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RIEKHOF ON PRICING No 75

The 11
Most Common Strategic Pricing Mistakes

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For over 20 years, I have been focusing on questions relating to strategic and operational pricing from very different perspectives. As a Business Unit Manager at an international corporation I negotiated prices and developed pricing strategies, as a Marketing Director I influenced the pricing strategy principles of business activities, as a professor for general business administration I have conducted more than 10 empirical studies on pricing processes in companies, and during this time I and my team have advised international corporations, companies listed on the German stock exchange (DAX) and medium-sized enterprises on pricing www.unicconsult.com.

Here comes an admittedly subjective, condensed summary of the pricing mistakes that I believe are still prevalent in many companies.

I hope you have an interesting read and gain many new insights, and I look forward to your comments and feedback.

Regards, Prof. Dr. Hans-Christian Riekhof

Fig. 1: In the case of interchangeable commodities, aligning prices with those of the competition makes sense.

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1 Pricing is Geared Entirely to the Competition and not to What Customers are Willing to Pay.

In many companies, the competition plays a hugely important role when it comes to their own pricing. This is also confirmed by our own empirical studies on strategic pricing (most recently published: Riekhof/Breustedt 2023). But what can you really learn from the competition in terms of pricing? What drives companies to closely scrutinize competitors' prices? In our pricing projects, we encounter companies that employ 15 or 20 people solely to analyze competitors' prices. Does that really make sense? (Pricing Newsletter No. 58).

There is only one group of companies that should be intensively concerned with competitors' prices, and that is those that have nothing special to offer – companies, in other words, that offer interchangeable products and services. These include mineral oil companies, which adjust their prices several times a day – fuel, like other commodities, is indeed an interchangeable product.

All other companies would be better advised to concentrate more on their customers and how they perceive prices and on asking what price comparisons do customers actually make? How much energy do they invest in comparing prices? What switching costs are incurred when customers change providers? Electricity is certainly an interchangeable product, and electricity is also traded on the stock exchange. But how many private households switch electricity providers when there is a cheaper offer?

Recommendation No. 1:
Invest more resources in researching your customers' price perceptions and the value of your services from the customers' perspective.

2 Price Actionism is More Important than Long-Term Pricing Strategy.

In our empirical studies as well as in our pricing projects, we regularly ask whether companies have a documented and approved pricing strategy (link to the Riekhof/Breustedt 2023 study). This is the case in far fewer companies that we might expect. Instead, rebate campaigns, in some cases highly complex customer-specific price agreements, regionally very different and sometimes quite contradictory price structures are the norm, making it extremely difficult for companies to charge appropriate prices for their own services.

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Fig. 2: Price actionism can easily become a problem for strategic pricing

Recommendation No. 2:
Invest more time and energy into developing, adopting and implementing a well-thought-out pricing strategy, and refrain from price actionism.

3 Pricing is Largely the Responsibility of the Sales Department.

Especially in small and medium-sized enterprises, we often find a very simple division of labor between development and production on the one hand (which defines and manufactures the product range and is thus responsible for the costs) and sales on the other hand, which sets the prices and rebates.

This is a conceptually poor form of division of labor (see my Pricing Newsletters No. 2 and No. 28), as pricing is not an operational function at the end of the corporate value chain, but a horizontal, joint, cross-departmental process. All departments should jointly decide which value-creating customer products and services should be developed, i.e. what value is generated and what price it is worth.

Like this, you also avoid the classic dilemma of the sales department complaining about excessively high manufacturing costs and only being able to sell the products at correspondingly high rebates.

Recommendation No. 3:
Establish a pragmatic, cross-departmental strategic pricing process involving all business units, which are responsible for and implement the pricing strategy jointly.

4 Product Management has Failed to Develop a Clear Pricing Strategy for all Product Areas and Categories.

In many companies, the product range has reached a substantial level of complexity for good reason, in order to cater to all the different market constellations and customer requirements. A corresponding product management system has been put in place to oversee the further development of the product range and also ensure the profitability of the business units.

But have these product managers developed a long-term pricing strategy for their area of responsibility? In our experience, this is very rarely the case: cost increases in particular often necessitate price adjustments, and products with poor contribution margins are put to the test – all of which falls short of a pricing strategy (see my Pricing Newsletters No. 29 and No. 48).

Recommendation No. 4:
Ensure that all product managers develop a medium-term pricing roadmap for their area of responsibility, which they present to management for approval. Make the product managers the drivers of strategic pricing.

5 Pricing is not an Elementary Part of the Annual Budgeting and Planning Process.

We learned it in the first semester at university: sales = price x unit output. And that's also how I got to know it at my first employer: the budgeting process foresees detailed product group-related volume planning and price development planning. Consideration of the planned and the realized average prices according to product areas and sales channels, volume developments according to market segments and customer groups was a basic prerequisite of any planning.

It only became clear to me later that many companies make life far too easy for themselves here: they plan sales, but not volumes and prices. And this means that price developments cannot really be mapped well in the systems – a fundamental deficit for professional pricing (see also my Pricing Newsletter No. 45).

Recommendation No. 5:
Ensure that prices and volumes are recorded, planned and evaluated separately in each product area.

"The top management is responsible for the creation of professional pricing processes and the necessary enthusiasm to work on pricing roadmaps for all divisions and business units of their corporation."

Prof. Dr. Hans-Christian Riekhof

6 IT Sets the Pace in the Implementation of Pricing Processes.

Detailed pricing management requires the availability of corresponding customer- and product-related data about planned and actually realized prices. But this is where many companies reach the limits of their IT systems: the implementation of pricing strategies is at risk of failing due to a lack of pricing information.

But do you have to let the IT department set the pace? We see a clear alternative: first establish a pricing data warehouse that provides the appropriate planning and analysis tools independently of the IT infrastructure. Don't let IT set the pace in your pricing project.

Recommendation No. 6:
Choose a pragmatically structured pricing data warehouse
if your IT systems do not support the necessary planning processes in pricing.

Fig. 3: The IT-department derives important parameters from the pricing strategy and pricing processes.

7 The Pricing Competence of your Managers is not an Elementary Part of Management Development.

In our workshops, projects and seminars, we regularly ask who among the managers present has taken part in a pricing workshop or seminar. The answer is always the same: fewer than 10% have really got to grips with the basics of pricing. This is, incidentally, also confirmed by our empirical studies (link to Study 2023). How many seminar days do you invest each year in the pricing competence of your employees (see my Pricing Newsletter No. 51)?

(Strategic) pricing is ultimately about correctly determining the value of your own services. All managers, whether from marketing, product management, development, sales, service or financial controlling, should have a sound basic knowledge of this topic.

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Fig. 4: Our empirical studies show that pricing competence is rarely on the management development agenda.

Recommendation No. 7:
Ensure that your management team as well as junior managers have a sound grounding regarding the leverage effect of pricing, the pricing strategy options, the implementation of pricing strategies and also the structure of pricing processes.

8 The Creation of a Pricing Manager is Seen as the Solution to all Pricing Problems.

Sometimes it can seem like a reflex reaction: whenever we point out the earnings potential of strategic pricing in the context of pricing projects, someone is always quick to suggest creating the position of a pricing manager. And our empirical studies show (link) that the number of companies that have created their own pricing department or pricing manager has been increasing for years (see my Pricing Newsletters No. 26 and No. 64). But is this really always the right solution?

Recommendation No. 8:
First, examine all alternatives to creating a pricing manager.
If the pricing processes are not right and there is no clear pricing strategy, then there is a fairly high probability that the pricing manager will fail.

9 Financial Controlling does not Really Have Pricing on its Radar.

We regularly take a critical look at financial controlling reports on the topic of pricing. Does the company have systematic price controlling with corresponding reports and evaluations in place? Does it account for the deviations between price specifications or target prices and the prices actually realized in the regions and sales channels? Does it present differentiated statements on the implementation of planned price increases and the development of average prices per product segment? Are there detailed evaluations of rebates according to customer group and sales channel? Only a handful of companies have established a professional price controlling system (see my Pricing Newsletter No. 45).

**Recommendation No. 9:
Establish a systematic and detailed price controlling system.**

10 The Sales Department does not Have to Present Detailed Rebate Analyses.

If, in an international corporation with sales of €6 billion, an average of 25% of sales revenues is allocated to rebates, then we are talking about €1.5 billion – a considerable chunk of expenditure that requires detailed analyses – and justifications. There are industries where it makes sense and is also customary to grant rebates of this magnitude. And in some sectors, list prices are no more than a rough initial guide. However, given the earnings potential here, it is worth analyzing the rebates in great detail according to products, sales channels, customer groups, order sizes, supply chains, utilization rates or seasonal aspects. And above all, it is essential that the system records and evaluates the reasons for each rebate granted (see my Pricing Newsletters No. 19, No. 22 and No. 65).

**Recommendation No. 10:
Obtain systematic and detailed evaluations and justifications of rebates granted.**

11 The Implementation of the Pricing Strategy and the Attainment of Price Targets is not Incentivized.

An old management rule states: What gets measured gets done. This can easily be extended: What gets incentivized gets implemented. This applies in particular to pricing.

In practice, however, sales-related key performance indicators and incentive systems still dominate, supplemented at best by the contribution margin as a KPI. But the contribution margin does not really reflect the implementation of pricing strategies. Incentives related to pricing strategy targets must be much more concrete, such as adherence to target prices, the implementation of price increases, the attainment of volume targets following price reductions, and the implementation of rebate targets.

**Recommendation No. 11:
Create concrete incentives for implementing the pricing strategy targets as part of the annual target agreement process.**

Concluding Remarks:
I have saved my most important – universal – recommendation until last: Start with a maximum of three or four carefully and jointly (!) selected pricing strategy topics that are driven forward and implemented with all due vigor over a period of 12 months.

The successes will beyond a doubt motivate your entire team to continue developing your pricing strategy. And in the following year, you can add and implement two or three further pricing strategy initiatives. A company's pricing competence does not develop in 12 months. But initial successes become apparent in the first year.

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