PROFESSIONAL PRICING SOCIETY

The PRICING ADVISOR

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In this piece Dr. Ekkehard Stadie and Martin Deutschenbaur look at current telco pricing models and why they need to change, providing pricing advice applicable to multiple industries. Stadie is a Senior Partner at Simon-Kucher & Partners, where he heads the global Telecommunications and IT competence centre. Deutschenbaur is a Director at SKP in London, where he heads the Telecommunications, Online Business and Technology Services competence centre. This article was originally published on Telecoms.com.

In This Issue:

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Today's Pricing in Mobile and Fixed-line Networks is Toxic

Revenue and profit sources of mobile and fixed-line network providers are under much more pressure than originally thought. Users are radically changing their behaviour, over-the-top (OTT) offers are highly competitive, and, most of all, non-future proof toxic price models are in place.

The most recent wake-up call came in the form of Facebook's takeover of WhatsApp and its announcement shortly thereafter that it will start offering voice telephony. **Classic telecommunication providers need to carefully scrutinize how services are priced. Simply pricing units of megabytes, minutes and text messages is no longer sufficient to maintain profitability and growth.**

The following six challenges have to be tackled with effective pricing solutions:

1. Mobile data usage with lower growth potential than expected

Data volumes in fixed-line networks have grown much more than in mobile networks. "Commercial" Wi-Fi offers will cannibalise mobile data usage. It's standard nowadays for restaurants, hotels, airports, companies and public transport to offer their customers and visitors free Wi-Fi. There is no urgent need to use mobile data offers in these places. The clear winner in volume growth is the fixed-line network.

- The telecoms industry is just beginning to re-balance its price models from voice and text messages to data. Maximum price differentiation on the data side is not fully exploited yet. On the contrary, CAPEX-intensive industries, such as airlines, railways, and logistics are becoming increasingly mature in their progress towards strong price differentiation. In the telecoms industry three data dimensions are still growing: the need for data speed/performance, the data volume (sum of fixed-line

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PPS Happenings

Serving the Pricing Community Since 1984

Upcoming Events

27th Annual Spring Pricing Workshops & Conference – Loews Chicago O'Hare Hotel – Chicago, IL / May 3-6, 2016

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and mobile) and the number of internet connected devices. Data pricing should not only focus on the transferred data volume; pricing also has to incorporate other price elements like quality of service, priority, and speed/performance. The optimal price differentiation elements depend on the market position, general positioning and assets of the provider.

2. Data roaming revenues under pressure through Wi-Fi

This highly profitable business line is not only feeling pressure from regulation, it's also affected by the Wi-Fi substitution. Many customers would rather commute from one Wi-Fi hotspot to the next instead of going through the effort of booking an extra data roaming option.

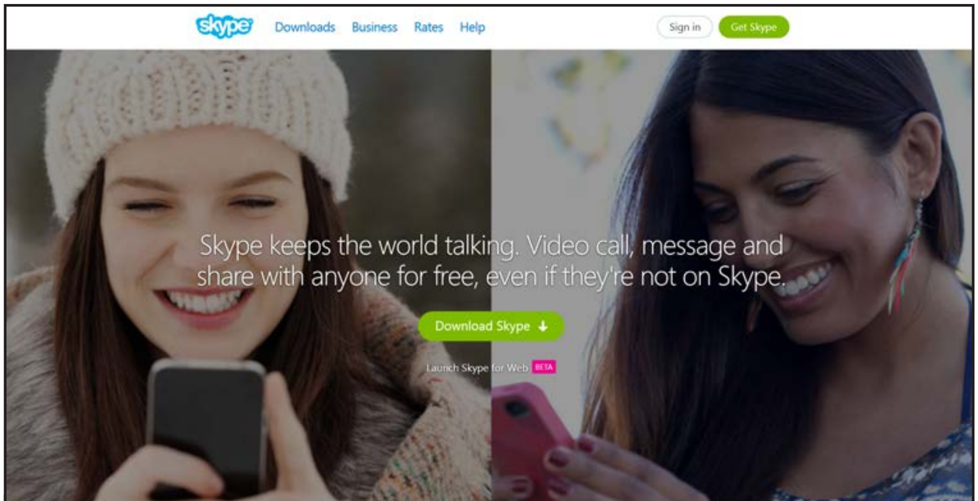
- Pricing is an effective tool here. An option for a different approach to pricing is the bundling of services, for example the packaging of roaming calls and data with national services. The proposition "calling and surfing like you're always at home" meets the customer need of a worry-free solution and increases positive customer experience.

3. Voice roaming revenue under pressure through OTT solutions

Voice roaming calls, still considered expensive, are partially being replaced by better and free solutions. FaceTime and Skype are more multi-media-oriented, and to some extent, qualitatively better.

Also in the B2B area teleconference calls and longer conversations with far-away locations are more attractively served by OTT providers. In its Skype service, Microsoft already offers multi-media features like group video calls, screen sharing and calls to specific countries can be added on.

While this offer can still be considered as a consumer/prosumer solution, Microsoft offers the corresponding multi-media functionalities also through Lync in a business environment.



In its Skype service, Microsoft already offers multi-media features like group video calls, screen sharing and calls to specific countries can be added on.

- Pricing can help here through bundling of services and the introduction of other price elements like quality of service and priority as well as the integration of additional services like video calls and file sharing. The key here is to extract the right product and price dimensions for the additional customer benefit delivered.

4. Text messages not yet re-positioned

The text message is an outdated technology. We are already seeing mass migration to offers such as WhatsApp. Yet text messages are the most reliable means of delivery, have the highest degree of privacy and have the most direct character of all messaging forms in business communication. But text messages are at the end of the life cycle. The end can only be slowed down.

- There are essentially two pricing options: either re-position the text message as a 100% reliable and secure premium service (delivery guaranteed to all networks with the highest level of privacy) with the suitable unit pricing on a much higher level, or offer it as a paid extra service bundled with other services.

5. National voice usage revenue can only get protected by differentiated service pricing

National voice usage is decreasing for many reasons. For one, OTT messaging is replacing traditional calls. Also, calls are being substituted by multi-media OTT calls. In the "Postpaid" area a revenue safeguard is reached via unlimited voice offers.

- Pricing can generate added revenue through product and quality differentiation (e.g. HD voice, priority). For "Postpaid" customers that are not yet making calls with unlimited propositions and for prepaid customers, a proactive migration into unlimited voice models should be considered.

6. Home data usage is rising, but hardly being charged. In the current price model access can even be substituted

As with public Wi-Fi hotspots, unlimited data usage is the dominant business

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model also for residential internet access.

In an IP-based environment, it makes little sense for all apartments of an apartment building to separately pay £20 to £30 per month for a fixed-line internet connection. Instead of e.g. eight individual connections one connection with a higher bandwidth and a Wi-Fi router for £50 per month would be enough for the whole building.

- Pricing can counteract this risk either by getting rid of unlimited data usage or by switching the price model away from household connection to the number of internet connected devices. Pricing of internet connected devices offsets old categories (fixed vs. mobile voice and data) and focuses on the full communication needs of the household. A pay per device price model could aim to differentiate prices for additional devices connected to the internet (e.g. smartphone, tablet, laptop) next to a base offer price which includes all household services (e.g. fixed broadband, voice and TV). The price level has to depend on the brand strength and the network quality of the provider.

Innovative price models can help to detox current pricing structures. The optimal pricing solution however depends on multiple factors like market environment and positioning of the provider. Telecoms companies have to evaluate different routes as there is no one size fits all solution. Price model changes are needed and beneficial for telecoms companies but they are the "decathlon" of pricing: a lot of experience and practice is required. It is like flying, the rougher it gets the more experienced the pilot has to be.

Price model changes are needed and beneficial for telecoms companies but they are the "decathlon" of pricing: a lot of experience and practice is required.

New pricing approaches: The time to act is now!

It is time for a completely new approach to strategic pricing. Voice, text messages and roaming are going through a downturn. Data volume is migrating at a high level into fixed-line networks with unlimited usage models that do not monetise any usage increase.

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Bed Bath & Beyond's Persistent Coupons and the Return of Thrifty Customer

The holiday shopping season always brings discussions of pricing and discounting strategies to the forefront, and especially debates concerning the issues related to online vs. brick and mortar retailer competition. In this article, the author presents several pricing strategies that retailers can employ to entice holiday shoppers without reducing all important holiday profits through excessive discounting. Rafi Mohammed is the founder of Culture of Profit LLC, and author of The 1% Windfall: How Successful Companies Use Profit to Profit and Grow. *He can be reached at rafi@cultureofprofit.com. This article originally appeared on the Harvard Business Review web site at HBR.org.*

It's going to be a rough holiday season for brick-and-mortar retailers. For starters, Amazon is heavily promoting its Prime program, which makes online shopping more attractive by providing two-day shipping. Jet.com recently entered the e-commerce fray with a pledge of being 10–15% cheaper than online rivals. Wal-Mart, a company whose primary weapon is discounting, is under pressure to boost its web sales, which made up just $12.2 billion of its $476 billion in revenue last year. And consumers, already attuned to price and accustomed to discounts, are becoming used to free, fast shipping from e-tailers — so they need a good reason to visit a physical store.

What does this mean for brick-and-mortar retailers? It's not feasible to lower prices across the board to match the web ("Our prices are the same as Amazon") since Internet retailers typically have lower operating costs. **The answer is to play defense: use surgical-strike discounts to entice customers who are at risk of defecting due to a cheaper price.**

When a company is losing sales because of price, its overwhelmed leadership might try to resolve the problem with one big price cut—but that strategy is a mistake. It's important for the company to embrace the fact that not everyone is concerned about price. In fact, many current customers are paying full price already. A better strategy is offering discounts with built-in hurdles, or requirements that must be "jumped over" in order to receive the lower price. This method enables a company to provide discounts to customers who require them while simultaneously charging full price to customers who are willing to pay it. Customers who make the effort to clip, store, and redeem coupons, for example, are credibly stating "Price is important to me."

Sales brought about by coupons can be significant. Bed Bath & Beyond's ubiquitous 20%-off postcards, for example, are helping overall sales: the store's revenue rose 1.7% in the most recent quarter. But increased coupon usage is starting to hurt the company's net profit, which dropped by 10%. The company's CFO highlighted "an order of magnitude" increase in coupon expenses—primarily higher redemption rates—as the key culprit for the profit drain.

It's easy to demonize coupons for depressing Bed Bath & Beyond's profits, but the company is lucky that it had its coupon strategy in place. Without it, profits could have been even worse. Since Bed Bath & Beyond hasn't mentioned a material change in its couponing strategy, the increase in redemption rates is a sign that more customers are becoming price-conscious. With customers becoming more price sensitive, consumers started using the ubiquitous coupons — instead of not purchasing from Bed Bath at all.

Providing the 20% discount option grants thrifty customers—an increasing number of whom likely would have purchased from an online retailer—permission to shop at a brick-and-mortar retailer where they assume the prices are relatively higher. So while an increase in coupon redemptions isn't optimal, some margin is better than no sale at all.

Target, with its similar goal of retaining price-sensitive customers, has chosen a slightly different strategy of offering discounts with hurdles. It made a big splash recently by announcing it would match the prices of 29 rival retailers (up from the five it previously matched). To receive a lower price, customers must show proof that one of the 29 retailers is selling the product for less. Is this a game changer? Not really. Target is simply admitting that its prices aren't necessarily the cheapest, so a customer who is inclined to do so should check prices at the other 29 web sites and shop Target last. This hurdle results in discounts being awarded only to those who demonstrate they care about price.

Hurdles aren't relevant only to brick-and-mortar retailers that are battling internet foes. **Every B2B and B2C company should employ hurdle discount tactics such as couponing, price matches, rebates, and periodic sales to serve customers who wouldn't otherwise purchase there.** Depending on the level of competition, hurdles can be used as a defensive or offensive pricing tactic. In price-war situations like brick-and-mortar vs. the internet, hurdles *retain* customers who may defect to a discounted rival. In less-competitive conditions, hurdles can be used as an offensive strategy to *attract* customers who otherwise would not have purchased.

Budget-conscious customers are on the lookout for deals. If you offer a discount, they will come. Employing surgical-strike discounts such as hurdles can help target these customers while minimizing the chances of full-paying customers also taking advantage of the lower prices.

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Outcome Based Pricing: A Practical Approach to Applying Value Based Pricing

In today's market, power has shifted to the buyers, who are more educated and socially connected than ever. As such, sales and pricing models must evolve to accommodate new buying behaviors and dynamic market conditions. This article provides practical examples of how Outcome-Based Pricing can offer a better way to work with your customers and stay ahead of your competitors.

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There is a new corporate reality upon us that is driving the need for new pricing models.

On the one hand, there is a renewed top-down focus on profitable growth, with senior executives increasingly compensated on profitability. Sales leaders, almost half of whom report having profit as a component of their compensation, are looking for better, more profitable and more defensible Sales strategies.

At the same time, **tectonic changes have shifted the power from sellers to buyers, who are now fiercely independent, highly social and connected, and more educated than ever.** Buyers have clearly evolved.

This new reality is changing the face of B2B Sales. Sales reps now need to be experts in their customer's business and be armed with new selling and pricing models that break with tradition.

The pricing function has an opportunity to step up to this challenge and support the organization with the development of better, Outcome-Based Pricing models.

Looking to the past, the Traditional Sales Rep....

- Sells from the list
- Understands his products and sells the technical features and their benefit
- Finds it increasingly hard to differentiate vs. the competition

… and lives with the draw backs of this traditional approach.

In comparison, let's take a look at examples of how Outcome-Based Pricing can offer a better way to work with your customers and stay ahead of your competitors.

Lighting Distributor in California

This distributor sold their products and services to supermarkets in a traditional way: per unit and then a fee per hour for any follow on services. As you can imagine, this is a fairly commoditized market and competitive offers were easily compared. Winning basically came down to the best price.

However, it was not light from the bulb itself that the supermarket valued, but the security for their customers resulting from a well-lit car park. If one of the lights in the car park was broken, the supermarket would call for a service engineer to come out. If this took too long, customers would complain that the car park was not safe and eventually even take their business elsewhere.

One sales rep, after talking to a store manager, came to realize what the true value of his offer was and recognized an opportunity to change the game. He returned with a pricing model based on a per hour of fully lit car park. If a bulb is broken, the supermarket does not have to pay. Of course now, bulbs do not break. The distributor has his service teams running regular checks. The result is a significant reduction in costs, because staffing for emergency call-outs has declined and the supermarket is a happier customer, even using the guarantee of a safe car park as part of their marketing.

Explosives Supplier to the Mining Industry

Suppliers in this market sell explosives, blasting caps and ignition systems for triggering those explosives. These are traditionally sold on a per unit basis.

In response to downward margin pressures, suppliers have innovated by introducing outcome based contracts with invoicing based on a new unit of measure: ton of mine output. So, how does this work? The customer and supplier agree on a daily mine output and on an audit mechanism to measure output.

The Supplier:

- Delivers explosives, blasting caps and services.
- Manages inventory for the customer: they never run out of explosives.
- Consults on blast patterns, driving

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efficiency and limiting waste. Ultimately improving the yield on the customer's operation.

- Takes ownership for the mine's actual explosive consumption.

The mine outsources blasting to the experts, who know how to maximize the yield of their products, while lowering costs and gaining predictable costing. The output based pricing mechanism has created value for both seller and buyer.

So, looking to the Future, the Outcome-Based Pricing Sales Rep:

- Understands his customers' needs
- Sells what the customer wants
- Prices based on customer value
- Finds it easier to differentiate vs. the competition

Outcome-Based Pricing clearly has its benefits, but if it makes so much sense, why isn't everyone doing it? In simple terms, it requires change – of your organization, in your customers and/or even in the industry – and it's never easy to lead change.

If however, you get there first, the prize will be well worth the effort.

So, where should you start?

- Think about what the customer values and what defines their willingness to pay.
- Review the applicability of the model. It will not be applicable everywhere, for all customers in all countries.
- Look for opportunities to monetize services that have previously been given away for free in support of the per unit sale.
- Establish what type of outcome based pricing models should be employed and how you are going to structure the model.
- Review execution capabilities and ease of deployment. It is generally fairly easy to come up with the models, but much harder to deploy and execute them effectively.
- Ensure the model can be measured and most importantly accurately invoiced.

> Look for opportunities to monetize services that have previously been given away for free in support of the per unit sale.

Think of all of these points in terms of market types, where different strategies will be applicable, and then be prepared to adopt a phased approach towards full deployment of a risk shared model. You may not be able to get there in one go.

Then, make sure you can monitor the effectiveness of the model. The type of analytics, KPIs and metrics you need, will change. Your perspective on profitability will need to change, to become more long term in its outlook.

With outcome based pricing models, you can arm your sales force with the tools to compete in the future.

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Three Common Pricing Mistakes (and How to Avoid Them)

Most businesses, when they want to increase profits, look at every avenue except pricing to achieve their growth goals. Although this is a frustrating reality for us as pricers, this also means that updating and improving pricing strategies can bring some quick wins for these companies. In this article, the author outlines the three most common pricing mistakes businesses are making, and provides simple and easy to implement solutions for how to correct them. Tony Hodgson is the Managing Director of Pricing Solutions UK. He can be reached at thodgson@pricingsolutions.com.

People tend to be clueless about prices. Contrary to economic theory, we don't really decide between A and B by consulting our invisible price tags and purchasing the one that yields the higher utility. We make do with guesstimates and a vague recollection of what things are 'supposed to cost.'
– William Poundstone

When businesses want to increase their profits, they will invariably try to get more customers, sell more products, reduce their marketing costs and cut overheads. They will do all of this before pricing ever enters the arena.

Why? Because pricing is something even very astute business leaders often overlook.

Though this is frustrating for pricers *– to see so much potential going to waste –* there is an upside. If you've not given your pricing strategy the attention it deserves, it's likely you are going to have some very quick wins.

Here are the three most common pricing mistakes most businesses are making, and how to correct them.

Update Your Pricing

You wouldn't believe how many businesses have the same prices that they did five (or even ten) years ago. This is a really easy trap to fall into. Your customers are happy with your current pricing and, if it isn't broken, don't fix it, right?

Rising costs and inflation alone should mean you raise your prices each year. However, there are many other reasons for you to systematically increase your prices. Perhaps the most influential is that an increase of as little as 1% can have a huge impact on your bottom line. Remember, your costs are already taken care of in your current structure. The price increase falls straight through to the bottom line.

Research shows that a price increase of just 1% on average increases an organization's net profits by 12%. So imagine the impact of a 3% price increase! You'll also be surprised at how little it bothers most customers and clients.

Tunnel Vision

"The mistake is to have only one price for your product."
– Nathan Barry

A large number of businesses operate a singular, narrow pricing policy for each of their products or services. Again, if this is you, you might be leaving money on the table.

Let's look at an example: In a recent study, pricing experts ran a test on selling beer. They priced one beer at $1.80 and one at $2.50. 80% opted for the more expensive beer. In this case, the lower priced product only served to emphasize and highlight the quality of the more expensive beer. Due to the minimal added outlay, it made it an easy sell.

To further emphasize the impact of tiered pricing (and the importance of getting it right), the researchers ran a second test. This time they introduced a bargain price beer at $1.60. In this test, 80% of customers opted for the $1.80 beer (the middle one). Obviously, this was disastrous for the profit margins.

Finally, the researchers removed the bargain beer and added a 'super premium' option at $3.40. In this test, 85% of customers opted for the $2.50 premium option. So, by simply offering more price options, this vendor was making an extra $0.70 (38%) per beer!

'Lowest is Best'

If your product or service is priced lower than all your competitors, you'll get more business, right? And because you're doing greater volume, you'll make more money? Unfortunately, this only works if you're selling exactly the same product as your competitors – and we mean *exactly* the same.

Don't price your products based on what other companies think theirs is worth – or the common denominator. Price it based on the value it offers your customers.

If you can revise your pricing strategy with these common mistakes in mind you will already be ahead of most of businesses. What's more, you'll also be on your way to unlocking the untapped profit potential in your business.

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Customer Centric Pricing

One of the key focuses for pricers around the world and in all industries in 2015 is the importance of understanding the customer. In this article, the author explains why customer centric pricing is key for success in today's market, and gives several examples of companies who have significantly increased market share due to modifying their pricing strategies to meet changing customer demands. Kyle Thompson-Westra is a Senior Pricing Analyst at Wiglaf Pricing. He can be reached at kthompsonwestra@wiglafpricing.com.

The Professional Pricing Society held its 26th Annual Fall Conference in San Francisco at the end of October. One of the biggest takeaways that was repeated in multiple forms across all of the events was the importance of understanding the customer. **Customers will reward you with sales and loyalty if you give them a reason to care. Understanding customer needs is the critical first step to effective pricing.**

The need to understand customer preferences may seem obvious from a product standpoint, but it is just as important for pricing strategy. How many companies fail to regularly reevaluate whether the assumptions they first made still hold true after a month, a year, a decade?

eBay first rose to prominence providing a unique buying experience for millions of customers. Its auction format was not only a great way for buyers and sellers to arrive at a mutually agreeable price, but also a delightful new buying experience. Auctions were fun.

Now, however, only 20% of transactions on eBay include auctions, according to *The Economist*. Due to pressure from other E-commerce sites and its own customers, eBay began offering a fixed price option a decade ago, which now amounts to over 60% of sales.

Intriguingly, otherwise similar items on the site tend to sell at a lower price via the auction format than the fixed price. Why should the manner of arriving at a price affect the final price of the product? It appears these days that the auction format, instead of delighting customers, incurs a "hassle cost": auctions cost customer time, require additional attention, and lack the certainty of a simple sale.

eBay was able to adjust to the changing E-commerce environment and stay relevant against strong competition from the likes of Amazon by paying attention to what its customers wanted. While its brand is still closely connected to auction sales, the majority of its business hasn't been for years. By being willing to adopt to this change, eBay remains a prominent online retailer.

We see similar transitions across the technology industry as once-dominant companies try to address the needs of a changing marketplace. Microsoft began to offer its flagship Office software suite as a subscription service back in 2013. This Office 365 represented a major shift away from buying a high priced one-off license to a lower priced periodic subscription. Customers had begun to find suitable alternatives to Office in the likes of cloud-based Google Docs, and it was incumbent upon Microsoft not only to expand its cloud integration but also reassess the method by which people paid for its product. This was critical to strengthen its presence with both consumers and the enterprise market.

Its strategy has been very successful for enterprise. As reported by the *International Business Times*, Microsoft's market share increased from 7.7% last year to 25.3% today. Google, in the same period, grew from 16.3% to 22.8%. Despite its strong lead, Google has fallen behind a company that many had dismissed from relevancy. Microsoft's pricing structure deserves much of the credit:

"Part of this growth can be explained by Microsoft's broader price structures, offering more tailored solutions compared to the competition. The Office 365 website offers seven different packages, with varying pricing structures that start at $5 per user/month for an annual commitment to the Business Essentials package, all the way up to $22 per user/month for the full Enterprise E4 package. Google, on the other hand, has two plans available. The base package will cost $5 per user/month, or $50 per user/year. The premium package will cost $10 per user/month or $120 per user/year, and adds unlimited storage with more than five users and 'advanced admin and audit controls.'"

Note that Microsoft has been able to enjoy this type of growth with substantially higher prices than Google's. Customers want value, not simply a low price.

It takes a clear strategic vision to undergo a shift such as those undertaken by eBay and Microsoft, but their innovative and adaptive pricing structures have led the way in ensuring their continued relevance in the marketplace.

But today clearly isn't the end of the story. Amazon and Google will continue to innovate and try to offer even better value propositions than eBay and Microsoft, respectively, to individuals and enterprise. Google is already reacting to the office suite news by incentivizing companies to make the switch from Microsoft, an unambiguous attempt to stop Office 365's growth.

Companies must constantly reevaluate their product offerings and pricing strategy in order to provide the best value for their target customer segments. Without a strong understanding of these customers, as well as the effort to continuously reevaluate this understanding, companies will see their share slip away to better positioned competition. Pricing requires just as much strategy as product; the right product at the wrong price is no longer the right product.