

Am I Charging The Right Price?

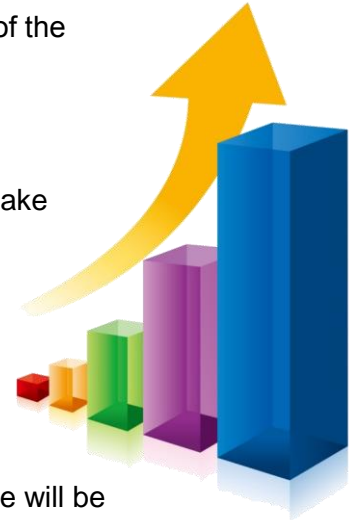
If this question is keeping you up at night, you're not alone. The scale of the pricing challenge for distributors is unlike any other industry:

- A restaurant has to make a few hundred pricing decisions
- A grocery store around 40,000
- A typical manufacturer will have 5 million pricing decisions to make

All of these pale in comparison to the average wholesale distributor. Considering the number of and diversity of items sold and the wide variety of customers served, a distributor can be faced with up to *100 million* potential pricing decisions.

The biggest mistake distributors make is depending on their sales people to determine the right price for items without giving them adequate pricing intelligence. In absence of this data, your sales people will be guided by their most vocal coaches – your customers. Fear of losing a customer will drive your sales people to price in a very narrow range. This approach can cost you at both ends of the price sensitivity spectrum:

- Sales people lose volume on competitive items when they start too high on the most price sensitive sales, even if they have the right average price in mind.
- At the other end of the spectrum, sales people leave money on the table on the least price sensitive, low volume sales when they resort to a comfortable average margin.



HOW DO YOU DETERMINE THE RIGHT PRICE?

Identify the price sensitivity factors: volume and frequency

You first need to identify what factors control item price sensitivity. Think about how your grocery store prices items: when you buy milk or hamburger, the store is making low single-digit margins. If you buy something at the bakery or deli, however, you'll pay 60% or more. Why? Because, while a shopper knows and remembers the prices of staple items they purchase in quantity and often, they are much less price sensitive to items that they purchase infrequently.

It works the same way for distributors. The catch is that your customers come from different industries and all have different purchasing habits, unlike shoppers in a grocery store that share purchasing patterns.

As a distributor, you need to factor in these customer differences. What is a high volume, high sensitivity item for one might be an incidental purchase for another. Pricing an item at the same average margin for both means you risk losing money on both. Instead, if you differentiate your price for an item based on how price sensitive that item is for each customer buying the item, you can make sure your price-sensitive customer will get a competitive offer while maximizing margin on your less sensitive customer. In other words, *you'll be charging the right price.*

Sounds a little too simple? Consider this: We see our clients gain an average of 1.7+ margin points within 12 months just by focusing on sales that aren't as price sensitive. A 1-point margin

gain can increase the earnings of the average distributor by 50%. Moreover, you will sell more price sensitive items and take less risk of inviting in your competitors if you carefully rationalize your pricing.

Generate specific target price recommendations

By analyzing the key metrics that determine price sensitivity:

- Industry
- Customer annual item spend
- Purchase frequency
- Price point

You can convert that into specific target price recommendations on every item you sell to every customer.

The good news is that you already own the pricing intelligence you need. Your ERP system collects a wealth of data. The problem comes back to scale: it's relatively straight forward to research optimal pricing for a few items, but you have a million.

That's where technology offers a solution. At Profit2, for example, we have specialized tools and a proven methodology to enable distributors to mine and leverage their own data. This process generates specific target price recommendations for each item based on the specific customer. In combination with your ERP pricing hierarchy, you can gain margin by improving pricing on incidentals and improve sales by charging the right price on price sensitive sales.

ABOUT PROFIT2

At Profit2, our focus is on leveraging technology in a practical and applied manner. The goal is to make sure our clients charge the right price for every sale they make. Not just incidentals, but also high volume price sensitive items, non-stocks, and large job orders. Moreover, we help program your ERP pricing hierarchy so every customer- item combination you sell will be priced at the optimal price.

Setting up pricing in your system is just the first step. The right price won't do you any good if your sales people don't use it. We've developed tools and methodology to involve your sales people in determining "the right price" and gaining their active support and price utilization at order entry.

To request our complimentary Full Executive Briefing on "How to Tell If I am Charging the Right Price" email bill@profit2.com or call (913) 897-0159.

Every member of Profit2's team is a specialist with just one area of focus: pricing! We have conducted over 200 successful margin improvement projects over 10 years. Our clients include distributors and master distributors in more than 30 industry segments. We work with all major ERP systems and legacy systems.

