

The Power of Pricing

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"The single most important decision in evaluating a business is pricing power. If you've got the power to raise prices without losing business to a competitor, you've got a very good business.

And if you have to have a prayer session before raising the price by 10 percent, then you've got a terrible business."

Warren Buffet

It has been a very challenging time for the MDF and Particleboard Panel business' within South East Asia due to the recent expansion of new capacity seeking out market share. This has created a lot of uncertainty within the market and many companies have approached pricing in a very reactive way. Many companies see pricing as the only way to maintain market share, often destroying hard earned price premiums built up over many years of loyal customer service.

Taking a pure, short-term view on price adjustments without having a contingency plan is the equivalent of

smashing the "In case of Emergency, Break Glass" panel to put out a fire. Odds are, if you are breaking that glass, you are already in a bad situation.

The basic arithmetic should be blatantly simple; when a business wants to manage a margin position amid cost and volume uncertainty, pricing is paramount. Bluntly dumping prices risks reputational damage, even more importantly, a blunt price reduction is often the product of an incomplete thought process on what the effects of the price reduction will be. Price is the biggest profit driver for any company, research has shown that a mere 1% change in price has a multiplier effect of between 6% and 30% on Gross Profits. Furthermore, any reduction in pricing will have a disproportionately high negative effect on Cash Flow.

I am not referring here to any abuse of power to control pricing levels, rather I am highlighting the issues companies face not just in the wood panel business but for all timber and furniture related businesses.

"The single most important decision in evaluating a business is Pricing Power." Warren Buffet

This is all the more reason to pursue creative, intelligent, and responsible price management in a time of uncertainty such as the current imbalance in Supply and Demand. Price management is the only remaining option for companies who want to survive now and thrive later. What separates these thrivers and survivors is a strong capability around price management with clear objectives, knowledgeable people, streamlined process and a flexible system.

Some advice on how to create a **Positive Price Management Strategy** would be to; -

- **Link the Customer Experience to Value.** You may have a wonderful product, but it will only mean something if you are able to communicate its value to the customer. Companies work intensively on creating the perfect experience, but forget to tell their customers, or even their own sales teams.
- **Create a Sales Management Structure that reports not only on Volume.** Most companies Sales Reports focus only on the volume numbers and ignores the broader impact pricing may have on the overall business. Sales incentives should include items such Profit Contribution and Cash Flow.
- **Re-think Customer needs for a "True" Relationship.** The best customer experiences offer much more than just the product. **Relationship = Product + Service.**
- **Optimised and Conditional Discount Structure.** Often the best customers do not get the best prices, those customers that complain the most get the biggest discounts. This leads to inconsistencies and frustrations within the business, so a more structured approach should be taken.
- **Create Value Based Price Lists.** Whilst products are rarely sold at list prices, these Price Lists are a tool to communicate the Value of a product. Many lists are produced on a Cost Plus calculation rather than reflecting the value of that product.

"You can determine the strength of a Company by the amount of pain it goes through to increase prices." Warren Buffet

I hope that this insight into the importance of pricing will help businesses to make informed and intelligent decisions. 📖