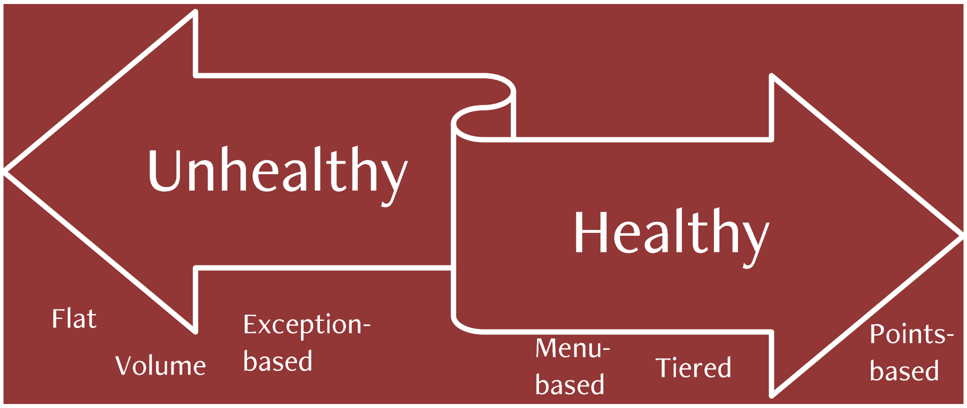
Channel Program Structure Alternatives—Why or Why Not?

A wide range of approaches to structuring channel partner programs exist. Historically programs were based on quantity or volume generated by the channel partner, or tied to revenue-based milestones, such as growth. However, the weaknesses (or inequities) of these approaches are well documented. Imagine your least committed channel partner getting your best deal because they happen to be in a large market, while your most committed partner is penalized because they serve a small or more challenging geographic region.

As a result of inequities like these, channel programs have evolved from volume-based to performance-based. Here we examine a range of program structures that are common in industrial and commercial markets.



Traditional Channel Pricing Structures—We consider the three most common forms of channel pricing structures "unhealthy" and highly risky. They promote channel (and manufacturer) behaviors that are misaligned with overall strategy objectives and can undermine your market position.

- Flat—Simply put, a flat channel pricing structure can be described as "communist" (i.e., designed to treat all channel partners equally). It is characterized by a flat discount or single channel multiplier. There is no recognition of exceptional, good, or even bad channel performance. While being easy to administer, this approach motivates the channel partner to minimize any investment in or commitment to your brand, as there is no risk/reward for doing so. The approach only makes sense when the channel role is solely transactional, or when your product represents a very small portion of the channel's total revenue (<1%).

- Volume—This "big dog" approach favors your largest channel partners. Channel pricing is highly linked to channel volume. The largest partners always get the best deal. The big dog approach does not recognize loyalty or commitment. In fact, for many suppliers their most loyal channel partners are smaller dealers/distributors who are always at a disadvantage vs. their larger competitors who have made little investment in your brand. Another drawback is that this approach often erodes street price (and potentially brand value), as big players pass on their pricing advantage to the street to "buy" business. The big dog approach best fits a highly concentrated market having few channel partners.

- Exception-based—The third most common approach is an "anarchist" model where there is very little structure or enforcement. Often evolving over years because of special pricing and "extenuating circumstances," the individual channel partner's price reflects how well they negotiated more than how well they represented your company in the market.

Unpacking Channel Program Structure Alternatives

"Healthy" Alternatives—More effective ways to structure a channel pricing program are being adopted by "best in class" suppliers in many industries. These "healthy" alternatives are rooted in a pay for performance philosophy. (Note that channel partner volume is <u>not</u> ignored, but instead volume is just one of many factors that these channel programs are based on).

- Menu-based—A menu-based structure is typically the first pay for performance model to which a manufacturer gravitates. Rather than abandoning the volume components of the pricing structure, a menu-based model adds factors for which a channel partner is rewarded. By exhibiting specified behaviors, the channel partner can "self-select" into additional quantitative or qualitative rewards. Examples of common menu-based items include prompt payment discounts, truckload discounts, and coop advertising funds. Each of these benefits is directly associated with a channel partner's activity, investment, or behavior.

- Tiered—A tiered program is another common iteration of pay for performance structures. Channel partners are given the choice of meeting specified sets of criteria to earn their way into a performance tier (e.g., gold, silver, bronze). Performance criteria consist of a range of management, sales/marketing, operations, and/or financial considerations. Tiers are differentiated by a combination of economics (e.g., pricing, rebates, etc.) and qualitative elements (e.g., access to new products, local marketing support, product allocation priority, etc.) that can be highly valuable to the channel partner's business.

- Points-based—The "state of the art" approach to a pay for performance channel program is a points-based system. In this type of program, a set of *mandatory* criteria are outlined for the channel partner. These business practices must be met for the channel partner to be considered for the program. Additionally, a set of *elective* criteria is incorporated. Each of the electives are associated with a value (i.e., number of points) that accrue toward tier standing. As in the tiered structure above, the higher the tier achieved the greater the rewards to the channel partner. One of the key benefits of the points-based system is the flexibility it provides. Each channel partner chooses a different path to achieve their target rewards level—allowing the program to be relevant for different geographic markets and under different growth opportunity conditions.

We have seen manufacturers make major gains in market position, revenue, and/or profitability by migrating to one of these healthy alternatives.

- One client improved its customer satisfaction ratings by over 25% as their new tiered program directly resulted in more channel partners investing in activities associated with delivering satisfied customers. The company also found that their customer retention rate and revenue gains correlated with the improvement in customer satisfaction.

- Another manufacturer struggled with position in the channel, often occupying a weak number two brand spot. A revised points-based channel program allowed this manufacturer to be viewed as a more channel-friendly (and more profitable) supplier, which resulted in significant share gains in the channel.

We have helped many clients optimize their go to market economics by structuring their channel programs to recognize the role the channel partner plays in your go to market strategy. If your team wants to be ready to roll out an impactful program in 2024, now is the time to start the redesign effort.

We would be happy to discuss your situation and our experience. We look forward to talking with you soon. Please contact Carl Cullotta at 224-239-2525 or cpc@lynncullotta.com. And for more on channel programs, see our series here.