MFL THE PRICING TIMES

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MFL Lesson's Learned—CEO's Do's and Don'ts of Good Pricing

There is no easy business today. The obvious and intuitive ways to improve profits are gone. You have cost-reduced, outsourced, gone lean, found all that free quality, searched for excellence and been a one-minute manager. Today every CEO faces the hard reality of customers who have become better buyers, demanding more for less and comfortable using new, sophisticated and tough-minded approaches to find great suppliers who are willing to provide a richer offering at a lower price. At the same time, competition is investing in new capacity and new capabilities, not just in their own back yard, but in every part of the world. In response to these challenges from customers and competitors, your organization is working more productively than ever, producing much better products at lower costs with fewer people. However, you know in your heart that, based on the value you deliver to your customers, your returns should be higher.

You are right. We have found that most businesses have a significant opportunity to use pricing to improve both revenues and margins at the same time. This opportunity exists because most businesses instinctively think and act first from their internal product, technology, and operations perspectives, often causing them to under-resource, simplify, and isolate pricing. This "inside out" perspective makes it difficult to understand the real value customers receive and perceive from your products and services, limiting your ability to set, communicate, and collect a fair price. Pricing is the sum of judgments made by many people at many levels within different functions of an organization. We have found that organizational pricing capabilities, judgements and impact can be improved and sustained by applying a few basic concepts and approaches consistently, insightfully and strategically.

A first step toward better pricing for a CEO is to walk into the offices of your heads of sales and marketing and ask them, "Are we doing as good a job as we can in the pricing area? Are we leaving money on the table?" Of course, the answer you are likely to get is, "Boss, we're doing a great job of pricing, in fact we always get the premium price. We know that because our competitors are consistently making offers 3%-7% below our best price. And more importantly, we're out there on the street every day. We know the market and we price at the market." On top of that, if you ask your key sales and marketing people what they could do to improve pricing, they'll respond, "We don't have time or resources to invest any more effort in this area." They will say they need to focus on new products, new customers and cost reductions. All of these responses are not only natural, but in some respects correct. However, from the CEO's perspective, they are signals that there are significant pricing and profit opportunities to be identified and captured.

Some Do's and Don'ts from a CEO Perspective

DO get involved in establishing, reviewing, and approving pricing strategy on a frequent basis.

DO ask for detailed analysis of price decisions, especially pricing analysis on won as well as lost orders.

DO push to understand your pocket price (what you truly receive after all discounts, rebates, special deals, give backs, etc.)

DO encourage your organization to constantly identify and close price leaks (unintended price cuts, and/or extra features/services not reflected in price).

DON'T Get involved with day-in and day-out tactical pricing decisions – you will always be pushed to cut the price.

DON'T accept summary pricing analysis or typical accounting results based on averages and allocations.

DON'T expect analyses of invoices, list prices or average discounts to reveal your real economics or messages you are sending to customers.

DON'T give away your hard-fought cost reductions and productivity gains by passing them completely on to your customers.

DO	require that your entire organization understand all four elements of the value equation involved in each type of buying decision (value = benefits – tradeoffs – switching costs – price).	DON'T	accept the belief that low price is a benefit or that you need to lower your price on a permanent basis to overcome one-time switching costs.
DO	ensure that every pricing strategy and tactic fully considers the integration of the price level, timing, and communication.	DON'T	neglect the importance of managing the timing of price changes and carefully crafting the way price, and price information, are delivered.
DO	recognize the power of aggregated versus disaggregated pricing in order to tightly relate the benefits perceived by customers with the price they perceive.	DON'T	commoditize your business by using simplified or industry standard price mechanisms such as list prices and discounts.
DO	get heavily involved in the elements of pricing strategy, including the pricing goals for all audiences, pricing policies, pricing segmentation and strategies by segment.	DON'T	allow pricing strategy development to be an afterthought to the development of a strategy for introducing new products.
DO	align your organization's incentives to support better pricing.	DON'T	permit performance metrics to drive poor pricing decisions or prevent the learning necessary to improve pricing judgment at every level.
DO	make sure that people at every level and function in your organization understand the basic principles of good pricing and are responsible for proper execution of any pricing element they can impact.	DON'T	permit pricing to be a "black box" kept carefully under wraps and in the sole control of either sales, marketing, or finance.
DO	invest in the skills, systems and style necessary to make good pricing the tool that allows you to capture your fair share of the value you deliver.	DON'T	view pricing as an administrative function that is a necessary evil or permit your pricing approaches and flexibility to be constrained by systemic limitations.

The challenge that we faced as CEO's is the same that you face every day—too many high leverage opportunities and significant problems with too few resources. Yet every CEO knows that there is no more powerful lever in their arsenal than pricing to simultaneously increase revenues and increase margins by leaving less volume and less money on the table. These gains can be sustained by managing and evolving the fine art and science of pricing in the same way that we look at all of our operations – as an opportunity for continuous improvement. This is done through the creative application of basic principals by talented people who not only understand what it takes for your customers to be successful but also know both their role in providing the benefits necessary to ensure your customers' success and how to capture your fair share of the value you deliver.

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MFL's consulting practice focuses on helping our clients build margins and volume by capturing their fair share of the value they deliver to their customers. We have found that pricing, while often managed in isolation, can be a powerful and integrating lever to drive a necessary shift in mindset and capability.

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