

# Gross Margin Management

In today's economic climate companies cannot simply grow their way out of profit problems. Manufacturing costs have been cut to the bone, there is pricing pressure, and demand is declining. Thomas Group offers an integrated approach to maximizing gross margins, called MarginMax™, providing a company with additional strategic alternatives to achieve bottom-line results.

Integrated gross margin management is a way to generate significant profits from a business by focusing on the existing value-creating activities without embarking on a major business transformation process that could take years to implement.

Improved gross margins are one of the most powerful levers of financial performance. To illustrate, a \$400 million company with a 40% gross margin rate that can increase its gross margin by 7.5% will add \$12 million to their gross margin, which is a 30 percent increase in operating profit. Figure 1 demonstrates our gross margin leverage.



Figure 1

## Gross Margin Leverage

The MarginMax methodology is implemented by focusing on gross margin as the leverage point and incorporating all the key drivers of gross margin into an integrated margin improvement program that aligns from strategy to daily execution. The key word is integration. Operational cost reductions alone are not sufficient in today's business climate to achieve your profit objectives. An integrated approach is required. The companies that employ this integrated methodology to manage their gross margin will be more successful in delivering bottom-line results.

MarginMax aligns the organization to facilitate understanding and management of all the key drivers that maximize gross margin.

The four key gross margin drivers are:

- Pricing optimization
- Product management
- Sales effectiveness
- Operational performance



Figure 2

Each of these key drivers of gross margin must have concrete, margin-related objectives, concise measurements, and clear ownership in the organization. Maximizing gross margins requires focus on the right drivers and alignment of these objectives from the senior management team to the front-line people closest to the action. Integration, focus, alignment, and teamwork sound simple conceptually; however, few companies do it. The good news is that all can.

Integrated gross margin management is a sustainable unique methodology that focuses on all the key margin drivers. The synergy from understanding the interdependence of the key gross margin drivers produces results that are greater than the simple sum of the parts as illustrated in Figure 2 above. Operational performance improvements enhance sales effectiveness. Product management drives improved operational costs and improved sales. A gross-margin-focused sales force improves operational costs, the pricing processes, and product management. Additionally, correct pricing strategies and processes benefit product management, sales effectiveness, and operational performance.

The MarginMax difference is an integrated management approach, focused on the right drivers and an aligned management team, as indicated below in Figure 3.


**MarginMax™ Program**

- Changes business strategy to managing gross margin
- Leverages all four key drivers of gross margin in an integrated approach
- Typically significant opportunities reside in the market facing (external) drivers
- Management works as a team
- Process changes build in a continuous improvement methodology
- Fundamental long-term shift in financial performance... a 5% to 10% increase in gross margins

Figure 3

A MarginMax evaluation will identify gross margin opportunities. Flags that indicate a company has gross margin opportunities are:

- A cost-based pricing strategy is employed
- The pricing process is not well defined or measured
- Customer profitability data is not used to manage customer accounts
- The sales force is compensated on revenue
- No formal cross-functional product management process exists
- Sales, marketing, and manufacturing are not synchronized

If these flags exist in your company, MarginMax, coupled with our team of experts, will enable you to take advantage of your gross margin opportunities. 

The MarginMax Rapid Implementation model, shown below in Figure 4, focuses on the key gross margin drivers and identifies the high value levers that will produce improvements after three months with substantial results in six to nine months. The objective of a MarginMax program is to increase your gross margin 5% to 10% and deliver a five to one return on your investment.

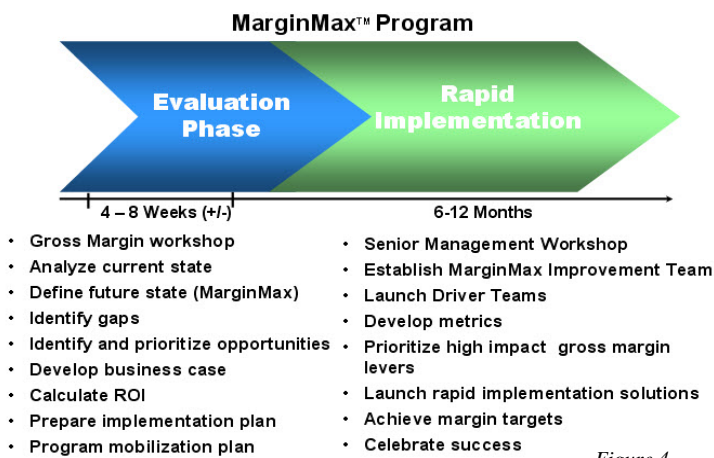


Figure 4