

## **Because You're Worth It: An Overview of Pricing Strategy**

*By Steve Deist, Partner at Indian River Consulting Group*

Do you want two more points of gross margin? Of course you do. Better pricing could be the way to do it. But, as they say, there is no free lunch. If you want to sustain those higher margins you must have a strategy.

By "strategy" I mean taking a long-term, customer-centric perspective rather than an opportunistic, internal, profit and loss view. If your starting point is "how much more can I squeeze out of unsuspecting customers?" then you're playing with fire.

A sound pricing strategy is based on ensuring that you are capturing the value you deliver; it's not about deceiving or tricking customers. Relying on ignorance or habit is not a viable approach, especially in today's information-rich world. In five seconds anyone can check your price on Amazon. Sure, you can probably sneak in price increases on low volume items and get away with it for a while. But at some point your pricing level will be recognized and you will have to be offering enough value to justify it.

Pricing projects are notorious for showing major margin gains up front that melt away over time. The last thing you want is for a loyal customer to catch you "speeding." You run the risk that a small dollar pricing gain destroys the trust that you've built up over years, leaving you with a suspicious customer who now examines every invoice with a magnifying glass. Poorly implemented pricing programs have put companies out of business.

Most distributors' success depends on long standing relationships and maximizing the lifetime value of customers. A customer's aggregate, ongoing revenue stream is more important than the profit from any particular order. You may be "over serving" some of your customers, who would be willing to pay more to buy from you. But other customers may be all too happy to switch you out for a few pennies. Ultimately, more effective pricing requires that you have some way to differentiate between the two scenarios.

The technical term for this differentiation is "segmentation", but that word has been abused in our industry. To be useful for pricing, a segment must be based on how the customer looks at *you*, not how you look at the customer. Grouping customers based on how much they buy or their profitability is the opposite of effective segmentation. These categories tell you nothing about how much they value the different elements of your service offering.

World class distributors treat pricing as a process, not a one-time project. They assign pricing responsibility at the executive level; invest resources to continuously



monitor and improve pricing realization; and have systematic feedback loops to objectively measure the impact of changes. We've found the best results occur when the pricing owner is in a product management or product marketing role. If this individual is measured on product profitability, she will be well placed to make appropriate trade-offs between gross margin percentage (speed) and revenue volume (altitude). Sometimes lowering prices will actually generate more total gross margin dollars, not to mention give the sales reps competitive weapons to open doors.

You can learn more about pricing strategy at my University of Innovative Distribution (UID) course.

## Where Do We Begin? The Case for Strategy

*By Steve Deist, Partner at Indian River Consulting Group*

A successful distributor CEO once told me that talking about strategy “makes the hair on the back of my neck stand up.” He was expressing the common complaint that strategic planning is an academic exercise that doesn’t add value. Historically, distributors have focused on execution not strategy. Growing the business one customer at a time, controlling expenses and having a strong enough balance sheet to survive recessions.

Today the world looks different. Distributors are facing new challenges from Amazon and other low cost, internet-only catalog houses. Manufacturers no longer see distributors as their only or even their best channel to market. Buyers have complete information at their fingertips. They spend more time on social media than listening to sales pitches. It’s getting very tough to survive, no matter how well you execute the same old game-plan.

But this is not the time for fear or panic. Distribution has overcome scary market shifts in the past: remember big box stores and online MRO market places?. Despite all the challenges, distribution represent exactly the same portion of our economy today as it was immediately after World War II – about 5.7% of GDP. I believe that future has never been brighter for distribution. The world is headed away from mass production toward an age of mass customization. Distributors that embrace data and think strategically are growing faster and making more money than ever.

Distributors are incredibly adaptive and know more about their customers than anyone else. The key is to use these strengths wisely – to focus your company’s limited resources on the right things. Strategy is really just another word for focus. It’s about deciding what you are going to do and, maybe more importantly, what you are *not* going to do.

There’s a lot of confusion about the word “strategy”. Most distributors have some form of business plan. This is often a set of numeric goals tied to some big projects or initiatives. A true strategy includes two more elements. The first is market positioning. Your ideal position in the market should be based on an unbiased understanding of who your customers are; what they are really buying from you and why; and where there’s a good fit between your capabilities and their needs. The key word is “unbiased”. You may feel that superior technical knowledge at your counter or face-to-face field sales calls are really important. But, if a customer chooses to buy from Amazon instead she is telling you loud and clear that these services are not worth a price premium. Understanding, accepting and acting on this knowledge is the essence of market positioning.

The second element is operating model alignment. A real strategy involves re-deploying your resources to fit your ideal market position. Let's say your target customers demand highly automated, "stupid easy" order processing. If you are spending 8% of your revenue on field sales and 1% on information technology then your operating model is misaligned. No matter how hard you work on those business plan initiatives you won't be successful. In fact, companies often discover that with the right operating model in place there is less need for big projects and cross-functional teams.

Market re-positioning and operating model alignment are not easy. But in today's world they are no longer optional. At my University of Innovative Distribution (UID) course I explain exactly how to develop a "real" strategy to tackle today's challenges head-on.

## Big M Marketing

*By Steve Deist, Partner at Indian River Consulting Group*

Most people in wholesale-distribution think of “marketing” as including things like advertising, trip promotions, search engine optimization and email campaigns. These are important activities but they are really tactical, not strategic. I call them “little m” marketing.

How do you know if the ad has the right message? Which customers should be targeted for promotional campaigns? To answer these questions you need to understand who your target customer segments are, and what they really want to buy from you. Figuring this out involves “big M” marketing. Big M marketing is about fundamental customer insight and market data.

Technology has radically altered the marketing toolkit, but the principles of Big M marketing haven’t really changed over the past 50 years. Big M marketing comes down to three things: segmentation, targeting and positioning. Segmentation is putting customers into categories based on what they want from a supplier like you. Targeting is determining which segments are a good fit for you. Positioning is adjusting your brand and offering to be aligned with the needs of your target segments.

Little m marketing is really the tactical execution of positioning.

Here’s an example. A distributor sells to contractors that do commercial audio-video installations. The distributor offers a range of services beyond basic product availability. These include inventory management, project management, training courses, business consultation and installation support. As part of a segmentation exercise the distributor realized that its customers fell into two very different buckets. One group gets jobs through a “spray and pray” approach: they bid on everything they can find and play the odds, winning 10% or 20% of their proposals. The other group focuses on innovation and specialization: doing jobs that no one else can pull off.

The distributor estimated the size and growth rate of both segments. It also did a profitability analysis to understand whether and how it could serve the segments economically. Both segments were deemed attractive but they clearly have very different needs. The distributor acted on this insight decisively.

For the “spray and pray” group the distributor stopped promoting training, project management and business consultation services. It changed its branding to emphasize low price and reliability. It added full visibility to quotes on its website and app.



For the innovative group it did the opposite. It focused all its sales, application support, project management and training resources on this segment. It created a sub brand that emphasized exclusivity and being on the leading edge. It started a product-of-the-month program to help its dealers stay ahead of their competition.

Needless to say, the distributor's little m marketing efforts for the two segments are totally different.

The distributor has gained significant market share in both segments and has actually lowered its overall cost to serve. It is handily beating its online-only rivals because it got the Big M marketing right.

I will cover the essentials of Big M marketing and how you can apply them to your company in my University of Innovative Distribution (UID) course.