

10 PRICING MISTAKES



**CUSTOMER
MANUFACTURING
GROUP**

Our friend and pricing expert, Jerry Bernstein shared the following 10 pricing mistakes he sees sales people making when they deal with procurement people. So as not to impose our thinking onto Jerry's concepts, we are reprinting (with his kind permission) his original thoughts and then, where we think we can add value, we are adding our own commentary.

Mistake 1: *Not understanding the culture, needs, and incentives of the procurement organization.* Price is important, but the procurement organization is measured on other factors as well. In this tough economic environment procurement may be pushed hard to implement and obtain immediate cost reductions or cash flow improvement. For example: As an incumbent supplier you may have an opportunity to lock in business with better payment terms. These terms may be implemented immediately vs. a competitor that may require lengthy qualifications. Procurement will tell you their objectives if you ask. They want to know how you will help them meet these objectives.

Customer Manufacturing Group Commentary:

This is sound advice and we may disagree with Jerry as to the weighting of those "other factors" compared to price. However, the important point here is to remember that in your negotiations with the buyer, price is only one factor and focusing only on price is usually a losing proposition for you as the seller since the only way most procurement people want price to go is down.

Mistake 2: *Sales representatives discuss only price not the value of their offering.* Contrary to popular opinion many procurement organizations are open to a "value" sell. Get to know what your customer values and create a clear value sell proposal and use it.

Customer Manufacturing Group Commentary:

We concur. Assuming that price is the only issue on the table puts you in a no-win negotiating position and misses important differentiation factors that top procurement people should be interested in understanding.

Mistake 3: *Assuming that procurement knows your value proposition.* For example: Procurement is considering two machine tools. One is priced at \$400 and the other is priced at \$800. The \$400 tool wins, right? If the two tools are measured on cycles before replacement, the \$800 tool may be the clear winner. If procurement doesn't understand this, the \$400 tool wins.

Customer Manufacturing Group Commentary:

So true and not just in procurement discussions. You know what they say when you ass-u-me.

Mistake 4: *Not recognizing customer cost of change* from the incumbent to a new supplier. This cost of change can be significant, easily exceeding 10% of the purchase price. Suppliers often don't recognize this as an opportunity to justify a price premium of five to ten percent or more vs. a new supplier.

Customer Manufacturing Group Commentary:

How often have you come in at a lower price than the incumbent and not been awarded the business? Customers rarely change for a small price decrease unless the cost of change is virtually zero, in which case the low bidder who can execute is probably always the winner, and that customer has supplier changes on a regular basis.

Mistake 5: Thinking *Reverse Auction award decisions are based only on price*. In most Reverse Auction events price is not the only factor that customers consider. If the customer doesn't publish in the Event that the "Lowest Bidder Wins" then in most cases factors other than price are used in the award decision. Suppliers are often intimidated by the process, not thinking of the risks that customers face when changing suppliers. Suppliers that only sell on price are bound to lose.

Customer Manufacturing Group Commentary:

We are not fans of participating in reverse auctions. Our research suggests that the primary result of reverse auctions is the incumbent keeping the business at a lower price than previously. It is an efficient way to get lower prices from suppliers. That being said, Jerry is correct, reverse auctions, or any sealed bid process, does not imply award to the low bidder.

Mistake 6: *Not acting quickly to pass on commodity driven cost increases*. If you are selling a product that has a cost structure that is significantly impacted by the cost of commodities then you need to act quickly on pursuing price in the rising market. Procurement professionals will be more receptive to you passing on the commodity increase while the markets are still high and especially if they can pass it onto their customer. Once the markets fall, price increases will be resisted.

Customer Manufacturing Group Commentary:

Definitely true. We have customers that failed to do it regularly and then tried to get a "large" increase when it became too much for them to bear and their customers balked ... hard. In addition to the inability to raise prices once commodities stop rising, when commodity prices drop and other suppliers are accepting decreases you may be hard pressed not to offer a decrease even if you did not get an increase previously because everyone else is reducing need?

Mistake 7: *Not capturing price by using your ability to help manage your customer's risk*. You might be able to help the customer manage his risk through material hedging, managing inventory, exchange currency, etc. For example: The supplier sells copper fittings. The customer is concerned about future price increases due to the volatility of copper prices. You can get a premium price if you can help mitigate the risk by providing a fixed price that relies on your ability to hedge your copper purchases.

Customer Manufacturing Group Commentary

You get paid for the value you provide (as long as you recognize it yourself). That value may be available in some ways your marketing department never considered.

Mistake 8: *A misguided view of strategic partnerships.* Be assured that procurement won't view your partnership as an entitlement for higher prices. The greatest benefit to the supplier is a stronger position to retain and keep the business by "locking in" customers over time. You have worked hard and battled to be named as a strategic partner but now is not the time to rest. That partnership provides you an opening to create strong relationships with procurement, operations, engineering and quality. Creating those relationships will pay big benefits when your competition tries to unseat you. Having these open doors will enable you to identify opportunities to create a value position that is difficult to counter. Driving lower cost transactions, assisting with kanban systems, demand modeling, and helping with product design are all opportunities for risk mitigation while creating value that is hard for an outsider to understand and compete.

Customer Manufacturing Group Commentary

The entire concept of strategic partnerships is an over-used and not well implemented concept. Even as a so-called "strategic supplier" this may just be a nice phrase used to get you to give the customer preferential pricing. In our experience true strategic supplier relationships are rarely driven by procurement. They are driven by engineering or operations who have a need for value-add that is not included in just the products being provided.

Mistake 9: *Expressing a weak financial (supplier) position in attempt to gain price.* Procurement will view this as a desperate move. The result may be that the customer qualifies and moves to a new supplier in the background because of risk mitigation.

Customer Manufacturing Group Commentary:

We concur wholeheartedly. Trying to gain price concessions by appearing to be an unstable supplier is a very fast way to get replaced as a supplier.

Mistake 10: *Not getting involved in the customer's New Product Development.* You as the supplier often better understand how to design a component for manufacturability and align it with your manufacturing process. By helping the customer design in standard products or designs with characteristics that align with your manufacturing capabilities you can create a win-win relationship. Aligning your manufacturing capability with customer needs gives you the ability to be more responsive to the customer while creating a strong environment to retain price.

Customer Manufacturing Group Commentary:

This is the most important of all in our opinion. While Sales' relationship and interaction with procurement is important, in most well run companies engineering and operations have more say in the supplier decision than does procurement. Most of your time, effort, and value needs to be focused in those areas not in procurement, unless your goal is to be the low price leader.

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