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In Brief—Sweating the Price

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Nothing is more contentious in a company than prices. Those on the front lines would usually like to see a lower price so that they can close more sales and move more units. Those in operations would prefer to see high prices to cover the costs. Finance enters and they too want to see upward pressure on prices to shore up profits. Enter the profession charged with balancing all these factors and managing the value proposition, and marketing squares off with all sides to create a rational price structure.

In the past few months, economic indicators have repeated the depressing news of downward price pressure. Even the financial wizard himself, Alan Greenspan, lamented not too long ago that firms are having difficulty exerting upward price pressures. Yet, on September 18, 2002, the Wall Street Journal ran a front page article concerning the current move to improve prices– charge for the little things and control discounting.

First, in an effort to keep pricing structures simple for customers, many B2B businesses had set a single price structure for all of their customers. When a customer had a special request along with the request for the usual product or service, the business would sell the entire package using the same pricing structure. Unfortunately, this approach to pricing fails to capture the extra costs associated with meeting the unique demand of the customer. This special request could be as simple as 500 of the usual 2 inch fasteners and 10 special 1 and 3/4 inch fasteners, or it could be 1000 licenses of your usual software but with one change to the labels of the fields. Either way, the special request of the customer doesn't look like it would have a large effect on costs and prices, but it can. And, if the customer values this special request, they should be willing to cover the extra costs required to meet their demand. This marks an improvement in marketing in capturing value by meeting special customer demands while also charging more for them.

Second, in an effort to keep customers and close more deals, many B2B sales have been discounted to beat competitors. Pricing to match competitors is a common tactic. Regardless of the type of company you are in, you know that your prices cannot be too out of line from those of your competitors. Any differences between your prices and your competitors must be matched by a difference in the perceived value offering. However, businesses are no longer taking their customer's word for it when they claim that their prices are too high. Instead, businesses are using discipline, supported by market research, to hold prices at a level that appropriately captures any value difference between their product and their competitors.

Neither of these ideas is really new. If the marketing department had been managing prices appropriately in the past, they would have been doing these things all along. At a theoretical level, prices for all goods and services should be set somewhere between the costs to produce the value offering the benefits captured in consuming the value offering. Yet, somehow, this simple dictum has been lost along the way. Or, at least, the details of the dictum had been lost and the organizational structure was unable to meet the demands for sound business decision making.

Managing prices is not a simple matter nor is it a trivial matter. Missing the mark can put a business under. For instance, consider Beloit Corporation that was one of the top three producers of high-value paper manufacturing machinery. They went bankrupt in 2000 due to improper pricing. This fate can be avoided however.

The immediacy of the need to close the sale must be countered with the need to manage profitability. To do

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this, best business practices in B2B firms indicate that business should create both a strategic pricing group and a tactical pricing group. The strategic pricing group is charged with creating an overall pricing strategy as well as a detailed price list or pricing mechanism, often on an annual or quarterly basis. The tactical pricing group is charged with reviewing single sales opportunities and making price adjustment accordingly on an ad-hoc basis.

Many customers of B2B businesses are unique and the uniqueness of a single sales opportunity may require alterations to the standard pricing strategy. To handle these issues, a tactical pricing group is required to make decisions alongside the strategic pricing group. The tactical pricing balances the overall pricing strategy with the unique requirements uncovered by the salesperson of a single sales opportunity. While the tactical pricing group must be held accountable to the strategic pricing group, it also needs the latitude to make independent decisions.

This two tiered approach to pricing is used by many small and mid tier B2B firms. While it doesn't remove all the contention in setting prices, it does appropriately manage the price setting function. In pricing, it does pay to sweat the details.