Commercial Policies: The Profit Booster That Protects Against Lost Margins

The importance of commercial policies in Life Sciences

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Rapidly evolving markets in Life Sciences are causing companies to take their best shot at adapting commercial models for competitive gain. Government pricing pressures and new product development designed to meet revenue expectations demand agility and quick time to market. Getting the commercial policy framework right should not be a shot in the dark. This is crucial, particularly for companies who want to develop products that meet revenue expectations because, on the one hand, there are smaller launches with smaller indication populations and on the other, there is increased scrutiny and challenge by consumers.

All of these changes are happening quickly and can potentially disrupt the progress and achievements that your company has made, especially when various initiatives unfold asynchronously, ultimately impacting your margin.

> **Therefore, the thinking must be "What is the right strategy?" and "How do we implement the strategy efficiently?"**

This is where commercial policies play a pivotal role in guiding your company by aligning initiatives and strategy while ensuring a positive impact on your margins.

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The WHO, WHAT and WHERE of commercial policies

Commercial policies...what are they? They are based on a commercial policy framework that refers to a set of guidelines, principles and regulations established externally, such as a government or governing body, to shape and govern commercial activities within a country while also aligning internally to company strategies. They serve as a foundation for economic growth and are critical in defining the rules and parameters for conducting business. To better understand a commercial policy framework at the highest level, read our blog: *Your Next Profit Booster: A Healthy Dose Of Commercial Policies Framework*

It's the business umbrella that covers the permitted trade term structure for discounts, customer advantages, service fees, logistic terms and financial terms.

Commercial policies can and should act as a general framework (cross-country and cross-business units), or local (specific to country and/or business units) and are, in general, approved by a committee.

A well-designed commercial policy framework will help your sales team gain agility while increasing customer relationships and customer satisfaction. If the sales team gains autonomy, they can provide better and faster customer negotiations and incentive offers.

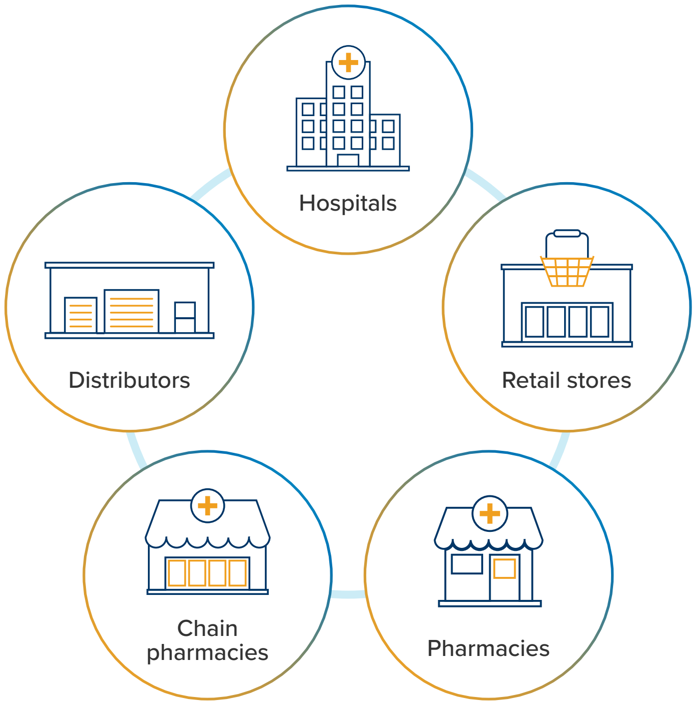
7 steps provide a healthy dose of profit protection

Moving beyond the basics of commercial policy framework boundaries will provide the strategies necessary to guide processes using commercial policies. This can provide the control you need beyond pricing and contracts by providing a profit booster. It's the shot in the arm your company needs to remain competitive.

1. Identify your target sales channels and customers

The commercial policy includes product target channels and customers. It should detail the approved routes to market. A route-to-market strategy outlines how your company will distribute its products or services to its target customers. It involves selecting the appropriate distribution channels, managing logistics and inventory, and implementing sales and marketing activities. A well-defined route-to-market strategy is essential for achieving sales and distribution goals effectively.

Your commercial policy framework should contain the standard sales channels and target customers, such as:



2. Defining the commercial terms

Once you understand who you are targeting and how you want to reach them, you'll want to define the terms that will meet that target's requirements. Understanding these requirements will help you avoid offering commercial terms that do not meet their needs and maximize your margin for that target or product. Determining which commercial terms you want to offer them requires planning and healthy communication within your company.

Benefit terms to consider include:

- **Discounts**
- **Free goods**
- **Special pricing**
- **Bundle offers**
- **Rebates**
- **Promotions**

3. Determine the allowed benefit types

When offering benefits, you want to attach terms that set guidelines that won't produce any adverse effects on your margins. Clearly outlining under which circumstances or conditions the benefit will be given is crucial to staying within healthy margin boundaries. There are 2 conditions of benefits to consider:

Conditional:
In the interest of both parties, you may want to offer a conditional benefit only provided under specific conditions or requirements. This can include your partner achieving a target, such as minimum sales, to benefit from the specific commercial term. You will also want to define whether it is based on sell-in, sell-out or sell-through.

Unconditional:
In Life Sciences, competition sometimes forces you to offer unconditional benefits. If that is your situation, aligning with all other steps is even more crucial to protecting your profits.

Either way you choose, you will need to determine the specific type of benefit, such as:

Lumpsum or fixed amount

Percentage and the base calculation

Cost per unit

Free goods

Service

Special financial terms
special payment terms with additional cash discounts for advanced payments

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4. Define the WHY of this benefit

In the previous step, you defined how you will offer the benefits. It's also essential that you capture the intentionality behind the benefit. More specifically than in step 1, you want to pinpoint which business stakeholders to target with the benefits mentioned. To do this, ask 2 questions:

- WHY should we offer this benefit?
- WHAT do we want to gain from offering this benefit?

These answers will be necessary for gaining a strategic view of your Gross-to-Net and shifting from a traditional view based on how you provide these incentives (on-invoice, off-invoice, etc.). Then, you can capture the WHY you are offering these incentives and what you want to achieve.

Gross sales	Example
Mandatory/statutory terms	Mandatory/statutory/ government pricing
Market access	Negotiated terms
Tenders	Tenders, price equalization
Commercial incentives	Product incentive, listing fee, etc.
Trade terms	Sell-out activation, customer sponsorship etc.
Incentives for supply chain players	WSD incentives, GPO incentives, etc.
Net sales	Net sales

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5. Identify common terminology

Suppose the purpose of the commercial policy is to define a common framework. In that case, it's important that you incorporate common terminology so everyone speaks the same language, with the added advantage of breaking down silos within the company.

When you determine boundaries or limits of what can be offered to a customer, you want the ability to measure the same. That means if a team wants to limit the discount that can be given for a set of products, the basis should be the same for all products. If this terminology is not agreed upon while making policies, some products could be based on list price while others are based on gross price or the ex-factory price, which is the same as the patient price.

6. Define pricing limits, corridors and margins

We're nearing the end of the 7 steps, and at the end of the day, everything you do is about revenue management. Depending on the company's maturity, you'll want to define pricing limits, price corridors and target price, and margin limits or target margin. Why? So that you can manage your revenue with transparency and accuracy. Companies using revenue management initiatives like these can build sustainable revenue and improve profit performance.

A new revenue mindset with margin at the forefront is needed. If your company requires the sales team to focus on maintaining a margin level, not just increasing unit sales, that team will approach discounts more profitably. Rather than offering higher discounts to secure more unit sales, the team will think strategically about when and how to incentivize a deal. Let's look at this example:

What happens when I give more discounts for closing a sale?

Margin before price decrease	Price decrease by...			
	-5%	-10%	-15%	-20%
30% gross margin	+20%	+50%	+100%	+200%
35% gross margin	+17%	+40%	+75%	+133%
40% gross margin	+14%	+33%	+60%	+100%
45% gross margin	+13%	+29%	+50%	+80%
50% gross margin	+11%	+25%	+43%	+67%

If you're considering giving a discount for closing a sale and you want to maintain the same gross profit, you should know how many additional unit sales are needed. You need to understand how total unit sales can drop (for a price increase) or increase (for a price decrease) for the gross profit to remain the same.

If you decrease your prices (a sale or discount coupons), how many more units do you have to sell to keep the gross profit the same? The numbers may surprise you.

Looking at the chart on the prior page, you see that if your product starts with a 30% gross margin and you want to offer a 20% discount for the closing, you need to sell +200% more units. That means selling triple the units initially planned to keep the 30% margin. If the incentives for the sales team were based on margin and not traditionally by units sold during a period, the story would be a bit different.

7. Consider guidelines for governance and approvals

Finally, defining the guidelines and procedures for creating, implementing, revising and maintaining the commercial policy will also be necessary. You'll want to consider how exceptions will be managed. Know the requirements for an organization to ensure that the commercial policy framework aligns with global and local company strategies.

When defining a commercial policy, it's important to remember the following elements:

Ensure processes are well-defined (creation and maintenance)

Create a governance model for aligning commercial strategies to company strategies

Manage exceptions at the global and local levels

Select an accountable organization at headquarters and local levels and a tool to support the organization throughout the process

The framework: 9 key reasons to give it a shot

1. **Consistency and standardization:** Commercial policies create a consistent approach to sales activities, ensuring they follow the same rules and guidelines. This consistency helps in building a unified brand image and customer experience.

2. **Clarity on sales objectives:** The framework outlines your sales objectives, targets and key performance indicators (KPIs). This clarity helps your sales team to understand what is expected from them and how their performance will be measured.

3. **Efficient decision-making:** Commercial policies provide a clear structure for decision-making in many sales situations. This empowers them to handle different scenarios effectively and make informed decisions that align with your company's goals.

4. **Customer focus:** A well-defined commercial framework emphasizes customer-centricity. It encourages the sales team to understand customer needs, tailor solutions accordingly, and build long-lasting client relationships.

5. **Risk management:** Commercial policies can include sales operations risk assessment and management guidelines. This helps the sales team identify potential risks, such as credit or compliance issues, and take appropriate measures to mitigate them.

6. **Alignment with other departments:** Commercial policies ensure that the sales team's activities align with other departments within your company, such as marketing, finance and operations. This collaboration fosters a cohesive and integrated approach to achieving overall business objectives.

7. **Adaptability and flexibility:** While frameworks provide structure, they also provide adaptability and flexibility. This enables your sales team to respond to changing market conditions, customer preferences and industry trends while adhering to the company's core principles.

8. **Ethical conduct:** Some commercial policies include ethical guidelines promoting fair and transparent sales practices. This helps build trust with customers and enhances your reputation.

9. **Performance evaluation and improvement:** With clear policies, assessing the sales team's performance becomes more accessible. Analyzing the outcomes against the predefined guidelines allows for continuous improvement and refinement of sales strategies.

Conclusion: Guiding sales and profit with the right strategy

Commercial policies play a critical role in shaping the future of Life Sciences commercial teams. They are essential for your company as they provide guidelines, rules and strategies that govern how the sales process should be conducted. These frameworks align the sales team's efforts with your company's overall commercial objectives and ensure consistency, efficiency and effectiveness in the sales process.

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Alejandra Garitonandia is an Industry Principal for Life Sciences at Vistex EMEA. Her expertise and passion are in revenue management for pharma, medical device and animal health. A background in medical and business studies led to an international career spanning a variety of positions in business and IT. She is an international speaker and leads Life Sciences industry-driven initiatives focused on complex topics and trends. Alejandra focuses on helping Life Sciences companies find their single source of truth where business processes meet IT systems to support efficient end-to-end revenue management.

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