PROFITABILITY ANALYTICS CENTER OF EXCELLENCE

eBook

# 6 Steps to Assessing & Improving Revenue Management Practices



Sponsored by EPMI

www.profitability-analytics.org

# INTRODUCTION

PACE's Profitability Analytics Framework integrates three bodies of knowledge relevant to an organization's profitability: revenue management, managerial costing, and investment management. In this eBook we focus on the first of these, presenting a six-step methodology finance and accounting professionals can use to evaluate and improve their organizations' revenue management process.

Revenue management does not go without attention in most organizations. Too often that attention is largely in the hands of marketing and sales managers without the support and expertise of management accountants and financial analysts. Yet revenue and cost management are two sides of the same coin. Neglect of one will hinder the other, and finance professionals need to understand both.

The methodology in this eBook can help finance professionals serve as effective partners with other business functions. It is based on a descriptive framework for revenue management that can be applied across all types of competitive organizations and industries. Implementation of this approach presents a competitive opportunity for organizations to invest in rigorous causal modeling, analytics, and systematic support of revenue drivers that can dramatically enhance value creation.

# 6 STEPS

Improving an organization's revenue management approach requires a cross-functional team, who need to make an initial assessment of the organization's current revenue, customer, and market practices; develop a revenue management system that is appropriate for the business needs; and then implement a system tailored to the organization's objectives and the needs of its various business functions.

In this eBook we show how this can be done using a six-step methodology that enables the finance and accounting function to serve as an effective partner with other business functions.

*"Modern organizations need cross-functional teams to manage the complexities related to managing revenue. Siloed thinking will not support the optimization of revenue. Management accountants play a key role in supporting revenue strategy development and implementation."*
*Dr. Julie Harrison*



**The 6 steps include:**

**Step 1:** Do a quick assessment of the organization's use of the four revenue management levers.

**Step 2:** Review levels of revenue management details to determine current practice and understand different intensities of practice.

**Step 3:** Analyze your organization's business strategy and business environment to find issues that can assist or hinder revenue management improvement.

**Step 4:** Evaluate revenue and cost driver importance in your organization's strategy and identify gaps in current managerial and accounting attention.

**Step 5:** Engage with other functional roles to design the appropriate level of revenue management and revenue driver attention for your organization, consistent with its strategy.

**Step 6:** As a cross-functional team, implement the new revenue management practices, supported by management accounting skills and tools.

# STEP 1

**Do a quick assessment of the organization's use of the four revenue management levers.**

In this first step, the goal is to evaluate how your business's context and practices affect the relevance for revenue management. Perform a quick assessment along the four levers of revenue management: pricing basis, inventory allocation, product configuration, and duration control.

Use the following questions to make the assessment, remembering that the more "yes" responses in any given section, the greater the importance and value to your organization from investing in revenue management practices.

*Pricing basis:*

- Do you tend to charge the same price for your products or services to all customers?
- Are your prices based mainly on costs and/or direct responses to competitor price movements?

*Inventory allocation:*

- Do you sell your products or services on a first-come-first-served basis?
- Do you charge the same price for your products or services during both high- and low-demand periods?

*Product configuration:*

- Does your product or service range require a wide variety of different resources to produce?
- Does your product or service innovation usually involve radically new products?

*Duration control:*

- Do you have the same operating procedures during both busy and slow periods?
- Do you accept variation in customer behavior as a given?

The greater the number of "yes" responses, the more you company can benefit by critically reviewing its revenue management approaches and the management accounting information provided across business functions.

# STEP 2

**Review levels of revenue management details to determine current practice and understand different intensities of practice.**

Now closely examine your organization's relevant revenue management practices. The starting point is to understand current business practices being used to manage customer demand and resources.

The table below describes different levels of revenue management practice based on the four levers. The appropriate intensity varies from company to company. Higher-intensity of practice is more complex and resource-intensive but potentially can have a greater impact on profitability. We find higher-intensity practices more likely to be employed by large organizations that have greater resources and operate in highly competitive markets.

*"The intensity of revenue practice will often reflect what works best for a given business strategy, level of competition, range of products or environment. But reviewing the level of intensity can help identify opportunities for improving revenue whether by changing pricing practices, more actively managing capacity, redesigning the product range or improving individual business processes."*
*- Proffessor Paul Rouse*



**Framework of Revenue Management Practices (Levers)**

| Revenue Management Practice | Lower Intensity (Level 1) | (Level 2) | (Level 3) | Higher Intensity (Level 4) |
|---|---|---|---|---|
| Pricing basis | Resource-focused | | | Customer needs-focused |
| | Pricing is primarily cost-plus or following not-for-profit objectives. | Pricing follows market standard prices. Limited variation in prices among different groups or area trends. | Pricing is strategic, aimed at a price point relative to the market. Pricing captures differences among groups or area trends. | Pricing is based on the value of specific product attributes. It captures differences among customer segments. |
| Inventory allocation | Ad hoc | | | Systematic |
| | No change or infrequent changes in price and customer priorities, often informed by unstructured judgment. | A fixed schedule determines how prices and priorities change over the year. These are across-the-board changes. | Periodic review to inform price and priority changes. Changes target groups of products and broad time periods. | Constant review to inform price and priority changes. Changes target individual products and specific time periods. |
| Product configuration | Physical differences | | | Nonphysical differences |
| | Offerings are made using diverse inputs and processes. Product range does not aim to segment customers. | Offerings vary in either inputs or processes. Radical new products are introduced as tactical responses. | Offerings are built from a set of core inputs and processes. Occasional use of radical new products. Product range is structured around add-ons. | New products are regularly created using existing core inputs and processes. Product range is structured around restrictions and add-ons. |
| Duration control | Reactive improvements | | | Stabilizing usage |
| | Initiatives target overall improvement or to speed up internal processes as problems arise without focusing on reducing customer variation. | Initiatives detect and alleviate bottlenecks. The focus is on internal activity, with indirect effects on reducing customer variation. | Initiatives actively mitigate the internal effect of customer variation. There is limited focus on changing customer behavior. | Initiatives regulate customer arrivals and discourage bespoke requests with a strong focus on changing customer behavior. |

The framework in this table applies across different business models, industry settings, and organizational structures. Each practice can be practiced along a continuum, with the scales shown providing a comparative view on how organizations choose to engage in management processes within each of the four revenue management practices (levers).

Note that higher intensity of practice is not always best. Managers must consider their strategy and resources with respect to their customers and competition to determine an “ideal” level of practice for each of the four revenue management levers.

# STEP 3

**Analyze your organization's business strategy and business environment to find issues that can assist or hinder revenue management improvement.**

A key issue when expanding revenue management practices is to identify how a business's context affects the four levers of revenue management practices. Revenue management does not look the same in all settings. You should establish appropriate levers of revenue management practice that will fit your specific situation.

Industry and business model characteristics arise from the type of product or service an organization delivers. These industry and business model features include:

*"For businesses today the distinction between goods and services is less important. What drives customers' willingness-to-pay are the things a product or service does that customers value. Not the form they take. If we can identify what different customers value, we can develop pricing structures and configure products that help maximize revenue."*
*-Professor Paul Rouse*

*Customer segmentation*
Customer segmentation refers to the ability to distinguish between the needs of different market groups, depending on how much variation exists and is observable. When there is clear variation in customer segments, it is easier to design products and services to encourage customers to pay a higher price.

*Perishability*
Perishability refers to whether resource capacity, or the products or services provided by the capacity, are sensitive to losing value over time. When capacity is highly perishable, inventory controls and pricing basis become more important.

*Varying demand*
Due to seasonal trends, special events, or demand patterns that shift across time of day, demand will often fluctuate more than supply. When there is high variability in demand, businesses have greater incentive to analyze trends and implement pricing basis and inventory allocation to maximize profitability during busy periods.

*Ability to charge varied prices*
Revenue management is impacted by differences in customer willingness to pay varying prices. That said, managing revenue using the pricing basis lever may be hampered in settings where prices need to be consistent to stay competitive, such as when selling commodity goods or services.

*Predictable customer duration*
Revenue management practices benefit from predictable customer duration. This predictability allows the business to plan and implement inventory allocation and to design product and service offerings to match customer needs and behavior

*Competitive environment*
Increased pricing and product transparency due to internet technology, as well as the pressure of recessionary trends, has heightened competition in many businesses. As a result, businesses in competitive environments have responded by increasing the level of detail in their demand and resource analyses and introducing more frequent changes to pricing and inventory allocations.

*Scale of business*
Larger organizations can practice higher-intensity levels because they have more resources available to invest in the required support systems. The reality of larger organizations reflects economies of scale, where a fixed cost of conducting revenue management analysis benefits a bigger scale of operations. As a result, smaller organizations without access to significant resources may employ less-intensive levels of these techniques, and this is quite appropriate.

*Growing and new organizations*
When a business is rapidly growing or newly established, variation in customer behavior may be more difficult to detect due to a lack of established history and because the organization's systems are continually developing during this phase. Failure to pay attention to appropriate duration controls until processes have been fully developed can lead to serious problems involving customer variation.

*Formalized organizational structure*
Managers in more formal structures are likely required to prepare regular reports regarding prior performance and expected future trends. Hence, more formalized structures are likely to be used for demand management decisions and to oversee resource management.

*Functional organizational structure*
Having a range of business functions requires more coordination to ensure staff is making changes that support revenue management practice as opposed to other business objectives.

# STEP 4

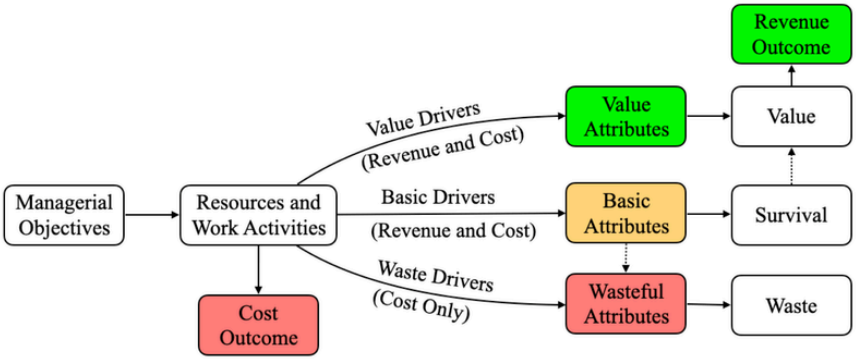
**Evaluate revenue and cost driver importance in your organization's strategy and identify gaps in current managerial and accounting attention.**

Revenue and cost drivers refer to identifiable parts of business operations, such as service outcomes or activities, that explain the amount of revenue earned or cost incurred. Cost drivers are used to help measure resource use or describe how operations and objectives cause costs. The guiding principle for cost driver modeling is causality, which is defined as the ability to reflect cause-and-effect relationships. This same guiding principle applies to revenue driver modeling.

The four revenue management levers should be assessed and managed using both a revenue driver and cost driver perspective. The figure below shows how revenue and cost are connected through resources and work activities that are used to deliver goods and services to customer segments.

Based on managerial objectives, organizations acquire resources and generate work activity with the goal of delivering value and achieving revenue objectives. All work activities in an organization require resources. Examples of resources include buildings, equipment, labor, inventory, and management.

**Revenue Driver Framework**




All revenue drivers are cost drivers but not all cost drivers are revenue drivers. Resources and activities increase revenue only by increasing or maintaining the value a customer receives from the product. Accordingly, only resources and work activities that offer value or basic attributes are revenue drivers. Resources and work activities leading to waste attributes should be reduced and, if possible, removed from the organization.

*"We have long appreciated the importance of cost drivers, but managing revenue drivers is paramount – every revenue driver drives cost, but not every cost driver drives revenue – if we place too much emphasis on cost drivers and costs we risk reducing revenue"*
*-Dr Julie Harrison*

# STEP 5

**Engage with other functional roles to design the appropriate level of revenue management and revenue driver attention for your organization, consistent with its strategy.**

To improve revenue management practices, organizations need to examine the types of data collected, the method used to collect data, and how data are analyzed. More intense data analytics, as shown in the table below, can help detect patterns in demand, incorporate a broad range of internal and external information, and improve confidence in decision making.

The analytical approach, types of data, and collection methods are the three main areas of data practice. Analytical revenue management relies on statistical models investigating causality to understand customer demand. This helps detect patterns in demand to inform pricing, yield controls, product offerings, and duration. Demand data includes data on customer and competitor behavior, together with demand trends and patterns.

Analytical revenue management relies on in-depth records of historical trends. Recording transaction details, operating performance, and customer characteristics for individual transactions enriches demand analysis. Analytical revenue management relies on accurate records of historical trends. Regular collection of transactional, competitive, and environmental demand data improves accuracy in demand analysis.

| | Intuitive | | | Computational |
|---|---|---|---|---|
| **Analytical approach** | Analysis is intuitive, relying predominantly on manager judgment and experience. | Analysis is mainly intuitive but informed by visualizations and comparisons. Ad hoc attention to revenue drivers. | Analysis blends intuition and formulaic techniques. Frameworks used to consider a range of revenue drivers. | Analysis relies on causality models, which systematically incorporate key revenue drivers. |

# STEP 6

**As a cross-functional team, implement the new revenue management practices supported by management accounting skills and tools.**

With a revenue management approach designed specifically for the organization's business context, cross-functional support is crucial to the final step of implementing a specific revenue management solution across the organization that is based on clear measures, aligned incentives, and coordinated systems and structure.

Many organizations are continuously improving and extending technology investments for other business needs. If the design of these investments can incorporate improvements in revenue management practices, then the incremental investment in technology for revenue management data gathering and analysis is more likely justified by benefits resulting from intensified revenue management practices.

*"Our client's finance departments observed an additional increase in value by adopting an EPM tool to analyze revenue management. EPM tools help identify Step 4 revenue drivers. Additionally, today's machine learning technology can help FP&A departments predict and prepare for their market's variability."*
*- Nihar Parikh, EPMI CEO & Co-Founder*



# CASE STUDIES

The following case studies describe two real companies (whose names have been changed to provide anonymity). These studies of a restaurant and a retailer provide examples of revenue management beyond the traditional ones found in the airline and hotel industries.

*"Revenue management practices are not the sole domain of large corporations or businesses in the airline or hotel industries. All businesses, including SMEs, can look at ways to adapt their existing business practices to better manage customer variability, or leverage differences in customer segments, or better optimize capacity use and business processes."*
*-Dr Frederick Ng*



# CASE STUDY 1

BigFood is part of an international fast-food company. It has more than 70 restaurants around the country and employs more than 2,000 employees. While part of an international franchise, BigFood management is relatively free to make strategic and day-to-day management decisions within broadly prescribed limits. Revenue-focused decisions are primarily centralized, with the marketing and operations department responsible for pricing, promotional activity, and product availability that are consistent nationwide. Restaurant-level managers operate within a structured set of standard operating procedures, although they have some scope to use store-specific promotional offers.

The company recently underwent a change in ownership, leading to a shift in business focus from controlling costs to managing revenue . This revenue focus incorporates consideration of competitor and customer behavior.
At the head office level, pricing and product availability decisions emphasize data collection and quantifiable results. Support for these decisions include financial analysis (variances and trends, and scenario modeling) and qualitative data collection (competitor site visits and benchmarking products).

## Revenue Management at BigFood

| Pricing Basis | Inventory Allocation | Product Configuration | Duration Control |
|---|---|---|---|
| Pricing is strategic, aimed at a price point relative to the market. Pricing captures differences among groups or area trends. (Level 3) | A fixed schedule determines how prices and priorities change over the year. These are across-the-board changes. (Level 2) | New products are regularly created using existing core inputs and processes. Product range is structured around restrictions and add-ons. (Level 4) | Initiatives regulate customer arrivals and discourage bespoke requests with a strong focus on changing customer behavior. (Level 4) |
| • Pricing is one of many levers of revenue management, complementing product mix and duration management.<br>• Changing pricing across the network is a costly and formal process. | • Product mix and drive-through emphasis are the main methods of prioritizing higher-value customers.<br>• Static menus and an inability to formally prioritize higher-value customers cause mismatches during different time periods and in different locations. | • Strong evidence that product range is linked with customer segmentation.<br>• Product range is created from a common set of ingredients and resources.<br>• Stores are required to follow head-office decisions about product range, but this intended product mix does not always fit at the store level. | • Head-office operations actively manage national systems used to regulate duration.<br>• The network formulaically controls standard operating procedures.<br>• Sample initiatives: Layout and equipment changes are being implemented to improve operations processes. |

# CASE STUDY 2

Independent Retailer is a stand-alone entertainment store that sells a range of music formats, gaming formats, clothing, and books. It is positioned as a specialty retailer, aiming to provide an immersive shopping experience. Compared to its larger competitors, Retailer maintains an extensive product catalog, preferring to compete through differentiation rather than price. This objective is achieved through a strong secondhand market, supplemented with an in-depth range of new products. Retailer is run by two owner-operators who oversee 27 staff employees.

Independent Retailer's use of the four levers of revenue management is shown in the table below. Revenue-focused decisions aim to balance the cost of processing a diverse inventory base and the benefit of price movements in response to demand patterns. This relies on a try-and-see approach using small, frequent orders to gauge product popularity and the need for price changes.

Decisions about pricing and product availability make strong use of item-level and product-level transaction histories. These data are collected using point-of-sale systems and inventory management software. Yet given the nature of the entertainment industry, there is also a strong reliance on manager experience to understand industry trends.

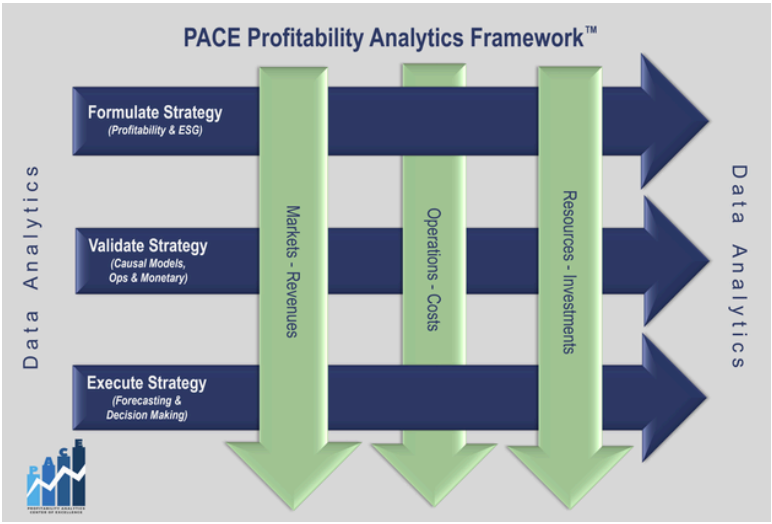
## Revenue Management at Retailer

| Pricing Basis | Inventory Allocation | Product Configuration | Duration Control |
|---|---|---|---|
| Pricing follows market standard prices. Limited variation in prices among different groups or area trends. (Level 2) | Periodic review to inform price and priority changes. Changes target groups of products and broad time periods. (Level 3) | Offerings vary in either inputs or processes. Radical new products are introduced as tactical responses. (Level 2) | Initiatives target overall improvement or to speed up internal processes as problems arise without focusing on reducing customer variation. (Level 1) |
| • New products are first priced at cost-plus. The price is adjusted for popularity when the product is restocked.<br>• Some evidence of differential pricing by customer segment; this is in the form of a club member program. | • A try-and-see approach is used to incrementally move prices of new product. This is based on speed of stock out.<br>• A business model of small, frequent orders determines the appropriate yield control methods.<br>• Yield control methods are chosen to balance the cost of processing stock and the benefit of price movements. | • The business model has evolved from a second-hand shop "discovery" experience toward a deep-catalog "comprehensive" experience.<br>• Working capital cost of maintaining a deep catalog is controlled using small order sizes. This may require more staff costs than if larger orders were used.<br>• Cost of certain promotions and products is prohibitively high due to the nature of the market and customers. | • Customer behavior is relatively stable in this retail environment. Accordingly, fewer duration controls are needed. |

# SUMMARY

Implementing more sophisticated revenue management techniques is providing companies with a competitive edge. Implementing these techniques requires a cross-functional team, on which accounting and finance can play an important part. By following the six steps here, you can help enhance the long-term revenue value of your organization.

Revenue management is an integral part of the Profitability Analytics Framework. The framework also encompasses cost and investment management. By holistically addressing these three levers of profitability, organizations can help ensure their future success.



# OUR SPONSOR

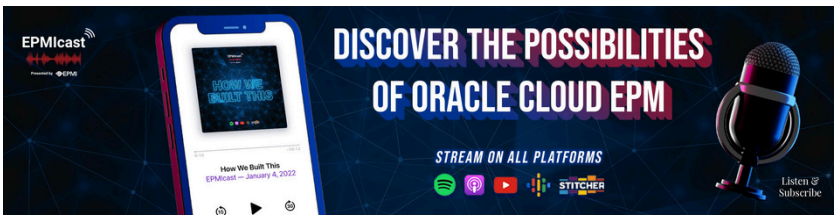
**About EPMI**

EPM Intelligence (EPMI) is a Houston-based systems integrator that leverages EPM technology to streamline business processes for organizations around the globe.

Working with Oracle and PACE, we partner with finance and accounting teams to gain efficiency by automating the budget process, reducing days to close, and enabling robust reporting.

With over a decade of experience across industries, we build solutions for organizations of all sizes.

Follow EPMI on LinkedIn and stream our industry-leading podcast, EPMIcast, for the latest EPM thought leadership.




Contact us: info@epmi.com
Website: https://epmi.com

Now that you know more about the PACE Profitability Analytics Framework, we invite you to explore the Profitability Analytics Center of Excellence Library for podcasts, webcasts, case studies, and articles.

Contact us: info@Profitability-Analytics.org
Website: profitability-analytics.org

©2023, 2024, 2025, 2026 Profitability Analytics Center of Excellence. All Rights Reserved. Permission to quote, reproduce, and disseminate granted provided appropriate attribution is given.