Lessons from selling adventures

A different approach to Business Analysis

Disclaimer:
The points made here are inferences based on personal experiences, please do your due diligence before applying these to your unique investment scenario.

Congruence Advisers

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Real world selling experience for almost a decade

Learning it the hard way

Tangible offering matters – however intangibles matter equally (sometimes more)

More the number of decision makers involved – greater the complexity of selling & higher the entry barriers (direct implications for duration of the sales cycle)

High switching costs occur when customer usage/habits are linked to the offering

Relationship based pitch too early in the sales cycle indicates a non differentiated offering

Charging a premium is easier than it sounds if the customer sees value

Difficult to pinpoint the core value add in intermediation businesses at first look

How salesmen spend their time is a lead indicator of how the business will pan out over the medium term

How can selling experience make one better at business analysis

The Customer perspective to any business

Buying process & Implications for businesses

How to use this in business analysis

Determining factors & categories

Fitting this into the business evaluation model

Incorporating this into the research process

Customer buying process & Implications

Shortlist

- Brand Recall
- Past Experience
- Association
- References, credentials

Objective Evaluation

- Tangible points of difference
- Product Fitment
- Templates & Checklists
- Cost Benefit analysis
- After Sales service

Decision

- Cost Vs Value
- Social pressures
- Intangibles – Trust, ease of doing business, incentives

Brand name & associations tend to assume greater importance in business segments where tangible points of difference across alternatives aren't substantial

Mismatch between the perceived importance of the Objective Evaluation stage and what actually happens on the field

In enterprises senior management usually get involved in the Decision stage while the Objective Evaluation stage is left to mid level managers & the Shortlist stage more or less runs on autopilot

Emotional aspects of decision making dominate the Shortlist & Decision stages

Tangible offering matters a lot in the final decision but can be a lower weightage in certain segments

One usually needs to look for combinations (multiple things working in unison) to be able to answer why some companies succeed while others fail.

Business Evaluation – Key Questions

What enabled the entrepreneur to build the business in the first place?
Important to take a story line & contextual approach, most things are a factor of time & place.

- Knowledge gained by working for someone else (AIA Engineering) or from markets that are more advanced (Amara Raja Batteries)
- Ready relationships one can tap into and create the customer base (TCPL Packaging)
- Commodity business that has evolved/evolving into a value added business over time (APL Apollo Tubes, Garware Wall Ropes)
- Tie up/JV with a foreign entity that is willing to bring technology while the local partner manages operations (Auto ancillary value chain)
- Beneficiary of an industry tail wind/an idea whose time has arrived (IT Services, E-commerce)

This is a good place to start when one is looking to identify entry barriers

What kind of customer relationships will the entrepreneur need to run the business well?
Direct Sales - How many touch points within the customer organization? At what level?
Channel Sales – Where does the power balance lie in the relationship? Most distributors work on the empanelment model since 1) much easier to run ops when the vendor list is consolidated 2) incremental effort for sales is optimized 3) better terms with higher volumes per vendor

How easy is it for customers to switch to alternative offerings?
Switching involves steps – access alternatives, evaluate & decide (needs incentive to shake out of inertial loyalty)
It is easy to dismiss most businesses on this parameter, think deeper. Understand the role of intangibles in the decision making process, other than fast moving goods all other brick and mortar businesses have elements of switching cost (do marginal differences in cost and quality make for enough incentive to switch?)

Business Evaluation – Key Questions

Is this a business enabler or a business driver? (e.g. residential real estate)
Customers tend to spend less time negotiating with business enablers since proportion of cost towards this is lower

How high is the annuity/repeat component of the business? (e.g. auto ancillary, packaging)
Higher this component, more the emphasis on reliability, relationships & ease of doing business, pricing will always be a challenge. However minor improvements by competition cannot take business away

Is the industry structure consolidated or fragmented?
Consolidated structure implies stable pricing, too many players entering means volatile pricing and business terms are experimented more

What is the extent of product/service differentiation among the key players? (e.g. Ceramics)
Lower the tangible differences, higher is the component of intangibles in decision making

Does the offering have a setup service attached to it?
If yes, the stakeholder performing the service becomes a key influencer in the customer buying process (e.g. system integrators in IT, fabricators in steel pipes, work technicians for plywood)

Has the business traditionally spent more on ATL or on BTL?
Usually a tell tale sign of the power balance between the OEM and the channel. Also analyse how this mix has been changing over the period, usually a good way to detect changing power balances and transitions

Any traction on concentrated buying centres emerging as an intermediary?
Look for presence of network effects in any emerging intermediation model, if so be very wary

Process – Combine common sense with multiple iterations

Understanding of what factors drive customer decision making	Appreciate intangible elements of the buying process You may not have in depth understanding, just be logical in your approach and use common sense Start with the ground reality and hypothesize why it could be that way
Study company genesis and how the business was started	Make notes on what enabled the entrepreneur to start off What skills did he have handy when he started off Those are the most likely entry barriers to the business
How does the sales model work? What kind of relationships are needed?	Direct Sales works when the payoff/deal justifies the cost Channel sales when customer are distributed and payoff/deal is way lower Appreciate how distributors work and the constraints they deal with
Understand competitive landscape & how switching could work	Switching process – evaluate how easy/difficult it is from customer perspective and what incentives are needed Make notes on why the customer may/may not want to switch
Checklist based industry analysis	Use this to challenge existing assumptions using real industry numbers & trends By the time one gets to this stage, a basic framework of the quality of the business and inputs for the moat analysis are in place Rest of the details to be filled in through field work

Key Learnings

The customer perspective is usually the best perspective to view any business. Most stock analysts do not understand this perspective as well as business people do. If you have run P&L in a professional company, you have a better chance of cracking this than most analysts

Competitive advantages are a factor of time, place and multiple things working in unison. One can at best have a framework ready for analysis but the analysis needs to be deeper and consider various perspectives. Always take a storyline approach, this ensures one isn't too theoretical

Brand + a sticky distribution channel in a consolidated industry structure is a very powerful moat. Usually the tangible points of difference across offerings are low here and intangible factors in customer decision making dominate

Understand that the enterprise selling cycle is very long. A well entrenched market player in a segment that is characterized by infrequent technology changes has likely built a customer base that suffers from inertial loyalty (this by itself is a switching cost)

Always invert when you analyse, things are usually the way there are for good reasons. Hypothesize on what these could be, over a period of time one can make sense of things. The road less travelled is less travelled for a reason

Using a checklist helps ingrain thinking patterns till they become drilled in

Unless one is able to translate the qualitative analysis into tangible inputs to the valuation model, all of this becomes any exercise in theory. Business projections/Reverse DCF are ways of doing this