THE EXECUTIVE HANDBOOK FOR PRICE OPTIMIZATION

INSIGHTS AND RECOMMENDATIONS ON WHY YOU NEED TO PULL THE PRICING LEVER TO DRIVE REVENUE AND PROFIT GROWTH

Realize Your Potential
If you’re an executive responsible for profit and loss in a volatile marketplace, realizing your revenue and profit potential is critical to both the success of your business and your career. In today’s business environment, the cost of inaction when it comes to improving sales and pricing effectiveness – the key drivers for incremental revenue and margin improvement - is getting higher with each passing month. Leaders who fail to address their transactional business challenges are likely to face declining market share, reduced shareholder value, and increased customer dissatisfaction over time.

Research from the Aberdeen Group shows that a dramatic shift in sales priorities is upon us (see below). Between 2014 and 2015 alone, sales priorities switched significantly, as bottom-line growth became a bigger focus than top-line growth.
With this increased focus on profits, organizations need to re-assess their traditional sales strategies, especially in regards to pricing, an area where many companies have relied for too long on intuition and business-as-usual practices.

Price optimization must be a key component of your growth strategy. According to Aberdeen Group research, ignoring price optimization can reduce your revenue growth by almost 50 percent when compared with businesses that deploy price optimization.

However, for many businesses, the pricing practice remains misunderstood, esoteric and manual. The problem boils down to bias, emotional pricing habits, or thinking your current process is working fine.

Understanding pricing and willingness to pay is complicated. Commenting on a proposed price optimization project, one CEO of a leading energy company stated: “pricing is not an exact science. In fact, it is much more of an art than a science.” It’s not surprising that organizations have trouble committing to change.

“In the entire Gartner Research CRM technology landscape, price optimization, along with CPQ, are the only two technologies classified as providing “transformational benefit” in the next 2-5 years.”
DO ANY OF THESE COMMON PRICING MYTHS SOUND FAMILIAR?

Many companies still rely on outdated, overly simplistic, or ad hoc practices that start with price setting and continue right through to execution in the field. If you want to grow revenue and margins, the first thing you need to do is take a close look at how pricing is set and executed in your organization. Let’s examine some common pricing myths and see if any of them seem familiar.

**MYTH #1: ALL CUSTOMER AND MARKET SEGMENTATIONS ARE CREATED EQUAL**

Many companies believe they’re already doing segmentation analysis for pricing. Although organizations often segment their market by customer size, geography or product line, none of these categories focus on actual purchasing behavior. Without understanding which attributes are really driving pricing behavior, companies are left with an incomplete picture of how to accurately price products to unique buying segments.

**MYTH #2: LOOKING BACKWARD IS ALL THAT’S NEEDED TO DETERMINE PRICING MOVING FORWARD**

The rise of business intelligence tools has given front office employees the power to analyze large volumes of historical data. But in highly dynamic markets with volatile costs, fluctuating demand and evolving competition, simply looking at old data isn’t enough.

To properly analyze trends in pricing and demand as well as to forecast where prices are heading, you’ll need more sophisticated price optimization tools. Only then will you be able to accurately set future prices and maximize your profits.
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**MYTH #3: PRICE ELASTICITY DOES NOT EXIST IN B2B MARKETS**

Many people in the pricing world have taken a position that there is no such thing as price elasticity in B2B.

In the foodservice industry for example, it is unlikely that a restaurant would increase its order from 14 to 15 cases of hamburgers just because the price went down. So how could there be elasticity? On the flip side, suppliers that raise prices will probably not see sales volume go down on certain types of products - you need what you need.

However, it is important to recognize what’s really driving volume. It’s likely not price. If you’ve won the business, you should get the volumes that are regularly ordered regardless of price.

Consequently, price optimization should not focus on what prices give you the best combination of volumes and profit but rather focus on the best chance of winning the business at the best profit level possible. Balancing the perfect combination of volume and profit doesn’t mean much if you don’t win the business.

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HITTING GROWTH TARGETS: FOUR REASONS WHY THE DECK MAY HAVE BECOME STACKED AGAINST YOU

1. Procurement Has Upped its Game

During the last economic downturn, many companies discovered the power of unleashing aggressive procurement teams on their vendors to extract concessions and discounts. Instead of facing disinterested contracting teams, your sales reps may now be battling skilled negotiators (often with legal backgrounds) on the other side of the table. If your reps cannot enter negotiations with defensible pricing positions, it is almost guaranteed they will resort to over-discounting, effectively taking a hatchet to your margins.

2. Buyers Have Become More Sophisticated

It wasn’t that long ago when prospects engaged with your sales team directly in the early stages of the sales cycle, perhaps armed with an analyst recommendation and not much else. Those days are over. Even though it took some time, the Internet has gradually changed the sales dynamic. The buyer and seller relationship has always been asymmetrical, however it is now buyers that are calling the shots. Vendor review sites, more aggressive marketing, and “sideways” references are making the early evaluation stages much more self-service. By the time your reps interact with prospects, they have likely narrowed down their choices and are more interested in price and value differentiation conversations, or even worse, using you as due diligence fodder.
The window of opportunity for the sales team to influence the customer’s buying journey is shrinking, even in some cases - disappearing. According to Forrester, **74% of B2B buyers now research and 30% now buy at least one-half of their work purchases online.** Sales teams need a new approach that enables them to be smarter and more productive with each interaction.

3. Pricing Technology Has Become Democratized
The move of pricing technology from process automation to true data science-driven analytics has exponentially increased its ability to positively impact both the top- and bottom-line. In addition, with pricing technology moving to the cloud, cost has dropped, allowing small and medium-sized businesses to mimic some of the advanced pricing capabilities of their larger competitors. The result: a large, experienced pricing team is not as much of a game-changer as it used to be because a pricing team of two to three can be much more efficient and strategic with their pricing strategy.

4. Lifetime Customer Value: You Better Be Thinking About It
Maximizing the value of existing customer revenue streams is more important than ever in this age of market volatility. Numerous studies from Bain & Company and others have shown that acquiring new business is considerably more expensive than retaining existing business. The problem is too many sales, marketing, and pricing organizations still look at deals as single “point” transactions and do not address the bigger picture of customer lifetime value. If you are leading with price to close deals, you are undercutting repeat, renewal, and expansion business value. It may be impossible to make up margin on future transactions after you sold yourself short on the initial deal as your customers will expect similar discounts down the road.

A data-driven approach to price optimization will help you find prices that win without sacrificing your growth goals (and help you better determine when to walk away from deals that may not be in your best long-term interest).
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SO YOU MAY HAVE A PROBLEM. WHAT ARE YOU GOING TO DO ABOUT IT?

Technology Is Key in Evolving Pricing Effectiveness

Many businesses today still use a “cost plus” pricing technique as a general way to price products in a B2B environment. For example, price equals cost plus 25 percent. Once prices are set, the effectiveness of pricing is judged by the product’s profit-and-loss statement.

In contrast, price optimization technology offers a practical and scientific alternative that determines each customer’s willingness to pay. Operating at a highly granular level – customer by customer or product by product – price optimization software makes a value-based pricing approach possible by estimating the value that customers actually put on products versus what they’re currently paying. Such pricing insight is critical in ensuring that sellers gain and sustain a competitive advantage in the marketplace. And remember, price optimization technology is becoming increasingly more powerful and easier to implement, allowing smaller competitors to close the pricing gap.
Hitting a Constantly Moving Target: Determining Willingness-to-Pay

Willingness to pay in the B2B sales environment is a constantly moving target. Consequently, it isn’t easy to quantify without the help of data science-driven pricing technology.

Take this example: if you lose your car key, how do you put a price on its replacement? Your car dealer has a battery-powered key fob that can detect when you are in proximity and automatically unlock your car. Alternatively, you can ask for a mechanical key that opens only the driver side door.

What is your willingness to pay for the added technology? Some would buy the mechanical key under all circumstances whereas a gadget geek might pay the price premium for the key fob convenience. In this situation, willingness to pay depends on a number of different factors. By leveraging a combination of science (micro-segmentation) and simplicity (technology that can crunch the data in real-time to provide a defensible price at that moment in time), your sales reps can hit the moving willingness-to-pay target, helping increase deal velocity and profitability.
EMPOWERING SALES WITH PRICES THAT WIN: 4 CRITICAL ADVANTAGES OF PROVIDING OPTIMIZED PRICING TO THE FIELD

We’ve discussed in basic terms how price optimization can help your business increase deal revenue and profit. Below, we’ll get into a little more detail by providing five distinct ways optimized pricing can better arm reps to lead on value and not on price.

1. SETTING CONTEXT FOR DEALS

When one of your sales reps goes into a pricing negotiation with little more than a gut instinct, the initial price offered likely will be too high, too low or lowered too quickly. All sales reps have experienced a situation where they come in too high and lose the business or come in too low and leave money on the table.

Sales reps are most effective when equipped with a rational pricing strategy that allows them to negotiate within a range that makes sense for their business and customer. Armed with optimized pricing, sales reps know when they have flexibility (and when they don’t) and have confidence that the prices being offered are realistic and data-based.

2. BUILDING TRUST IN CUSTOMER RELATIONSHIPS

Personalized, data-driven pricing makes customers more comfortable with accepting your sales proposals, improving your win rate while reducing sales cycles. For customers, you become the only vendor they trust to provide the solution they need at the price that works for them.
3. INCREASING CONFIDENCE IN NEGOTIATIONS

To win deals at the prices your organization needs, sales reps must have confidence in their pricing position.

Often, the buyer has the most comprehensive and up-to-date market research and thus more power in the negotiations. When sales reps don’t have confidence in their price position, the first thing they do is back off the initial price. This signals customers to keep pushing until they find the lowest possible price.

Armed with optimized pricing, reps have the confidence to hold firm on price and spend more time on communicating the value your solution. This approach helps change the sales conversation from haggling over the lowest price to helping customers internalize the full value they receive from your solution. Maverick discounting is probably the single-biggest pricing execution failure at most companies, especially at quarter end as your sale teams goes into panic mode to make quota. By delivering winning prices at the time of quote, price optimization will eliminate maverick discounts and the end-of-quarter squeeze.

4. CAPTURING INCREMENTAL REVENUE

Price optimization divides your customers into segments based on buying behavior, products purchased and transaction types. From there, you’re able to identify which customers are being offered prices far below the average for their segment. These customers represent an opportunity for reps to capture incremental revenue by using this intelligence to ensure prices reflect the true value of your product.

SOMETHING TO CONSIDER:

What percentage of your deals close at quarter’s end?

How does this impact your forecasting accuracy?
The fundamental first step in the successful adoption of a price optimization project is recognizing that your departmental teams have different perspectives and motivations. Being able to cater to each of their needs will help you sell pricing strategy to all departments.

When meeting with each group, prepare your list of key stakeholders well in advance, and identify pricing champions for each major audience. Pricing champions are people you can enlist for each major department who can help you implement your pricing strategy.

Your pricing champions should be team members who are:

- Experienced in rolling out major projects
- Able to influence senior leaders and decision-makers
- Gregarious by nature and are willing to share their opinions
- Well-respected across the organization
- Well-versed in existing reporting tools, data and/or processes
- Veteran managers with several years’ tenure (these people bring credibility to your project)

Changing the pricing paradigm in your organization will be a scary proposition for many given its sensitivity, so patience is a requirement.
Here’s a quick overview of what motivates each department and what you need to provide to sell them on pricing strategy:

**PRICING**

Pricing team members need functional exercises, spreadsheet-style reporting and the ability to generate ad hoc reports quickly. Their needs are driven by the fact that they want answers to their queries as soon as possible. They are usually familiar with data structures and working the numbers. They don’t mind getting their hands dirty with the data. They need to feel confident that the numbers coming from their pricing system match the data every other department sees.

**FINANCE**

Finance team members are all about the numbers. They must have confidence that the pricing numbers your project generates are accurate and trustworthy. Showing them how a pricing project can generate trend charts for analysis usually gets them intrigued, especially when they can access the same reports and charts month after month.

**MARKETING**

In contrast, the marketing team typically wants more graphical information and responds well when the team is able to work with a few standard reports that show meaningful analytics. Marketing team members run the same reports repeatedly using various inputs and test different pricing scenarios. Motivating the marketing team means demonstrating how the pricing project can resolve its specific pain points.

**SALES**

The sales team members have to feel as though the pricing project is going to make their lives easier and sales efforts more effective. Providing illustrations and examples is critical to getting buy-in from sales. Starting with a price optimization pilot group (one product line or geography for example) is the best way minimize disruption and start showing value. It also will provide some compelling benchmark comparisons between the test group and the wider sales organization.
WRAPPING UP

Price optimization is the most effective way to drive sales and increase your profits. Research from Aberdeen (below right) show that adopters of price optimization technology not only tend to be more profitable but also demonstrate a superior level of sales effectiveness and competence.

Data science and prescriptive analytics are hot topics in sales enablement these days, and for good reason. Businesses have a wealth of data at their fingertips and technology has now reached the point where it can put that data to work. It is a reasonable assumption that some component of your sell-side business process is leveraging prescriptive insights powered by technology, whether you are aware of it or not. This begs the question: why isn’t pricing part of the mix? According to PwC, a **1% price increase typically delivers an 11% impact on profit.** Pricing is one the biggest drivers of revenue and profit and needs to be handled as rigorously and adeptly as any other critical sell-side function.

In this era of constant market volatility, the time to act is now. The first big step is evaluating your current pricing practices to identify where you may have performance gaps. If you are not using data science-driven price optimization, you likely have a problem.
About PROS

PROS Holdings, Inc. (NYSE: PRO) is a revenue and profit realization company that helps B2B and B2C customers consistently realize their potential through the perfect blend of simplicity and data science. PROS offers solutions to accelerate sales, formulate winning pricing strategies and align product, demand and availability. PROS customers experience meaningful revenue growth, sustained profitability and modernized business processes because of PROS revenue and profit realization solutions. To learn more, visit pros.com.