rental models, lacked differentiation - and did not add compelling value to customers. By contrast, a few focused on understanding customer needs beyond "low cost" and:

- Created tailored applications - not just re-cycling versions of existing functionality;
- Enabled incremental service delivery – not a wholesale shift to applications rental;
- Innovated with access to scarce skills, superior service and leading methodologies.

Companies willing to evolve their original value propositions survive crunch periods. Trying to anticipate how demand is shifting is a tricky and risky proposition. Managers need robust models and an effective process to reach consensus and execute strategy successfully.

Modelling allows managers to test scenarios, get everyone on the team to see where the greatest value lies, and quickly redeploy resources to capture business improvement opportunities. Across sectors, these methodologies have led to growth in revenues, margins and underpinned sustainability.

Using performance drivers in scenario based models

Don't just know who your customers are – get inside their heads

Customers talk about price and product features because they matter. Get inside your customer's head and truly understand buying decisions – and you may find other considerations. These will include: reliability; ease of deployment; maintenance and service arrangements; or certainty of delivery date. Cumulatively, these influences may account for 70% to 80% of the purchase decision.

Assessing future potential means quantifying outcomes, inputs and performance drivers. Surveys are useful starting points -but fail to identify growth opportunities as they are:

- Detached from business economics. Research rarely links findings such as "we are difficult to do business with" to what the customer means by this – and still less with what needs to change, the cost of change, or what that change will yield to revenue and profits.
- Marketing insights describe customer segments, but less often what the business should do differently in order to serve those segments more profitably.
- Marketing typically focuses on customers' current needs and satisfaction levels with existing offers. Rarely systematically analysing customers' emerging priorities.
- Research is too far removed from the day-to-day product or line of business – often handed off external research - the odds of receiving the right answer to nuanced questions are low.
- Multiple market research sponsored by sales, product development, corporate marketing, and other functions yield a fragmented and often contradictory mosaic of data.

" Value Engineer" your customer

Firstly, use your knowledge about their customers and apply the business performance drivers. Second, build consensus by pooling the entire management team's knowledge – and challenge the folklore about the customers' behaviour and the dynamics of the market.

Customer Value Engineering provides insight about the next major sources of value for customers and for shareholders – going beyond market research to uncover what customers will value and pay for and linking these insights business performance drivers – creating consensus and driving change.

Combine insights of customer demand and company cost

1. Analyse the drivers of demand. Tool such as Strategic Impact Grid help get inside the customer's world to uncover which factors drive demand based on the choices made by customers. Ultimately, this approach can quantify the impact for instance of brand, outside influencers, and so forth. Identify the key performance questions - and develop the interpretive skills to derive customer value. Models are used for strategic analyses - for instance, the effect of changing price plans and price levels – with predictions about which competitors gain or lose share as you forecast the results of attack and counterattack.

2. Segment in a smarter way. In some consumer industries, companies have become adept at highly segmented customer acquisition and retention patterns. Firms in many other industries, especially the business-to-business sector, are content with basic segmentations based on revenue, number of employees, or industry category. Factors such as size do matter, but buyer behaviours and priorities matter much more. Understanding segmentation means using value-based analysis, including customers' current profitability to the business, differences in elasticity of their demand and their prospects for future growth.

3. Create a robust strategy model in order to answer the "what if" questions. Value drivers and business economics data need to be built into a representation of the company's business. Managers use the models to evaluate the impact of possible initiatives or actions on various financial metrics – and how countermoves by competitors will affect any given strategy.

Illustration: Exit or reinvent? A technology provider was eking a 1% profit in a line of business that had become commoditized. The firm was losing profits faster than it was gaining market share and managers were at the point of deciding whether to exit the business. Based on the analysis and scenario modelling, the firm shifted resources away from product features and toward post-sale services such as remote monitoring and fault detection. The additional value discerned by customers justified an increase in price and led to revenue growth and 4% margin within a year.

Illustration: Gaining visibility to end users. A multinational service company was looking to grow its share among small and medium sized businesses in a highly competitive market. Bracketed by low-cost established players and high-end strongly branded newcomers – and reliant on third-party distribution channels - management had limited insight into buyer needs and preferences. Anecdotal evidence said that offerings were overpriced relative to the market. In fact, customer segments had distinctly different price sensitivities and offering requirements. This allowed a scenario for each customer segment – where offensive and defensive pricing could be modelled. The company lowered prices in some segments, while in others it has focused on adding features and service assurance that make the product more valuable to customers rather than on dropping price.

Illustration: Accentuate the positive. Managers in a product manufacturer had a long-held belief that their products, while integral to their customers' operations, were essentially a commodity. That is, all buyers used the products in the same way, and all comparison-shopped based on price and functionality. In reality, the market was sharply divided along almost every important dimension. As a detailed picture emerged by using a quantitative analysis of buyer needs, attitudes and economic trade-offs, the company identified groups of customers with very different price sensitivities. Their "one size fits all" pricing model had been leaving money on the table with some customers and losing them share among other customers. Marketing and sales tweaks got the right offer to the right segment. Finally, different groups of customers had preferences among the channels they wanted to use - to learn about the company's products, buy them, and then maintain their post-sale relationship. Result, a shift from commodity margins to a more profitable model

Scenarios allow teams to model the "unthinkable". Managers can test direct elements, such as price and features; and indirect elements, such as ease of use, reliability, and post-sales support. Models integrate demand and cost into an interactive profitability model in a way that no other process can. Using an inclusive, cross-functional, team sales, marketing, product management and development, delivers consensus about the outcome by addressing all key performance questions.

Europartnership delivers high quality support designed to improve organisational performance through consulting, facilitation and training in strategy development, performance management and Balanced Scorecards. Our approach is to work in partnership with clients to establish continuous improvement programmes – adding value by knowledge and skills transfer.

Our mission is "to equip organisations to improve performance"

For more information contact john.shuttleworth@europartnership.com