Pricing Pains Are Hiding in Your Dated ERP

by: Barrett Thompson

Enjoy this throwback article from 2020, recently updated for current context, and one of the most popular Zilliant articles to date. It details how companies tend to shortchange their pricing capabilities by conforming to the limitations of their aging ERP (Enterprise Resource Planning) system, and how a real-time pricing engine offers a way out. Barrett Thompson is the General Manager of Commercial Excellence and leads the Business Solutions Consultant team, aligning Zilliant solutions to customer needs and promoting pricing and sales best practices among customers. He can be reached at barrett.thompson@zilliant.com.

What would you think of a business that did the following? Imagine with me...

A wholesale distributor uses a very old ERP system that was only built to handle five-digit SKUs, meaning it can only offer 99,999 unique SKUs to its customers. Meanwhile, the average competitor sells 300,000 SKUs. Yet the distributor decides this is just fine: "We'll just ignore those other 200,000 SKUs and take a third of the market share and revenue we could be earning." Even though the number of SKUs a distributor carries is a deeply strategic choice, the company's leadership team is willing to sacrifice its future success by a technical limitation introduced decades ago.

You would, of course, be rightfully shocked by this decision. The logical solution is to figure out your inventory strategy first – what to carry and why - and go from there, rather than let the 20-year-old ERP dictate your market potential. The tail shouldn't wag the dog.

Any savvy businessperson will recognize the absurdity here because smart people do not accept such arbitrary, technical constraints on their business. Right? Well, you might be surprised.

What if I told you there is a HIDDEN way in which companies severely kneecap themselves in a similar fashion every day? Many businesses have implemented a version of this when it comes to managing their pricing by conforming to the rigid pricing capabilities of their legacy ERP. The problem is an insidious one that I continue to see in many businesses.

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Though not as glaring as the example above, it can be just as damaging to financial performance when companies strain to fit their pricing strategy into the inflexible, less-than-ideal confines of their system of record.

To be clear, this is not a conspiracy or a plot. It's just not very visible outside of the pricing or administrative teams. We're at a point at which a majority of multi-billion-dollar companies know that pricing is the most important lever available to increase profitability. Thus, major investments are made each year in consultants and pricing strategy, only to have it all shoved out the window thanks to the harsh reality that often exists – instead of picking systems that support our price ambitions, we've stripped down our price ambitions to fit into our ERP capabilities.

Four Examples of the ERP Pricing Bottleneck

Quantity-Break Pricing

A common example is when a company's ERP lacks the ability to perform quantity-break pricing. When an analyst goes to load a price for a product in such ERPs, he or she can only enter one number. What does that mean in practice?

Say the business is promoting a quantity break to its customers when more than 50 units of a given SKU are purchased. With rigid ERP constraints, a rep has to intercept each qualifying order and do a manual price override to achieve the quantity-break price. This scenario plays out over and over again, introducing the potential for human error, lost productivity, and rote-task burnout.

Lack of Pricing Dimensions

Another limitation I see is when the ERP system will not allow

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sufficient dimensions to be set up in a price matrix. Companies often want to differentiate price by region, industry, customer type, and more. But what if you can't factor in the additional dimensions? Consider a parts provider who serves both the automotive and aerospace industries (among others). There is a wide variance in willingness to pay in these two customer segments.

The company is global so it has to set up a country dimension in the price matrix, but it may not be able to add an industry dimension because the ERP can't support it. The effect on price is drastic. This company may choose to offer a price on a part that is low enough for automotive customers to buy it, causing them to bleed margin on the same part for aerospace customers.

Conversely, if the price is set initially at the higher aerospace level, the result is hundreds of manual price exception requests for the automotive customers, or the loss of the automotive business altogether if they simply offer the matrix price in a take-it-or-leave-it fashion. Companies like this have to make a devil's bargain: either give up the margin, give up the revenue, or create a ton of work for your sales reps and price analysts.

Limited Functionality

Some ERPs are extremely limited in their pricing methods. I've seen systems whose entire pricing function boils down to taking a cost and marking it up. But I have customers who say, "I'd rather do a discount from list price than a markup over cost. If I go change those list prices at any time, I want all of my customers to see the new prices dynamically."

This is a sound modern pricing strategy laughed away by many ERPs. I run into pricing teams that are forced to work around this limit by maintaining a spreadsheet of all their customers and their agreed-upon discounts from list for each item. Any time they have a list price change, they have to back-calculate their cost-markup to align to the net price implied by the discounts, then embark on an ugly process to get those markups loaded into the ERP.

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This situation could occur either because the ERP simply doesn't have the capability to handle discount from list calculations or, when it was implemented 20 years ago, someone chose "markup over cost" rather than "discount from list" and now that has become deeply entrenched in systems and processes which are lost in the mists of time. The prospect of reconfiguring the ERP to match the latest strategy is untenable. This is how companies quietly hold their business hostage to either the inherent incapability of their ERP or to a sunk-cost implementation choice from back in the day.

Customer-Specific Price Agreements

Finally, let's talk about customer-specific prices, which is a common and necessary price type in a business. However, many ERPs don't understand the idea of an agreement object. Instead, they operate strictly on single price-exception records: essentially a line item that says, "This customer pays this price for this item." At first, it's not an issue. But over the course of time, you might have 150 such lines for an individual customer, they're not grouped together under the customer's ID, and there is no way to easily run a report of special prices currently in effect for the given customer.

For many, the only way to figure out what a customer's special prices are is to follow this nightmare process:

- Create a dummy order with the customer's ID on it
- Put all 10,000 SKUs from the catalog on the order
- Run the order through the ERP's pricing logic
- Get back the prices on all those lines
- Compare each of those lines with the list or matrix price
- Search for lines that don't match up to the list or matrix to deduce a special price
- Filter on these non-matching lines to create the price agreement you have in effect with the customer

An unfortunate pricing analyst has to do all this work just to get sales an accurate record of the special prices for a single customer. It's slow, it's manual, and it's backward. When it's time to renew prices on that agreement, how do you do that? First, you have to go back through that ugly process, then ask questions like, "How much did they buy from me last year?" or "What was the revenue impact?" or "What was the margin performance?" No one has any sense of the history.

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Three Potential Responses

Businesses whose pricing strategy is constrained by their ERP generally take one of the following tacks.

Grin and Bear It

Accept the constraints of the status quo, often due to the perceived pain of rearchitecting the ERP. Use heavy doses of manual effort and Excel sheets to work around issues when possible.

Wince and Fix It

Undertake a costly and difficult project to get the ERP to function the way you want it to. In addition to the upfront project costs, companies will often have to bring on headcount to maintain and reconcile prices within the ERP going forward.

Invest in a Pricing Engine

There is a third door that provides reliable, robust price optimization and management capability to relieve the technological, administrative, and process pains inherent in any outdated ERP system. The right application can actually replicate the ERP's existing logic and connect to a real-time engine to execute price calculation and data lookup logic dynamically. This simplified and centralized architecture sits alongside ERP, becoming the new pricing system of record. The real-time pricing engine can then perform the desired pricing functions and deliver prices to commercial execution systems like CPQ, CRM, or eCommerce - in a matter of milliseconds.