February 2008 Distribution & Pricing Techniques
THE EXECUTIVE SUMMARY

Raise Prices?

Successfully implementing a price increase affects profits more positively and immediately than does any other marketing tactic. The prices of B-to-B products have been relatively stable since 1995, consequently many managers have little experience increasing them. Rising costs (energy, commodity prices, etc.), however, now dictate that prices must be increased for many product categories.

Let's examine some of the things that most affect the success of a price increase.

A. ***Knowing your competitors.*** Most B-to-B manufacturers respond very predictably to a price increase by a competitor. In the auto, airline, steel, energy, and lumber industries the participants typically react to a price increase by one of their counterparts by matching it. How have your competitors reacted in the past?

B. ***Differentiating your product offering.*** Salespeople are often instructed to "sell on quality not on price," but that misses the point. Product quality is not important unless its value can be quantified to the customer. Saying that the features and benefits of your products are valuable is not enough. Their value must be quantified in terms of saving time, money, minimizing reworks, increasing distributor profitability, etc. Both your salespeople and distributors need to communicate a quantifiable value proposition if you are to successfully implement a price increase.

C. ***The position of your product lines in their lifecycle.*** If your product lines are in the mature phase of their lifecycle, then it is likely that your competitors are aggressively cutting prices to maintain volume/share. You should hold your prices and pass along inflationary increases even in the face of declining sales. If your products are in the declining phase of their lifecycle and some competitors have already or are now exiting the business, then prices may be increased more aggressively, generally by the rate of inflation (CPI) plus 2% to 4%. Although counter-intuitive, this proven "harvest" strategy works.

D. ***Knowing the economic environment.*** Surprisingly, it is much easier to implement a price increase in a difficult economic environment than in a good one. This is because most industry participants in this situation search for any opportunity to increase profits to compensate for declining sales. In a depressed environment, a price increase by one participant, especially by a leader, is invariably followed by similar increases by all competitors within 30 to 45 days.

The Point. There are 13 B-to-B pricing strategies. Space does not permit a discussion of each; however, we offer the following:

- *Don't go "half way."* A 2% difference in the size of the increase does not materially affect demand or brand selection.
- *Don't announce a price increase in advance.* Price increases are not sales promotions.
- *A price increase can negatively affect the unit sales of capital goods,* but usually 60 to 90 days later.
- *A price increase can negatively affect the unit sales of consumables,* but usually five to seven months later.
- *Cutting prices affects profits* as quickly and negatively as raising prices enhances them. Think long and hard before reducing prices in any environment as the affect on profits is often an order of magnitude.

Recommended reading: *The Strategy and Tactics of Pricing*, Thomas T. Nagle and Reed K. Holden