DUCKER CARLISLE

Inflation is decreasing. Should your prices fall, too?

Many original equipment manufacturers rely on simplistic models to make all-important pricing decisions, when they should be using more data inputs to deliver 5% to 10% incremental revenue improvements.

Does it sometimes feel like you're walking a pricing tightrope? You're not alone.

Most original equipment manufacturers are struggling to factor a wide mix of variables into their pricing strategies. From the costs of raw materials and supply chain issues to consumer sentiment and labor challenges, OEMs are grappling with a multitude of challenges.

As the economy creeps out of pandemic disruptions, pricing strategies won't get any easier. Decreasing inflation will lead customers to expect lower prices.

As that happens, what will you do? Retain the status quo of traditional approaches?

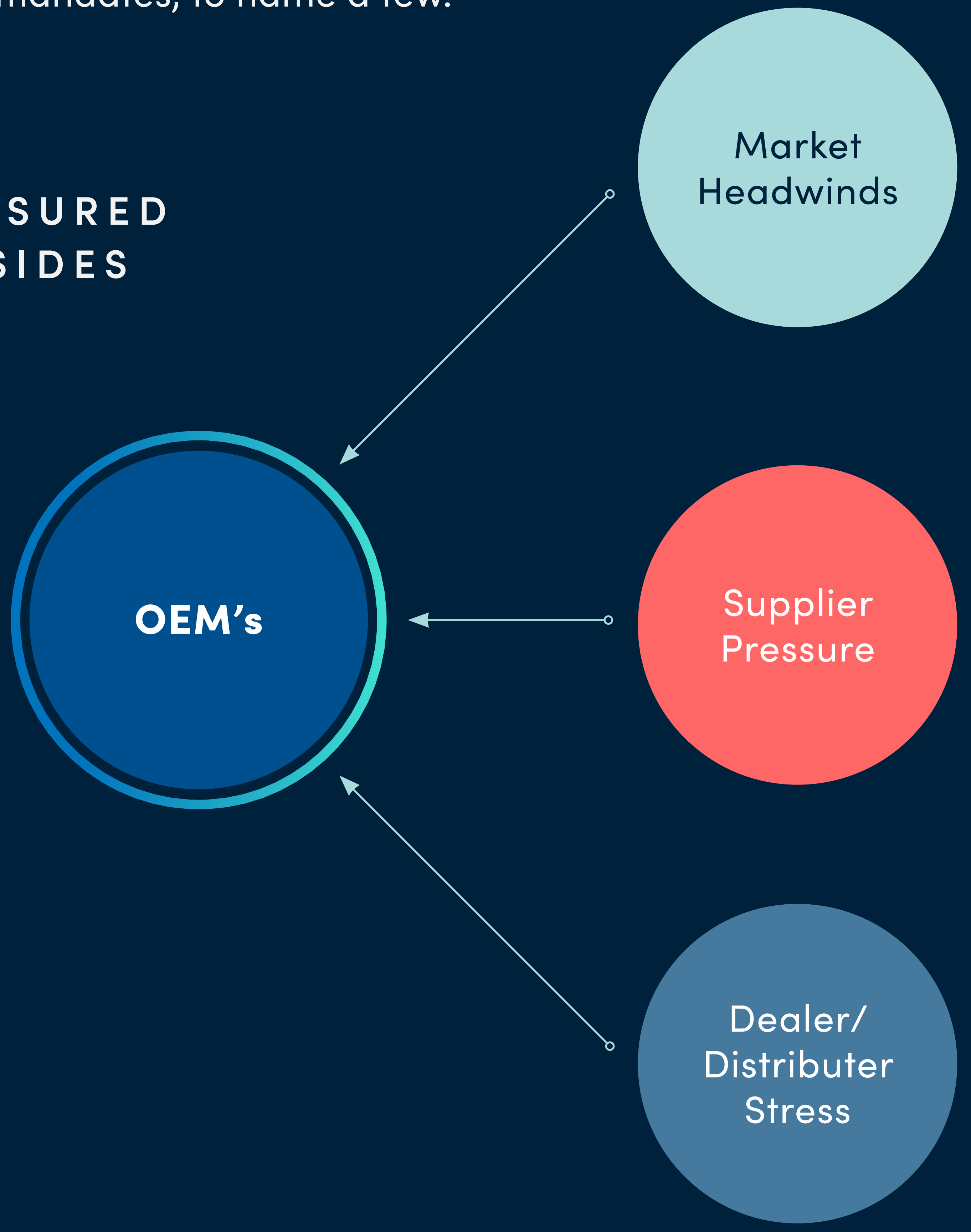
Broad, scattershot pricing and basic supply and demand strategies are risky. These processes typically rely mainly on cost and margin targets and lack the ability to optimally set pricing – regardless of what's occurring in the market. In addition, they risk exacerbating already over-priced products, while leaving money on the table by underpricing other products. In turn, the status quo risks losing customers who, seeking competitive pricing, may perceive highly priced items as price-gouging.

There's a better, more agile and flexible way that accounts for what's happening in the market, while also creating true value and profit.

Caught in the middle

OEMs are getting squeezed from all sides — customers, suppliers, consumer inflationary measures, workforce shortages, fluctuating commodity prices, and compliance mandates, to name a few.

OEMS PRESSURED FROM ALL SIDES



The fallout from Covid-19, for example, is still sending pricing tremors throughout the automotive industry. Although the demand for new vehicles has steadied, car buyers are still sensitive to potential over-pricing and are increasingly turning to online services for competitive shopping. Also, many consumers have turned out to be dismissive of electric vehicles (EV) due to their price tags – a pain point for manufacturers that have invested heavily in EV components and production lines.

On the supply side, OEMs in this sector continue to be challenged by the availability and pricing of raw materials, which is causing longer lead times for new vehicles. Also, suppliers – faced with their own cost challenges related to a rise in some commodity prices – want to either pass along these higher costs to OEMs or require increased order quantities or guarantees.

Meanwhile, carmakers are contending with other issues, including:

- Labor shortfalls and union activities
- Dealers pressing for automotive incentives
- Increased pressure from innovative competitors
- Geopolitical issues and international conflicts
- Aftermarket pricing of tens or even hundreds of thousands of spare parts

This dynamic of being "caught in the middle" is not unique to the auto industry. Manufacturers in the industrials and heavy equipment (IHE) sector, as well as building and construction, are being pressured on one side by customers who want price reductions or stabilization, and on the other by commodity prices, and high interest rates.

Also, there's the factor of dealer commissions, which further inflate prices for industrial and heavy equipment, and yet manufacturers can do little about them. Buyers of these products and machines are already feeling price inflations due to the rising costs of materials, so IHE makers are truly squeezed on all sides around pricing.

Organizations in these sectors cannot sustain traditional pricing strategies and also expect to substantially increase revenue and profits. The variables are too many and too unstable.

> Hitachi had to raise its prices by 8% in 2023 due to higher costs for energy, raw materials, and logistics.

A more predictable, reliable approach accounts for shifting pricing factors and offers the flexibility to adapt and pivot where necessary.

How to structure pricing decisions

If prices are left unchecked, increased costs in a cost-push environment could squeeze OEM margins. On the other hand, if prices are raised too fast consumers may push back, and demand and loyalty could dissipate.

OEMs today can rapidly make informed pricing decisions — and maintain profit margins —

by integrating all the data they have into a market- and value-based strategy. In addition to commodity costs, as well as producers and consumers price indexes, OEMs need to include data related to product features and value-added capabilities, such as availability, customer service, product support and training, warranties, return policies, service levels, and trained sales staffing. They also should take into account brand image, how customers make purchasing decisions based on value, and the need to price for competitive alternatives.

From a broad standpoint, this sophisticated model offers greater visibility into all factors that influence pricing, and it attributes value to them. But at a deeper, more impactful level, the benefits of a market- and value-based pricing strategy can create substantial profit opportunities, such as:

- Real-time value gained through market analytics aligned with what customers are willing to pay
- The ability to rapidly respond to competition based on an overlay of market-based product pricing
- The maximum value of each product/part/component to drive greater profitability
- Bundled sales opportunities with fair pricing and the elimination of lengthy negotiations
- Satisfied and increasingly loyal customers, who can obtain transparent and competitive pricing
- Incentived innovation by being able to detect shifts in the market and demand

Often for OEMs with selling channel partners – such as distributors and dealers – the increased revenue from pricing initiatives can be shared with channel partners to further multiply positive impacts from the initiative.

Results will vary by OEM industry and as the organization matures with this pricing process. Among its clients, the Ducker Carlisle Group typically sees between 5% and 10% increases in incremental revenue.

Here's a recent example: An aftermarket automotive client wanted to see the difference between their traditional pricing approaches and a market- and value-based strategy.

Using their more basic pricing methods gained them a 3% improvement on their sales performance. On the other hand, the data-enriched model returned a **7% improvement**. That incremental 4% is a significant revenue enhancer.

The bottom line

It can take a great deal of time and effort to spin through all the cost factors and market implications that affect pricing strategy. These multiple factors can either cause OEMs to retain the status quo or get caught in pricing paralysis.

There's a better way to make these decisions. Lean on an expert partner that can help accelerate additional revenue with a market- and value-based pricing strategy.

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