MFL THE PRICING TIMES

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DON'T COMMODITIZE YOUR BUSINESS

Now more than ever, great pricing should be a CEO's top priority. The business world as we have known it has all but disappeared, leaving us with a host of new challenges.

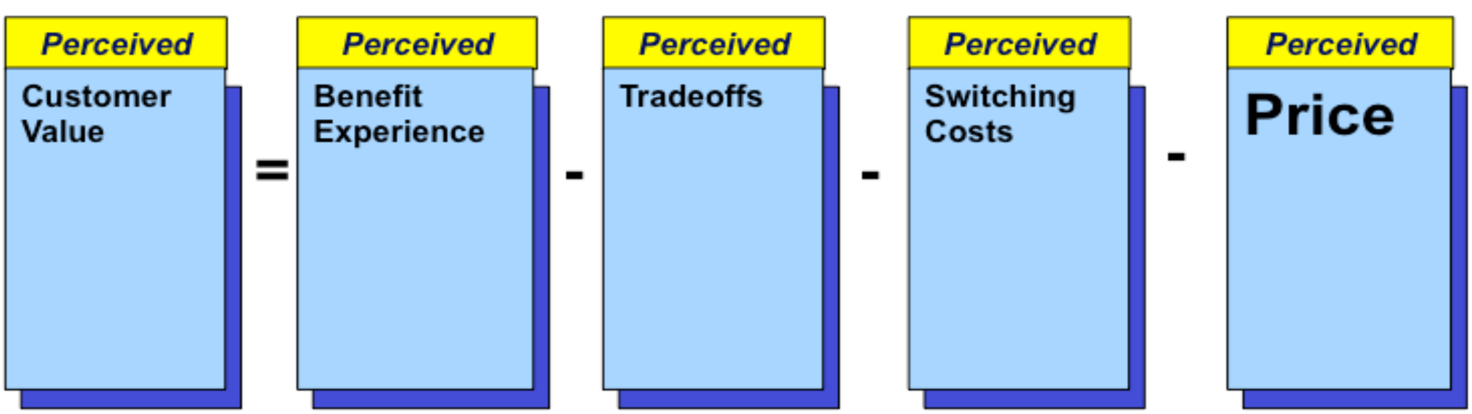
- Demand is recovering, but customers' needs and expectations are shifting.
- Aggressive buyers have strengthened procurement capabilities and gained online access to product and price information.
- Pressure from global competition with labor and other cost advantages and excess industrial capacity continues to cause disruption.
- Everything is more volatile; oil, commodities, other raw materials, and the dollar.
- Major cost reductions from lean, six stigma and staff cuts have already been captured.

In the face of these challenges, too many businesses ignore the power of good pricing and continue to follow conventional wisdom by further slashing costs, cutting price, and doing almost anything they can to gain volume. Yet unless they are (and can remain) THE low cost provider in their industry, these actions will have the unintended consequences of commoditizing their business—and very likely starting or supporting a price war.

Why do so many companies fall victim to the conventional wisdom? All too often functional leaders have the mindset to respond to the current environment with cost cutting and volume increase practices that can destroy, not build, profits. For example,

- Sales says: "Any order is a good order," which results in a plant full of low-margin and non-strategic products.
- Sales also says: "We should cut the price on business we cannot win to punish the competition," which leads to a price war as competitors' perception of your price is largely based on what you do at their best accounts.
- Marketing says: "We should focus on big accounts because we do not have the time or resources to spare on smaller business," which has the consequence of limiting growth by walking away from low-competition, high-profit orders.
- Operations says: "Complexity is bad as it only leads to higher operating costs," which means you walk away from the profit from accounts that are willing and able to pay for a customized offering.

Why and how do these mindsets cause profit declines instead of increases? For the answer, we turn again to our old friend the Value Equation. When you look at your business from the outside-in—from your customer's point of view—as opposed to from the inside-out, you see how many conventional wisdom business practices reduce the benefits customers receive, causing them to view your offerings as undifferentiated commodities worth a much lower price.



In tough times, conventional cost-cutting measures often run counter to effective value delivery and can reduce, not increase, profits.

Conventional Cost-cutting Measures	Simplify and narrow offering
	Reduce direct sales and application engineering staff
	Reduce inventory and lengthen lead times
	Reduce marketing expenses
Impact the Value Equation	Reduction of real and perceived benefits
	Increased perceived tradeoffs
	Reduction of perceived switching costs
Negatively Effecting the Bottom line	Downward price pressure
	Lower switching costs
	Greater risk of losing existing accounts

We are not suggesting, of course, that you avoid taking tough actions to reduce costs. Rather, we have found that investing time and resources in good pricing practices done in parallel with using an outside-in perspective for evaluating internal cost cutting measures maximizes a business's opportunity to capture its fair share of value delivered.

Good pricing starts with understanding your customers' business challenges, application economics, and switching costs. This understanding also permits you to evaluate your internal cost reduction actions and choose the ones that reduce costs without reducing benefits delivered to customers or reducing their switching costs. At the same time, a solid understanding of your customers' business challenges and application economics also gives you the ability to communicate the added value they receive from your offering and to more confidently, and successfully, command a price that aligns with those benefits.

The key to creating this opportunity to grow profits in these tough times is to ensure that mindsets across your organization are refocused from an outside-in perspective so that you can avoid the pitfalls of following conventional cost cutting wisdoms—especially those followed by your competitors. As a result, your customers will receive and perceive your superior offering and have the willingness to pay a fair price for the value they receive.

The MFL Group

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 focus first on helping our clients view their business from the "market-in" as a way to clearly understand where and how to compete most successfully. We then focus on improving pricing because, while often under managed or managed in isolation, pricing is a powerful and integrating lever that can drive a profitable shift in mindset and capability across all functions of a business. The end products for our clients are enhanced abilities to develop winning and sustainable strategies and pricing approaches and capabilities resulting in signifigant top and bottom line growth.

Our extensive consulting experience at McKinsey & Company and MFL, combined with our line general management experience, has enabled us to help our clients sustainably improve profits and growth by building their organization's capabilities to increase and capture a larger share of the value they deliver.

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