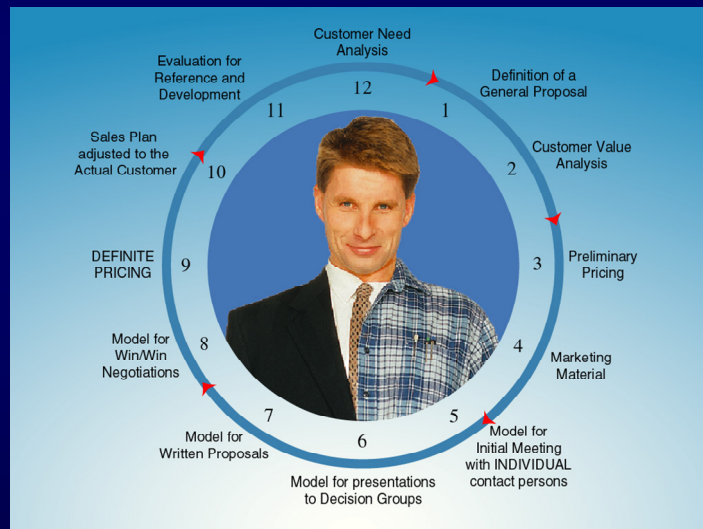


Rosvall

The ALTERNATIVE *to Price Competition*



Teknosell®

On the language in this paper

This paper is written in international English. All words have passed the proof-reading if they can be found in any of the eighteen (18!) spell-checks in Microsoft's Word-program, ranging from English written in Australia over India to USA.

English is a truly international language, which makes it so rich. Most nationals can find a little bit of their own in it. Our favourite is the word "smorgasbord", which only lacks two dots above the first o and a ring above the a - otherwise it would have passed the Swedish spell-check also.

Anyway, we hope that the reader will find the content of this paper more interesting than the peculiarities of the language.

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In the good old days . . .

Once upon a time, not very long ago, it was easy to be a businessman. You only needed common sense. Common sense told you that prices had to be calculated and that every business deal should carry its own cost. This strategy was very well suited for the mass production and the mass marketing of standard goods like nails and pulp - but it was also very well suited for complicated machinery like electro-mechanical telephone switches, because of the long life cycles of the products.

As the product was well known and hard to differentiate, *a lower price always won the order.*

As the product was not differentiated, you could run the production without knowing who finally would pay the bill. You could use stocking as a buffer when the demand fluctuated. *You could take capacity utilisation for granted.*

Given this, you could apply cost based pricing and full cost profitability analysis, fostering an efficient administrative business culture. This strategy paradigm circled around price competition based on cost effectiveness.

The back office could take the two most important decisions: "*What should we charge?*" and "*Which business deals should we accept?*"

However, if your company supplies technology and knowledge intensive services, products or systems, the Cost/Price Strategy has become obsolete.

engineer

*to originate, cause, or plan in a clever or devious manner
(Latin: ingenium)*

The New Collins Concise English Dictionary



Business Engineer

a person with an extraordinary ability to design a customised problem solution and, above all, who can communicate its value to the customer

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A New Era in Business

Value based Pricing

If your company supplies technology and knowledge intensive services, products or systems, *a low price is not the most effective competitive weapon*. Your customers want the best rather than the cheapest. Who, for an example, wants to buy a brand new, but three year old model of a computer system at a 20 % discount?

When you supply technology and knowledge intensive services, products and systems, being cost effective is not good enough. You must also be revenue effective. You must apply *Value based Pricing according to Customer Perceived Value*, in order to secure the gross margins needed for the development and communication of values.

A new corporate hero

To sell on Price is not as difficult as to sell on Value. It is *easier to ask* the question: "Why pay more?" *than to answer* the question: "Why do I have to pay more to you?"

To answer this question *you have to be able to translate technology and knowledge into customer value*. This requires an extensive training and experience in the trade, plus a specialised proficiency in business skills. *A person with these qualifications we call a Business Engineer*.

Nowadays, specialists cannot exclude themselves from the business development any more. Every key person has to have a holistic view of the business she is in and take part in the business development process.

They have to become Business Engineers.

The era of Business Mechanics is over.

The customers pay for benefits - not for costs!

Thinking about it, it is obvious that the customers do not pay us because we have accumulated costs. They pay us more or less because of the comparative competitive value we can offer *and the value they can perceive before the deal is done.*

How come then that a majority of firms still calculate their prices based on full costing?

The alluring charm of the Price/Volume Strategy

The charming simplicity of the traditional Price/Volume Strategy is little short of irresistible.

"Calculating what we must have" is so much easier than "finding out what we can get."

"Calculating what we must have" can be done with the help of a computer system in the office. In order to "find out what we can get" we shall have to leave the office and look for the answer in the bewildering world of a competitive market.

A costly convenience

It is easy to show that cost based pricing is a very costly convenience.

The reason why it is costly is that the market only corrects our mistakes downwards.

If we, for instance, add up a lot more costs to perform a service or deliver a product than our competitors - without creating supreme value for the customer - then we have "calculated ourselves above the customer perceived value." No problem. The market will tell us very loudly.

However, if we by a stroke of genius manage to create supreme value for the customer with less cost than our competitors can - will a professional buyer then tell No, he will still tell us that we are too expensive. A good deal can always be better with a lower price.

So, if you start the pricing "at the wrong end", i.e. with the costing, then you will always end up at a lower price level than if you had bothered to start with "finding out what you can get." This means that you are spending a fortune on the wrong competitive weapon - a low price - when you need every penny for development and communication.

Moreover, if you have decided that Price is not your main competitive weapon, a price cut is a fat wallop in the blue air. Of what avail is it, if you offer the customer something cheap, when the customer wants the best? The only thing you accomplish, is to do away with the gross margin you so desperately need to develop the best alternative!

This does not mean that you can skip the costing! We are only talking about the order of the proceeding.

Great Confusion

Focusing on the value perceived by the customer instead of the cost of our operation, is no less than a shift of paradigm in business.

A shift of paradigm leads to confusion.

The cost-based paradigm is rooted in a hundred years of successful business development in the industrial era. Basing your pricing and profitability analysis on solid costing created law and order in the company. Value based price and business development creates chaos. However, we have to learn to thrive on chaos, as Tom Peters wrote in his famous book*.

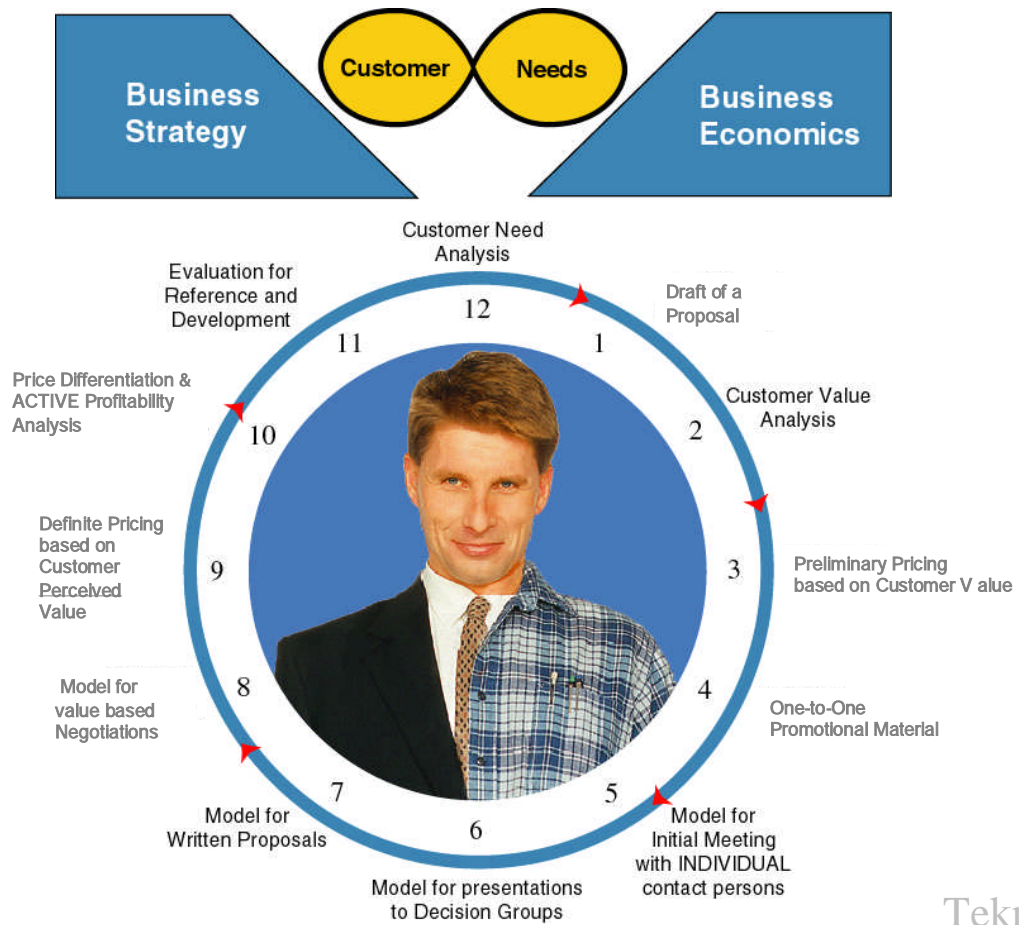
Nowadays, when we cannot isolate the pricing from the rest of the business development any longer we desperately need something else to create at least some order in the chaos of post-industrial price and business development.

May we suggest the following model?

* Peters, T., "*Thriving on Chaos*", A.A. Knop Inc., USA

A model for post-industrial
PRICE and BUSINESS DEVELOPMENT

The Business Engineering Process



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A time-tested model

The model we propose implies a process aimed at creating a customised solution to a relevant problem that is worth solving for the customer as opposed to the mass marketing of standard commodities. Our model is suited for computer systems, computer aided log chipping, customised paint spraying systems or management training programmes, etc..

The model has evolved through more than twenty years of practical and academic work and it has been accepted by a large number of international technology and knowledge intensive companies.

The Strategic Level of the model

Unlike the old type of industrial firms, a post-industrial company is not naturally limited in its business development by its fixed assets. If you are running a paper mill, you hardly start production of polyethene film on an impulse. But the great brains in a technology and knowledge intensive company find it very hard to resist a customer who presents a new exciting problem only adjacent to our core business

- unless they are guided by a clear and firm strategy.

In a post-industrial company, where people are more important than machinery, all key people have to have a clear understanding of the company strategy. Otherwise, the strategic focus is quickly lost. That is why the model starts with the infinite customer needs being screened through a funnel consisting of our strategic and economic constraints.

The Operational Level of the model

When a business proposition has passed the strategic/economic funnel, it is accepted into the operational level of the model.

We have chosen a clockwise description of the operational level of the model because modern Price and Business Development is a race where time to market is decisive.

During "the first quarter (00 - 03) we analyse a Draft of a Proposal based on a Customer Need Analysis as to its Customer Value, whereupon we draft a Preliminary Price based on this theoretical customer value.

However, it is not recommendable to base a price on customer value. We should base it on customer *perceived* value. The difference is the "communication kit" we develop between 4 o'clock and 9 o'clock in the model.

Please note that the ambition in this communication is much higher than usual.

In the old cost based paradigm, it was only necessary to reach the minimum communication level where the customer accepted our calculated price. Now our communication is decisive for the price we get. We get the price we can motivate and it is when we lack good arguments and cannot answer objections that the price comes down.

Around the clock

The clockwork also indicates that post-industrial Price and Business Development is an iterative process.

The first iteration around the clock is done with colleagues in the office. Maybe the second and third also, if we find that we have to adjust ourselves after having checked facts. When it is time to present the proposal to an actual customer, it takes very little time to adjust the model to the facts valid in this specific case. These facts and experiences are then used for sharpening the model one step further with every following business deal.

Would you like to read some more?

This leaflet is an excerpt from the book

VALUE BASED PRICING B2B **- a modern approach to Price and Business Development**

This is a radically revised edition of the book “The Business Engineer” originally published by The Institution of Electrical Engineers in London, about which the famous BBC profile Sir John Harvey-Jones wrote:

“... I can think of no greater help than this excellent book, which covers the subject both in its simplest and most direct terms, but also involves much of the more sophisticated business thinking currently available.”

If you want to order a copy (or want a special offer for a quantity) please visit www.rosvall.se/books

What can we do for you?

Teknosell[®] is a network of academics and experienced business consultants focused on value-based. price and business development.

For more than twenty years, we have assisted technology and knowledge intensive companies as consultants and coaches. This has given us a unique experience and knowledge of the short-cuts to an efficient Value based Price and Business Development, resulting in better prices as well as higher sales volume. If you want to know more, please contact

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