Pricing for the for the Product Management Team

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Ok. Regardless of where you are in a product's lifecycle, pricing will be an issue for the Product Management team.

This posting is in anticipation of Mark Stiving's webinar , taking place February 8, 2012, which is based on his book " Impact Pricing, Your Blueprint for driving Profits ", which I'm currently reading. I'm very tempted to include things from the book, but we'll have to wait. I'll try to post a spoiler alert if I do. I'll be trying to keep this posting as close to life as possible, without Mark's book. I intend to come back and add some additional concepts and thoughts that are already a result of Mark's book in a follow-up after his webinar.

So what drives pricing? It all comes down to two things: differentiation and your relative cost-position. I know others disagree with me on this, but this is my blog. In all seriousness, my father (a farmer) taught me a principle that I just have to share with you. He said, "Val - now as you grow up, you're going to hear many ducks fart underwater. But, let this be your warning, regardless of how beautiful and shiny they are underwater, in time they all rise to the surface and their true self becomes apparent...nothing but foul air”. When it comes to pricing, you're going to hear that all too common sound.

As a product management team you need to stay focused on differentiation and your relative cost-position. These are the two factors that impact the every pricing decisions you make. Let all the rest be the focus of others. With these two factors, we offer three value propositions. Yep, that's all. The value propositions are: economy of scale, uniqueness of offering, and/or intimate relationships. So let me explain.

Differentiation: Yes, this means the difference between you and your competitors, but only in a special way. In other words, don't get distracted in the other types. I'm reminded of the birds on the Galapagos Islands who've become so differentiated that they jeopardize their very own lives. Also think of the differentiation seen in the '60s (yes, I was there). In these two examples, we see differentiation, just not the right type. In both cases, differentiation is self-serving, however in today's world, this isn't enough.

When talking about differentiation, we mean how your offering impacts your client's value chain differently. Of course we mean differently as in better than our competition. In the examples I gave, the male birds looked great, but couldn't forage for their mate’s food, nor protect young chicks. Our type of differentiation would require the male birds to differentiate in a direction so that they would be better service to their mates and offspring. In the '60s, we thought about how we looked, and used color to make ourselves stand out, not how we made those around us look. We were the typical "me" thinker, not today's "we" thinker. Remember, when it comes to pricing, we mean differentiation in such a way as to contribute to our client's value chain. The more perceived value we offer our clients, the more we differentiate ourselves, and the higher the price we can charge, all other things being equal.

If our strategy is to deliver the "intimate relationship" value proposition, then we're claiming we know their customer's problems better than they do. In other words, without us, they'd need to gain our experience the expensive way in order to deliver the same value to their customers. We differentiate our offering by impacting their value chain more rapidly and effectively than they could do it themselves. Thus we can keep prices somewhat high. I'll talk more about what I mean by that a little further down the post.

If our strategy is to deliver the "uniqueness offering", then we're claiming we have something that will help our clients deliver a unique value to their customers. Because people can't get this value anywhere else, we can ask for a higher price. However, there is a limit. The price we ask for can't cost more than the value we deliver to their customers. It's worse than that, most or your customers are going to want at least a 20% margin, thus the unique value that you offer must be priced at least 20% lower than the value you deliver.

Finally, if you're going to play the "economy of scale" strategy, then you're claiming you've delivered this value so many times and found so many shortcuts that you can deliver it lower than anyone else. If this is your strategy, then you must have a relatively low price.

This brings me to our second factor, the relative cost-position. I've heard folks say, "Don't think of cost when deciding price" or "Price has nothing to do with cost". Well, remember what my Daddy told me, it's that old familiar sound again. Ok, to be fair, we'll give them a chance, but be skeptical. For now, it's not cost, as much as cost-position.

Relative Cost-Position: Your relative cost-position is the level of your costs compared to the costs of your competitors’. Here's why this is so important; the sustainability of your price is dependent on the perceived value of your differentiation. With me so far? It's also dependent on your ability to drop prices when required, and fall back on the "economy of scale" value proposition.

If your cost-position is higher than your competitor's, and you're stuck in a competitive position requiring low-prices, eventually you won't be able to subsidize your product's price and you'll either have to raise prices, or kill the product. I know this seems drastic, but reality is even worse. In this situation, with prices outside the margin, while you're trying to survive, the competition with a better cost-position is still taking in profits and reinvesting. Your differentiation is dropping because they keep getting better, which causes increased pressure to lower prices even further.

In the short-term, cost may not be your primary factor in setting price, but in the long-term, your cost-position is to live and die for. As a product management team, we must continually improve our differentiation, and relative cost-position to give us the margins required to play out as many value proposition strategies as we may need. Otherwise, I believe we're living is a crystal bubble waiting to be broken.

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