Archived Newsletter Articles

Capturing a Fair Return for the Value Delivered: Part 1

Value

Capturing a Fair Return for the Value Delivered: Part 1

This is part I of a two-part article on how to capture a fair return for the value delivered. In this installment, we focus on step one: making the sale at a value-based price. In the next newsletter, we will discuss step two: making sure the customer realizes the value.

Picture this: Your company has created an innovative new product. The sales force has communicated the value, and customers are salivating to get their hands on it.
To use a football analogy, you're at the one-yard line. It remains only to communicate the price and close the deal. Sounds simple, doesn't it? So why don't we always score a touchdown?
There are three main reasons why we "drop the ball": the sales force loses confidence when they have to discuss price; the pricing guidelines are ineffective; or the new offering is not properly priced.

The sales force loses confidence when they have to discuss price.

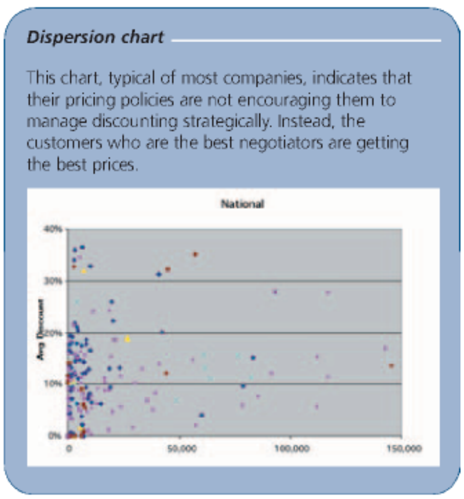
There are generally two reasons why reps lose confidence. The first one is fear, usually driven by compensation systems that reward volume instead of profit. If the rep senses any possibility of losing the deal, he will reach for the pricing card to increase his chances. The second cause is lack of experience. Customers will take their time when making a buying decision. If they are professional buyers, they will seek openings in which to negotiate down price. An inexperienced rep will often lose confidence when the customer "pushes back" on price.

The solutions:

- Reward *profitable* volume, not just volume.
- Limit the ability of your inexperienced reps to reduce price.

The pricing guidelines are ineffective.

If you plot price against volume, you are left with a scatter diagram (*see Dispersion Chart*). In most situations, this indicates no meaningful relationship between price and the quantity purchased. There are two possible reasons for this inconsistency: companies either do not have pricing guidelines, or they do not adhere to their guidelines.



The solutions:

- Set pricing guidelines and live by them.
- Establish a process whereby the sales force can execute deals within the guidelines without seeking approval; if they want to go below the guidelines, they must explain why.

A policy that we have seen work in the case of innovative products that have high value is not to discount at all. This removes the temptation and keeps the sales team focused on capturing a fair return for the value.

The new offering is not properly priced.

If your product provides real value and the sales force is doing its job of communicating, but yet can't close the deal, the third possibility is that the product is not properly priced.

You have this problem when one of two situations occurs:

- Units are flying out the door much faster than expected; or
- Units are moving much more slowly than expected.

In these cases, the challenge is to quickly find out what is happening, and why. Let's assume you are not selling enough units to meet forecast. You need to find the answer to the following questions:

- Are there different segments of the market valuing the product differently?
- Is the market as large as we believed it to be?
- Are there competitive alternatives available to the customer that we did not anticipate?
- Do customers have limitations that we did not anticipate (e.g., signing authority does not allow them to buy without going for approval, etc.)?

The solutions:

- Conduct research to determine the root cause of the deviation.
- Adjust your pricing strategy and/or value proposition. For example, for the more price-sensitive market, you might want to structure your offering so customers get a lesser offering for a reduced price.

If you have developed a great product and communicated its benefits, don't let all that hard work go to waste. The final step is to capture a value-based price. If you can keep up the sales force's confidence when they have to discuss price, implement good policies, and price the offering properly in the first place, you are sure to capture a superior return!

Corporate Headquarters:
Pricing Solutions Ltd., 38 Wellington Street East, Suite 200, Toronto, Ontario, Canade M5E 1C7