



Pricing for Long-Term Profit and Growth (Part III of III)

By Jim Saunders

In Parts I and II, we established the framework for performing price optimization to maximize long-term profit, by looking at the Customer Lifetime Value and the impact of pricing on the possible future outcomes. We also discussed how the

“Price/Volume/Profit Tool”, a vital element for achieving Level 3 of the World-Class Pricing framework (www.pricingsolutions.com), links to this model. In addition, we also delved into the available margin pool and extracted a number of factors that could affect future profitability from a pricing management stand point. In this newsletter, we will discuss how to grow volume profitably in a long-term price optimization model (see *the profit/growth model in Figure 3*).

Ultimately, the optimization of both everyday prices and promotions leads pricing managers to focus on segmentation. More effective segmentation, as well as a pricing structure that responds to the needs of specific segments, provides an opportunity to improve both growth and profit in the long-term – the “Holy Grail” of pricing. Figure 3 (page 2) shows the range of potential impacts that a pricing move can have. A move that takes the company up the vertical axis (such as a price increase) can increase profits but does not improve value and may, in fact, hurt the long term future of the business. Similarly, a promotional move that entices new customers, (e.g. temporary price reduction), but does not link customers to the value of the brand can grow the customer base, but possibly



trains these customers to wait for future promotions leaving them unprofitable.

While many companies in recent years have adopted initiatives to improve pricing management – typical starting points include implementing price increases or more effective management of promotions and other discounts

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– the real opportunity lies in the ability to segment customers based on their willingness to pay, and introducing a revised pricing structure that caters to the needs and constraints of each. If we return to the example of the bank savings product, the bank had taken a “one-rate-fits-all” approach. However, analysis of the cost structure revealed that high-balance customers were extremely expensive to replace if they were to leave. A change to the bank’s pricing structure allowed it to offer premium savings rates to premium clients. The reduction in lost volume led to a healthy growth in assets, while a reduction in the required acquisition costs improved the bottom line.

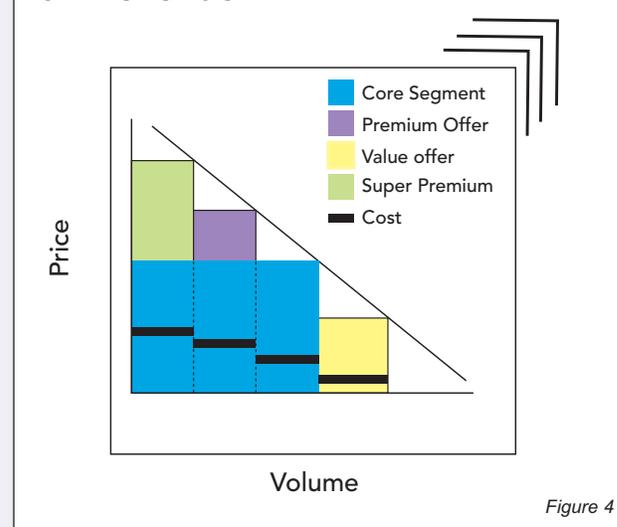
If we think about price structure changes in terms of “willingness to pay,” the opportunity becomes clear. Figure 4 (to the right) shows a simplified demand curve where we have plotted willingness to pay as a function of different

customers who did not buy because the offer was too expensive, respectively. If, through effective segmentation and price fencing, the company can offer a new price structure, as shown by the addition of the green, purple and yellow rectangles, the revenue opportunity will grow, and the money left on the table will shrink. A pricing manager should structure the offers so that costs to service customers decrease with decreasing willingness to pay – but that’s a topic for another article.



market segments. In the simple case where the company has one offering at one price, the available revenue is represented by the blue rectangle. The revenue “left on the table” is represented by the two triangles (above and to the right of the rectangle). These are the customers who were willing to pay more but were not given that opportunity, and the

The Effect of Price Structure on Revenue



In this article, we have presented examples and a framework for maximizing long-term profit and growth. Unfortunately, too many pricing managers fail to consider more than one of the trajectories in our profit-growth model. Yet, our work has consistently demonstrated that innovation in pricing structures offers one of the most powerful opportunities for a business to grow and be profitable in the long run.

To access the entire article, please go to our website, http://www.pricingsolutions.com/the_newsletter.cfm under “Pricing for Long-term Profit and Growth”

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Frugal is the New Black *By Paul Hunt*

Positioning your company as the smart choice in the tide of consumer and corporate thrift.

Conspicuous consumption is passé. Nowadays, frugal is the new black. Cheap is chic.

The value calculus for making purchases has changed. There is a much sharper focus on price. People are re-evaluating everything before laying out their hard-earned cash. Consequently, it's a dangerous time to be the high-priced player in any category, as Starbucks is learning the hard way. While the once high-flying chain is closing stores and trying to figure out how to avoid being seen as an unnecessary luxury, consumers are flocking to McDonald's for its inexpensive, yet tasty, coffee.

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The story is no different in corporations. Finding ways to conserve cash and still get the job done is the new modus operandi. Insurance company AIG, the current poster child for corporate excess, has not grasped this concept, and is paying the price for its arrogance. Holding corporate events at four-star resorts and doling

out hundreds of millions of dollars in bonuses while at the same time accepting taxpayer bailouts has provoked public outrage. It's like wearing bling to a funeral – ostentatious and insensitive.

In the B2B market, every purchase and expense is now viewed in the context of: "could we have done that cheaper?"; or, "rather than outsource that requirement, could we have done that ourselves?" The focus is on preserving cash and, in turn, jobs.

Companies are still making purchases for "strategic initiatives," and if you are fortunate enough to be selling something that is defined as strategic, you may still get top dollar. But don't count on it; these products and services are few and far between.

The much wiser approach is to "ride the rapids" of frugality, to make sure that you're the new black and, in so doing, position your company as the smart choice.

Here are some ways to accomplish this:

- reposition your value proposition to demonstrate why it is frugal to buy your offering (e.g., unbundle, provide tiers of offerings with a sweet spot for the frugal buyer);
- sharpen the focus of your messaging (i.e., would Scrooge approve?)
- reward loyalty (e.g., reward your best customers with unique ways to save money).

Paul Hunt is President at Pricing Solutions Ltd. To reach Paul, please call 416-863-0685, ext. 121 (as of July 15, 416-943-0505, ext. 121) or email him at phunt@pricingsolutions.com.

Pricing Research Practice Update

Greg Thomas, Leader, Pricing Research Practice, reports that Pricing Solutions is experiencing high client demand for our pricing research services. According to Greg, "Our new and existing clients recognize the need for pricing research to be conducted by highly specialized pricing experts such as Pricing Solutions, particularly in this challenging economy with changing consumption patterns."

The Pricing Research Practice is also proud to announce the successful completion of the Marketing Research and Intelligence Association's Gold Seal Certification Review process, <http://www.mria-arim.ca/MEMBERSHIP/CorporateGoldSealProcess.asp>, and our new designation as a Gold Seal-Certified Corporate Research Agency. The Gold Seal Certification is one of MRIA's primary mechanisms for developing and delivering world-class professional standards and ensuring member compliance. This achievement demonstrates Pricing Solutions' continued commitment to excellence.

To discuss how we can apply our pricing expertise, innovation and collaborative approach to your research projects, please contact Greg Thomas, Leader, Pricing Research Practice at 416-863-0685, ext. 120 (as of July 15, 416-943-0505, ext. 120) or email him at gthomas@pricingsolutions.com.

News and Events

Webinars

June 25 – Design to Value –
“Leveraging Customer Value Intelligence
to Design Better Products & Services”
with Loic Le Corre, Managing Director,
Pricing Solutions Europe

September 16 – “Competing on Pricing
Analytics” with Loic Le Corre, Managing
Director, Pricing Solutions Europe

17:00 to 18:00 CET • 11:00 to 12:00 ET

Visit www.pricingsolutions.com
to register.

Seminars and Workshops

June 15 – The Canadian Institute’s
3rd Annual Drug Pricing &
Reimbursements in Canada
Conference, Pre-conference Workshop,
Toronto

“How to Make Effective Pricing
Decisions” with Paul Hunt, President,
Pricing Solutions

Inquire about our Special discount for
Pricing Solutions clients when
registering for the Conference at
www.canadianinstitute.com

October 13, 14 – FMCG Pricing
Excellence Seminars, Paris

with Loic Le Corre, Managing Director,
Pricing Solutions Europe

Contact llecorre@pricingsolutions.com
for details.

October 21-23 – PPS Annual Fall
Conference, Orlando, Florida

“Pricing 2.0 – The Next Generation of
Pricing Management” –

Keynote Speaker –
Paul Hunt, President, Pricing Solutions

“Effective Pricing in Latin America”,
Fernando Ventureira, Iberia
(Spain & Portugal) Practice Leader

November 25-26 – PPS Annual
European Pricing Conference, Brussels

“Pricing 2.0 – The Next Generation of
Pricing Management” –
Keynote Speaker – Paul Hunt,
President, Pricing Solutions

“Measuring & Managing Pricing
Effectiveness” (CPP Workshop),
Loic Le Corre, Managing Director,
Pricing Solutions Europe, and
Tony Hodgson, United Kingdom
Practice Leader

Visit www.pricingsociety.com
for more information.

Pricing Managers Forum

Pantages Hotel, Toronto – An
opportunity for pricing managers to
regularly discuss topical pricing issues
and challenges. Contact Jim Saunders,
jsaunders@pricingsolutions.com, on
how to join.

June 26 – “Pricing Systems”

September 25 – “Building Your
Pricing Team”

French Pricing Club Breakfast Meetings

Pôle Universitaire Léonard de Vinci,
Paris

An opportunity for pricing managers to
regularly discuss topical pricing issues
and challenges. Contact Loic Le Carre,
llecorre@pricingsolutions.com,
on how to join.

September 8 – “New approaches to
Pricing Research”

October 8 – “Pricing Analytics”

November 19 – “Service Pricing”

Pricing Practitioners Breakfast Meeting

September – Venue to be advised,
London, United Kingdom

Contact Tony Hodgson,
thodgson@pricingsolutions.com,
United Kingdom Practice Leader, for
more information.



Avy Punwasee
has recently
joined Pricing
Solutions
Limited as a
Senior

Consultant, focusing on pricing
management and strategy.
Prior to joining Pricing
Solutions, Avy was responsible
for pricing management in the
service parts business of a
major domestic automotive
company. In this capacity he
managed over 400,000 SKUs
and \$700 million of revenue to
a diverse customer base. In
addition, he was a key
contributor to developing and
implementing the organization’s
long-term strategic vision and
financial business plan.

Avy has a wealth of experience
in numerous operational areas
including channel pricing,
competitive realignments,
promotional pricing, input cost
negotiation and change
management. Over his pricing
tenure he has added tens of
millions of dollars in profit while
still maintaining a focus on
increasing sales.

To reach Avy, please call
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ext. 105) or email him at
apunwasee@pricingsolutions.com

Visit www.pricingsolutions.com for an update on all events.

New Phone Number for North American Office

Please note that effective July 15, 2009, Pricing Solutions’ new
North American (Toronto) office number will be: 416-943-0505

All extension numbers and our fax number will remain the same. Our 1-888-771-8326
number will also remain the same. Please update your records. Thank you.



www.pricingsolutions.com

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