Inflation as a Catalyst for Change

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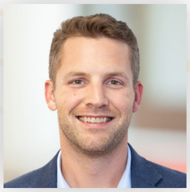

Getting ahead of rising prices in an inflationary environment is one thing; staying ahead is another. Data, technology, and savvy management can turn cost pressures into pricing opportunities, as the authors explain. Although focused on private equity, this article provides insights that can be applied by pricers dealing with the challenges of widespread inflation. Hugh MacArthur is a Partner in Bain's Boston office and Head of the Global Private Equity practice. He can be reached at hugh.macarthur@bain.com. Shawn O'Brien is an Associate Partner in Bain's Denver office and is a leader in the firm's Advanced Manufacturing & Services practice, with particular focus on go-to-market, growth, and full potential transformations. He can be reached at shawn.obrien@bain.com.

Getting ahead of rising prices in an inflationary environment is one thing; staying ahead is another. Private equity firms that learn to manage inflation over the long term are most likely to generate differentiated performance in this highly volatile economic environment.

Many, if not most, of the companies in private equity portfolios are midsize enterprises run by management teams that have never before seen an 8% jump in the consumer price index. They typically have limited data on how they price, who influences those decisions within the enterprise, and whether they are actually realizing the prices they've set.

That presents a challenge for teams trying to react thoughtfully to sudden cost pressures. But it can also create opportunity for firms that understand how to bake inflation management into their value-creation plans. Playbooks that make full use of customer and market data lead to better, more strategic decision-making around both pricing and costs.

After initial pricing moves, thriving in an inflationary environment over time depends on building pricing strategy into the weekly, monthly, and quarterly planning process. That means deploying scorecards that use data to monitor specific pricing moves, whether those moves are being fully realized, and how they are affecting volume. This sort of rigor gives leaders what they need to stay on top of pricing strategy. It also gives them visibility into where things like discount authority, differential payment terms, and unallocated freight expenses create leakage that erodes realized price. Plugging those leaks can, in effect, increase prices without actually having to push through another increase.

But the private equity firms managing through this period most effectively recognize there is more at stake than simply maintaining margins. They're finding ways to create new value, using pricing and cost management strategically to focus portfolio companies on where they deliver the most value to customers. Pricing to value rather than just pricing against cost can be a powerful driver of profitability. But it requires developing an intimate understanding of your customers and the trade-offs they are willing to make between your offerings and those of competitors.

Insights into brand strength, product preferences, and other drivers of purchase behavior allow companies to price aggressively where they can and tread more carefully where they still need to build a stronger value proposition with customers. Those insights also inform how best to think about cost management amid inflationary pressures. While it may be critical to manage rising input, labor, or logistics costs, it is equally critical to know where not to cut so as to protect signature customer and employee experiences. A holistic approach anchored in the company's broader strategy points to a balance of pricing and cost actions across the product portfolio.

Every portfolio company is different, of course, but for many, this approach to pricing and cost will essentially become a new capability—one that reimagines how you can deliver products and services most efficiently without dampening the customer experience. This takes investment, but the results can be scaled.

Inflation, in other words, has become a catalyst—an opportunity to break down old ways of doing things and find ways to use data, technology, and new management approaches to deliver better customer experiences with attractive economics.