■ Allegheny Marketing Group ■

Seeds...

Issue Number 2

Pricing

The marketing role is changing rapidly as the concept of developing strategic partnerships between buyers/sellers gains momentum. The pricing implications in a partnership arrangement need to be studied and taken into consideration before jumping into such arrangements. Too often the thought of having a captive customer with large volumes of business overshadows the pricing risks.

There are many examples illustrating the risks of entering into partnership arrangements. A common situation is when the buyer informs the seller he likes his product, service, quality and delivery – but he will have to reduce his prices 8 – 10% to remain a partner. The automotive, chemical, and semiconductor industries are examples where pricing risks are high.

The traditional role of pricing is different during a partnership arrangement. The normal bidding process changes, the opportunity for value selling frequently disappears, and the chance of increasing prices is diminished. Many buyers demand more value at lower prices! The partnership concept of a win-win situation can quickly turn into a win-lose environment as the glow wears off after the first several years.

Our best advice is to assess your leverage against your buyer's leverage -- before entering into a partnership. If the buyer appears to have more leverage -- be careful.

To develop leverage criteria, think about what makes a buy more powerful in the negotiation process -- his size, his sales potential to other sellers, how many other sources of supply he can buy from, and how important your product is to his business. If the answers are all larger or numerous, then the buyer will likely have a high degree of leverage.

Conversely, think about what makes the seller more powerful -- how important is a single customer, how unique is the seller's product and service, and what is the potential profitability?

The case shown below is one where the buyer has leverage over the seller. The buyer is large, the seller small.* The buyer can buy from other sources* with minimal switching cost* even though the seller has unique product attributes.* And the seller has few other customers.* All these points favor the buyer. Overall, the buyer's score of 67.8% is much stronger than the seller's 50%.

You can develop your own rating system to make the assessment. What is most important is understanding the long-term consequences relative to pricing in a strategic partnership.

* Note shaded areas in tables below.

MEASUREMENT OF **BUYER'S** LEVERAGE			
Strength Criteria	Scale Value (Range 1-10)	Weights (5 = Best)	Total Score Value x Wt.)
1. Organization's Size	6	4	24
2. Sales Potential	8	5	40
3. Number of Available Suppliers	9	4	36
4. Importance of the Product	5	2	10
5. Switching Cost	4	3	12
Total Perfect Score = 190 (10 x Total of Weights Column) Percentage Score = 122/190 = **67.8%**			122

MEASUREMENT OF **SELLER'S** LEVERAGE			
Strength Criteria	Scale Value (Range 1-10)	Weights (5 = Best)	Total Score Value x Wt.)
1. Organization's Size	2	4	8
2. # of Customers for Product	3	5	15
3. Unique Product Attributes	9	4	36
4. Unique Services Offered	5	2	10
5. Potential Profitability	7	3	21
Total Perfect Score = 190 (10 x Total of Weights Column) Percentage Score = 90/190 = **47.4%**			90

Customer Satisfaction

Based on the Allegheny Marketing Group's experience with customer satisfaction surveys, there are five key mistakes companies make.

First, they don't understand and use information from their competitors' customers. A company may be improving customer satisfaction but not as fast as their competitor. Thus their ratings go up but their competitiveness goes down.

Second, they don't understand that customer satisfaction factors can be important to customers but they don't influence the decisions for selection. For example, safety is an important factor for airline passengers, but not a distinguishing factor on airline selection.

Third, they fail to include price factors into their customer satisfaction criteria. Price is a value to customers as well as the many product and service attributes.

Fourth, they fail to determine customer standards that may be used to determine supplier quality levels. This information quantifies quality levels and provides actionable information.

Fifth, companies do not have a structured process to ensure that market information is truly utilized by interfunctional business teams.

To be competitive in any market, companies must move beyond continuous improvement in customer standards and relative to their competition.

Marketing Channels

In the last issue of *Seeds...* we discussed the factors that can influence the choice of sales channels. These factors should be contrasted with the profiles of various channel selections such as an all-employee sales force, independent representatives, distributors, teleselling, and direct marketing (catalogs, mail-order houses, etc.). When making asseme assessments of the advantages and disadvantages of different channels, care should be taken in generalizing <u>all</u> situations the same.

The following matrix summarizes the general strengths of different sales channels. Many companies use a combination of these channels trying to balance the effectiveness with costs. This is an approach companies use when trying to reach multiple market segments. The drawback to using multiple channels is the likely duplication of functions and thus, a duplication of costs.

Comparing these strength profiles with the business situation allows an overall assessment of channel selection.

STRENGTHS

Employee Sales Force	Independent Representatives	Distributors	Teleselling	Direct Marketing
Company Focus	Excellent Selling Skills	Product Availability	Reasonable Cost	Low Cost to Reach Many
Market Intelligence Feedback	Geographically Focused	They Are a Customer	Touches Many Customers	Low Cost Order Entry System
High Loyalty	Sells Associated Products	Save Some Transportation Costs	Good Feedback System	Focused Selling on Product Line
Long-term Selling Approach	100% Variable Cost	Reaches Smaller Customers	Fast Response	Consistent Selling Messages

These assessments are important; however, the most important factor may be overlooked -- which channel currently has the best <u>relationships</u> with your targeted customers. The real world still works on relationships.

Market Research

When companies decide they need to conduct a market research study, there are five important issues they should consider.

1. **How the information will be used.**

   "If you don't know where you want to end up, then it doesn't matter which direction you take."

   Deciding how you will use the market information once it is obtained has a major influence on the design of the research project. For example, if research results are aimed at valuing product features for product changes, then the design must be specific enough to link features with benefits and price levels. If research results are to validate or provide strategic directions, then designs should concentrate on trends and competitor changes.

2. **Who we should talk with.**

   In many types of consumer research, all respondents have an equal vote and random surveys may be appropriate. This is not the case in typical industrial research studies. Customer samples need to be segmented, not only by the types of customers, but also by the respondents' responsibility relative to the specification or purchase of the product.

3. **How the questions should be asked.**

   Depending on how the question is asked, a respondent can provide many different answers to a similar subject. Good questionnaire design should be:
   - clear and very specific
   - logical in the sequence of questioning
   - developed to double check key issues, but not be redundant
   - as short as possible to collect the required data
   - both quantitative and qualitative
   - created so as not to "lead" the respondent to a conclusion

4. **How the information should be presented.**

   Information is not very useful if it is presented in a manner that is difficult to understand or is not pertinent to the end use. There are many technologies available such as:
   a. Question/Answer/supporting research proof
   b. Hypothesis/research evidence to support or not support
   c. Storyboarding the information
   d. Qualitative discussion with supporting attachments
   e. Recommendations/Conclusions/Findings method.

5. **Who should be involved in our organization.**

   If the purpose of the study is tactical implementation to improve short-term results, it may be important to include many functional employees throughout the study. Ownership and understanding are key success factors. If the purpose is to provide strategic direction, only one or two high level executives may need to be included.

In the next issue of *Seeds*… we will discuss different uses for market research.

Marketing Thoughts

Additional thoughts about Marketing and Sales.

- No news is bad news.
- A bad product is a bad product is a bad product.
- Beware of alleged needs that have no real market.
- Secret negotiations are usually neither.

Afterthought

We thought you might want to give this test to your employees. First take it yourself – the results may surprise you.

This is a timed test – you have only three minutes to complete it.

1. Read everything carefully before doing anything.
2. Put your name in the upper right hand corner of this paper.
3. Circle the word “name” in sentence 2.
4. Draw five small squares in the upper left hand corner.
5. Put an “x” in each square.
6. Sign your name under the title of this paper.
7. Put a circle completely around sentence number 7.
8. Put an “x” in the lower left hand corner of this paper.
9. Draw a triangle around the “x” you have just put down.
10. On the back of this paper, multiple 703 by 12.
11. Draw a rectangle around the word “corner” in sentence 4.
12. On the reverse side of this paper, add 8950 and 9805.
13. Put a circle around the answer, and put a square around your answer, and put a square around the circle.
14. Underline all even numbers in this test.
15. Now that you have finished reading everything carefully, do only sentences one and two.

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