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Pricing issues in industrial marketing

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Abstract

Developing an effective pricing strategy today is becoming a difficult task for industrial marketing managers. The failure of firms to totally understand the implications of their pricing decisions often leads to missed opportunities and eventually lowers profits. Price setting and implementation are multidimensional processes affecting customers, products, cost recovery efforts, produce margin levels, customer retention, market share, and domestic and international sales. This issue of *Industrial Marketing Management* provides some insights into the complexities of this process for managers by examining pricing on several levels, including the organizational influences on industrial pricing, the factors affecting international pricing, the importance of pricing in controlling supply chain costs, the influence of information on pricing decisions, the degree to which the Internet and reverse auctions are affecting customer relationships with their suppliers, and the importance of developing a strategic pricing plan.

Keywords: Pricing strategy; Auction; Industrial marketing

1. Introduction

Industrial marketing is a field that is challenging and complex. To be successful, a company and its management group must have a comprehensive understanding of what the challenges are and have a well thought out strategy to take advantage of them. The challenges are numerous and include the development and introduction of new products, controlling costs, competitive analysis, responding to competitor market strategies, prospecting for new customers and new market segments, developing long-term relationships with current customers, building, quality, building value and service into the company's product portfolio, and pricing. All of these challenges require that a firm take a strategic view of each area and develop the appropriate plan and implementation program for each one. Unfortunately, one of the areas is often overlooked when it comes to planning and implementation, and that is pricing. The reason for this is that "...price is often the centerpiece of strained relations with a customer; the weapon competitors are using to steal market share; and the source of conflicts within the company as those with the spreadsheets, pro forma income statements,..." (Dolan & Simon, 1996, p. ix) and the lack of accurate cost information in the setting of prices.

Industry managers continually complain that pricing is a headache and not an opportunity for increasing profits. Many firms have "thrown in the towel" on pricing. They blame this on the fact that they "determine (their) costs" but are forced to take their industry margins. They also complain that they have no control over prices since "the market sets the price and (they) have to figure out how to cope with it." (Dolan & Simon, 1996, p. ix).

What are industrial business managers to do to view the price setting process as an opportunity? What is the cause of this frustration in pricing? What are some of the organizational obstacles to setting prices in firms? What are the price setting opportunities firms can take advantage of in the management of their supply chains? How can the departmental conflicts over pricing in industrial firms be over-

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come? What are the challenges industrial firms must deal with in international pricing? What role does the Internet play in the price setting? Also, what are the impacts of reverse auctions on industrial price setting, and what impact are they having on maintaining customer relationships? Of course, it is not easy to provide simple answers to these questions, but in this issue of *Industrial Marketing Management*, the authors provide some insights into the challenges and opportunities facing industrial pricing managers in the future. They include:

(1) Viewing the supply chain as an opportunity to reduce costs and improve product profit margins through more effective pricing.
(2) A better understanding of the intraorganizational influences on industrial pricing strategies.
(3) The recognition of how to better manage the influence of internal and external determinants on international pricing strategies.
(4) An understanding of how the Internet influences the flow of information between vendors and their customers and the effect it has on pricing.
(5) An understanding of how reverse Internet auctions affect pricing in the management of customer relationships.
(6) The need for the development of a strategic pricing plan to coordinate price setting, tactics, and policy with an effective implementation program.

2. Supply chain management and value pricing

Supply chain systems were for years regarded as simply channels of distribution. From this perspective, the focus of channel management was on making each firm in the distribution channel more efficient and productive. Each firm operated on its own, seeking to make the highest profits and acting independently to price its products and services. With the advent of supply chain management and the concept of a supply system emerging, the perspective of industrial managers changed from one of an "…*intrafunctional* vision, where the focus was on the individual firms in the channel, to an interfunctional view where emphasis is now placed on the cooperation that occurs between firms" (Lancioni, 2000, p. 2). The closer relationships have made customers more value conscious in their purchases from their suppliers and less brand loyal. This has increased the opportunities for more creative pricing strategies and the extraction of higher profit margins in supply chains.

Christopher and Gattorna point out in their article *Supply Chain Cost Management and Value Based Pricing* that profit margin opportunities are decreasing due to the fact that companies are losing control of their costs because of outsourcing. This has limited cost control to "…only those costs that are contained within the four walls of their business entity" (Christopher, 2005). They point out that today's price competition takes place not between companies but between supply chains. (Christopher and Gattorna). The proper view of costs in setting prices has to be "end-to-end," (Christopher, 1992) since all costs in price setting will be reflected in the price of the finished product in the final marketplace.

The authors point out that contract manufacturing has also reduced the degree of cost control of industrial firms. Since cost control is gradually being dispersed throughout the supply chain, it makes sense for a company to seek cost reduction in the wider supply chain. They point out that this can be accomplished by "reducing the cash-to-cash cycle" (Christopher and Gattorna). Another strategy for higher margins is through the alignment of a company's supply chains with its customers' logistics needs, thereby creating more value and more stable pricing (Christopher and Gattorna). By managing and designing supply chains to fit the logistics requirements of customers, including delivery times, packaging types and design, inventory levels, just-in-time programs, warehouse and depot locations, inbound and outbound transportation strategies, and purchasing programs, an industrial firm can set its prices based on the tangible value-added it provides through its supply chains.

3. Obstacles to effective industrial pricing

An important dimension to price setting in industrial firms is the impact that the firm's internal organization and political system, as reflected in interdepartmental coordination and rivalry, has upon price setting (Lancioni, Schau, & Smith, 2005). The authors point out that a company's pricing strategy has a substantial economic impact on the firm in contrast to other financial management options available to it. For example, they present the fact that only a 5% decrease in the average selling price of an industrial product increases earnings-before-interest-and-taxes (EBIT) by an average of 22% (Lancioni et al., 2005). They point out that price setting is difficult given the plethora of internal and external economic political influences that shape a firm's pricing decisions. The authors conducted a study of leading US industrial firms where they examined the departments in companies that make pricing strategy development difficult and identified potential courses of action to overcome the obstacles to the price setting process. The authors discovered that, in a majority of industrial firms, the finance department puts up the most obstacles to effective price setting and execution.

4. Managing international pricing strategies

In developing international pricing strategies, industrial marketing managers typically take into account a wide array of factors that are both internal and external to the firm. A