When the economy slows, top companies resist the temptation to get sales at any cost—and use the time to build commercial capabilities to excel in the recovery.
Introduction

The laws of gravity are still in place: a recession eventually will end what has become the longest economic expansion in U.S. history. When the downturn arrives, deal volumes may fall, sales teams may sweat, and competitors may lure customers away with lower prices. Some leaders will react in haste, offering discounts across the board and chasing unprofitable deals. Board members and shareholders may push CEOs to look for sales at any price and postpone investments in future growth.

But letting go of commercial discipline, even briefly, can have serious and lasting consequences. In the 2008 recession, for example, a multinational chemicals supplier reacted to declining orders by abandoning pricing discipline and slashing headcount across the board, starting a spiral that led to bankruptcy.

In contrast, a media company reacted to declining consumer spending by holding fast on pricing but doubling down on value. It offered a wider range of products and improved its value proposition, retaining customers and even upselling them. It emerged victorious from the recession and ready for a new wave of growth.

While commercial strategy was not the only differentiator between these two companies, maintaining commercial composure helped one thrive while the other struggled. In this brief paper we offer a timely overview for C-suite executives of a strategy to maintain best commercial practices during a slowdown and prepare to take share when demand rebounds. This involves action in five areas to limit immediate damage to margins and build long-term commercial strength.

01 Develop a dynamic response model
02 Identify and stay close to the best customers
03 Maintain discounting discipline
04 Strengthen sales muscle
05 Build commercial excellence infrastructure
Dynamic response modeling is the ability to make decisions or execute a set of actions that are repeatable, sustainable, and lead to superior business outcomes. In pricing, dynamic response means adjusting prices in rapid response to a well defined external or internal trigger. Some ride-sharing companies, online retailers, and airlines update prices several times a day to reflect changing demand and supply dynamics. And the practice is becoming more common in B2B markets, such as chemicals and component manufacturing. Dynamic pricing allows companies to capture more value in favorable conditions—when demand rises—and lower prices when necessary.

In sales, dynamic response requires identifying what drives value for specific customers: some require just-in-time delivery, for example, while others value custom features. It also requires understanding cost drivers, such as the cost of changing manufacturing runs for rush orders.

A consumer goods company developed a dynamic-response model that generated scenarios for a full range of potential competitor actions. It built a full suite of competitive intelligence capabilities including “patterning” historical competitor moves and pricing actions. It then tested response plans, which included no-regret moves, strategy adjustments, and preemptive actions. The program helped the company add 75 basis points to its bottom line, a big achievement in the low-margin business, and build lasting competitive advantages.
When a downturn arrives, requests for price reductions soon follow. Who will get the discounts and who won’t? It’s a difficult trade-off between holding the line on price and managing customer churn. In a downturn, every order counts and getting a new customer costs more.

To determine which customers are worth fighting for, sophisticated customer segmentation is paramount. Traditional segmentation defines the “best” customers in terms of revenue. But a more useful segmentation will look at customers in terms of (fully loaded) profitability, growth rates, relationship quality, and market power. A detailed segmentation can identify unprofitable accounts and inform plans to restore profitability for the account. Or, it can indicate which customer should not qualify for further discounts. Companies can decide to invest in true partners, by offering good prices or more value in the form of technical sales time, extended warranties, or post-sales support.

It helps to be candid with top customers about the company’s intentions. Openly discussing ways to increase share of wallet with valued customers, including offering incentive rebates or volume discounts tied to share of wallet (rather than volume or spend), can help secure revenue with limited effort.

A global packaged foods company seeking to boost profits analyzed economic contribution by customer by costs, including inventory, storage, and production. The company discovered that its top ten customers contributed 80 percent of value—and that the bottom 30 percent were unprofitable. The firm developed targeted action plans for the bottom 30 percent, bringing data into negotiations to propose changes in pricing or drivers of cost to serve. For each negotiation, the sales rep was given a “walk-away” point. Over time, the company returned the entire customer portfolio to profitability through a mix of pricing and service actions.
As demand softens, many companies are tempted to discount or cut price to sustain volumes. But lowering prices is a short-term move that competitors may easily replicate. Indeed, a recent KPMG survey of executives across industries shows that the No. 1 trigger for pricing moves is competitor action (Exhibit 1).

Multi-period recessions can drive prices lower as customers repeatedly demand price cuts. But then the supplier is left with sharply lower anchor prices that persist after a recovery, depressing revenue and tarnishing brands and quality perceptions.

Exhibit 1—Price moves are often driven by competitors, not data

Why do you make pricing moves?

- Change in competitor pricing strategy: 36%
- New entrants in the market with new business models: 29%
- Launch of new products/services: 28%
- Improved capability/data: 20%
- Disruptive technologies changing the product/services: 19%
- Economic cycle: 16%
- Increase in cost of input: 15%
- New management: 11%
- Change in regulations/tariffs: 11%
- Our pricing strategy has remained unchanged: 9%
- Weak financial performance: 7%
- I don’t know: 1%
- Other: 1%

Source: KPMG cross-industry pricing survey, 2019. n = 425
Price reductions are not always visible. We find that most companies suffer from hidden “value leaks” as they give away freebies to close the sale—neglecting to invoice for freight surcharges, for example. In our experience, these and other forms of leakage can dent profits by 2 to 5 percent of revenues. In tough times, every point of margin counts even more.

A quick pricing analysis or “diagnostic” helps senior leaders get a clear view of current and potential leaks and craft a plan to address them. By reviewing transactions in detail, a pricing diagnostic can reveal all the sources of leakage. Examples include failure to charge when customers don’t meet contracted minimum-order sizes or clawing back volume discounts when quantity commitments aren’t met.

Based on the diagnostic, the company may keep offering some generous terms but market them as part of a superior value proposition—while holding the line on rebates, incentives, and other terms.

A diagnostic can also identify areas of pricing policy that may spring leaks under future pressures. The exercise can show what foundational capabilities are needed to enable growth without leakage and identify specific tactics for long-term growth.

Leadership can prepare for price reduction requests by developing tactical (re)negotiation plans and establishing the governance and training to support them. Sales teams should be ready to offer customers compelling trade-offs instead of rushing to discount. The most effective sales teams know what each customer is willing to give up to meet its cost-reduction targets.

Price reductions are not always visible: we find that most companies suffer from hidden “value leaks.”

An industrial equipment company’s revenues were rising, but margins were falling. When a pricing diagnostic identified value leaks, leadership modeled the impact of pricing changes to build a case for change. They used a strong communications and marketing plan to sell the change to customers. It included new markups for items such as urgent deliveries and stocking surcharges on low-velocity items. The change led to positive financial impact within two months, with less than 1 percent incremental customer churn.
An industrial equipment distributor, looking to grow revenue and profitability across regions and product lines, recognized the need for better contract negotiations. It hosted intensive two-day workshops for 500 sales managers, tailored to their geography, experience and other considerations. The training led to better contract negotiations and some notable wins, and helped add $80 million (in a multibillion-dollar corporation) to margin contribution in the first 18 months. The impact has increased as more sales people have gone through the training.

During slowdowns, many businesses initiate cost-reduction programs, which frequently include cuts to selling, general, and administrative expenses. Cuts in sales and marketing spending can backfire if sales team capacity, capabilities, or motivation leads to lower sales.

Indeed, when business is slow, most companies need stronger sales capabilities to pursue and close deals with minimal discounting. In fact, investing in sales talent and capabilities in a downturn may do more good than including sales in company-wide cuts.

To learn how to get more bang for the sales and marketing buck, companies can start with a sales effectiveness review. This can reveal common areas of opportunity, such as increasing sales time allocations and improving incentive plans. The most effective sales teams spend more time selling and less on paperwork and other non revenue-generating activities that can be offloaded to lower-cost resources. From running sales effectiveness diagnostics, we have learned that most commercial companies have multiple incentive plans. These are seldom realigned to match changes in pricing strategy and desired outcomes.

In a recessionary environment, firms may need to reset quotas and incentive payouts to keep the sales team motivated and reduce unwanted behaviors. In a non recessionary environment, we find that fine-tuning incentives can unlock sales improvements of as much as 5 percent; during a slowdown, they can limit the decline in sales or even produce some gains.

Investing in sales talent and capabilities may do more good than including sales in company-wide cuts.
Many companies see slowdowns as periods of retrenchment, but our experience suggests that this may be a critical time for building commercial capabilities and systems. As we have seen, it takes more skill, data, and sophisticated tools to manage pricing and discounting in a downturn than when the orders are pouring in.

New insights, monitoring, value measurement, and governance models can help companies make sales decisions. A dedicated team in a “war room” can focus on high-quality deals and invest only with the right customers.

A recession can be a good time to invest in the people and technology for making smarter pricing decisions. One upside of a slow period is having the time to take stock of what’s working, and deploy idle resources to roll out better tools and processes to help teams be more efficient and accelerate growth during the recovery.

Companies can learn how great an opportunity they have for improvement by undertaking a pricing maturity assessment. This exercise shows how a business performs across key capabilities, and indicates whether new people, systems, or processes are needed to help improve performance. In a 2019 KPMG survey of 425 companies across six major industries, we found that companies that rank high on pricing maturity have EBITDA margins of 3 to 8 percentage points higher than peers. The same survey shows that it takes a dedicated pricing team to reach a high level of pricing maturity.
In conclusion: Preparation matters

The practices and actions described in this paper can boost performance in good times and bad, but we’ve found that they most clearly distinguish strong performers during downturns. But that happens only for companies that plan in advance—when demand in the economy dries up, it’s hard to plan and implement a new pricing model or build a salesforce with the right skills and behaviors.

When the downturn arrives, companies that have prepared to maintain their commercial discipline will keep their heads above water. And once the economy revives, they will be better placed to find new opportunities and quickly recover—while less-capable competitors flounder.

How we can help

Through booms and busts, our Commercial Excellence and Pricing practice supports clients in improving revenue and profitability. Our Pricing Diagnostic, Sales Effectiveness Diagnostic and Pricing Maturity Assessments can help businesses take action across the five areas identified in this paper. Companies that have built a high level of pricing “maturity” and use these actions have improved return on sales by 3 to 8 percentage points, depending on industry sector. We work side-by-side with our clients to design and execute solutions, starting with our diagnostics, which uses data analytics, proprietary methodologies, and visualization. These tools yield rapid, actionable insights and identify specific pricing opportunities. Our solutions are designed to drive performance improvements in the short term—in all types of market opportunities—while also building long-term capabilities.

KPMG assists clients in achieving Commercial Excellence through five levers

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Serena helps clients optimize pricing, sales, and marketing strategies to increase revenue and profitability. Over more than 12 years of strategy consulting she has focused on supporting companies through evolving market conditions (new market entries, product launches, competitor moves, changing macroeconomic and trade conditions) by updating go-to-market strategies. She has led engagements on customer segmentation, sales effectiveness models, and offer, pricing and discounting strategies. Serena supports clients in technology and industrial manufacturing industries.

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Kinsey helps clients to improve pricing and commercial capabilities through design and implementation of data-driven strategies that incorporate internal and external data points to inform decision-making. She leads development of analytical tools for the Commercial Excellence and Pricing Practice. These tools identify margin improvement opportunities, segment customers and products, and improve sales performance for her clients.
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