Putting Value and Customers at the Centre of Your Business

By Jon Manning

In the first article in this series, I explored the challenges associated with managing costs. In this second article, I will explore pricing management as a stagflation tool: why it is more important to manage value than costs, as well as understanding customer psychology.

This should help readers acquire that elusive skill of being able to pass on price increases without losing customers.

I have already devoted a fair amount of column space (1,143 words to be precise) to talking about costs, while also pointing out that customers rarely care about them. What they ultimately care about is value.

A few years back, as part of a consulting project I was engaged for, I asked florists what was most important to them when it came to dealing with a flower wholesaler, asking them to allocate 100 percentage points across four attributes. **Range and Product** attracted 45.8%, **Service and Support** and **Convenience** both attracted 18.3% each, with the balance of 17.5% being associated with **price**.

I then asked the florists to rank their wholesalers across those attributes on a scale of 1 – 10. The graphs below show the raw scores, as well as scores weighted by the percentages above, for one wholesaler on the left, and for another wholesaler on the right

The wholesaler on the left is focused on providing value by focusing on Range and Product, Service and Support and Convenience. This has enabled this business to successfully de-sensitise customers to price. The wholesaler on the right, on the other hand, has been less successful in capitalising on non-price value attributes. It is not difficult to work out which wholesaler understands the value s/he provides and can thus command higher prices.

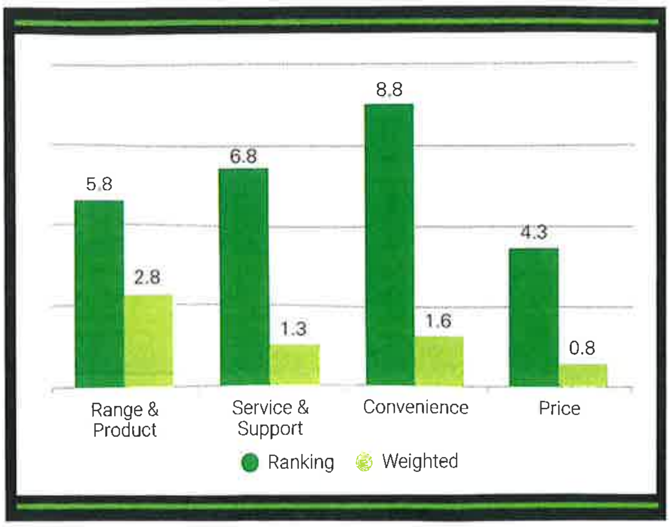
Beside understanding the value you provide, how else can pricing management help you through this stagflation environment?

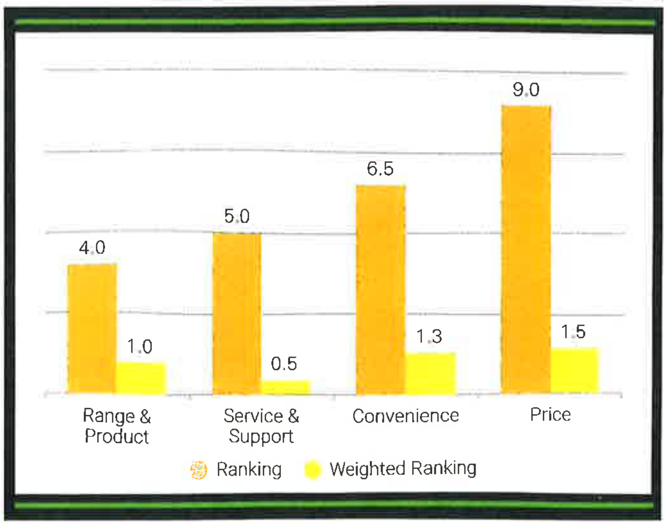
First, take a segmented approach to products, customers and pricing. Start by identifying KVIs ("Known Value Items") – the products and services you provide to different segments of customers that they know details of (including price) off the top of their heads. These will also be non-discretionary products that will remain essential to customers. Leverage the differences, in costs, in demand, in different geographies and adjust prices, upwards and downwards accordingly (not across-the-board) .

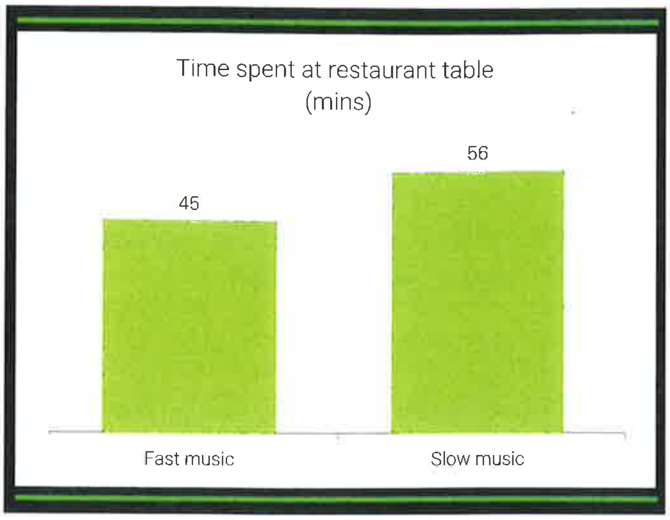
Second, adopt the same segmented approach with any promotions. Remember that excess inventory you found while looking at your working capital in the first article in this series? Put that excess on promotion, rather than the inventory for which demand is still healthy.

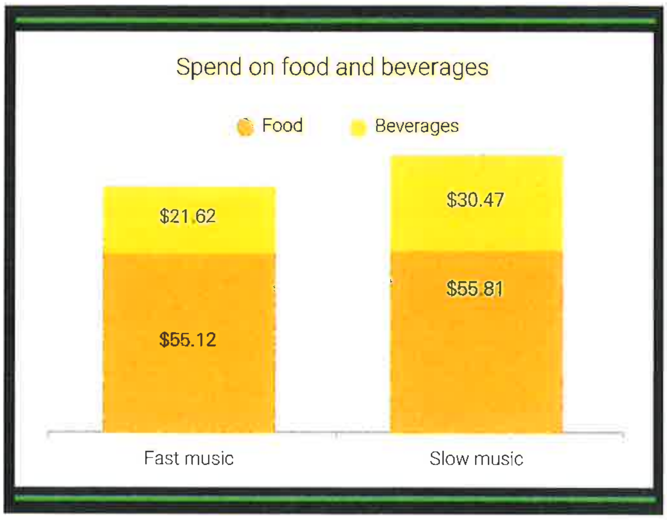
Third, when running promotions, always time-box them with start and end dates and conduct a post-implementation review at their conclusion. Answering the following questions, and applying the learnings, will make your next promotion even more successful:

- What was supposed to happen?
- What actually did happen?
- Why was there a difference?
- What can we learn from this?









Fourth, take stock of both your brand power and brand positioning. How did Unilever raise prices 8.3% in Q1 of 2022 and their volumes declined by only 1%? How did McDonald's, in the same quarter, raise menu prices by 8% and grow overall sales by 3.5% and same-store sales by 11.8%?[1] Heinz's 12.4% price rise in Q2 yielded a 2.3% drop in sales units but a 10% increase in sales value.[2]

Australian SMEs don't have the brand strength of Unilever, McDonald's or Heinz, which would have undoubtedly been a factor in the above-mentioned results. But for a SME running multiple brands, manage them properly. If you've got one brand selling non-discretionary products, geared towards more price sensitive customers, that's where your demand is likely to be strongest rather than a premium priced brand selling a non-discretionary product that is more likely to be susceptible to inflation and customers will cut back on.

Fifth, consider changing your pricing model. Consumers and customers are more likely to try something new in difficult economic times than when things are going along swimmingly (which explains why companies like IBM, Microsoft, Apple, Uber, AirBnB (to name a few) were started during recessions or difficult economic times).

For example, can you introduce dynamic pricing if demand varies by, say, the hour of the day, the day of the week or month of the year? Airlines do it, hotels do it. While I was writing this article, Mercedes Benz was advertising a vehicle on Melbourne radio station 3AW as "dynamically priced".

Sixth, can you de-risk big purchases for your customers? In 2009, Hyundai in the US offered to buy their cars back if customers lost their jobs. The US car market fell by 20% in 2009, but Hyundai's sales increased by 8%, and they only purchased 50 cars back from customers in the first 9 months of this campaign.

[1] Chaudhuri, Saabira (2022, April 29). Unilever Increases Prices over 8%, Hurting Demand. Wall Street Journal, B6. And Haddon, Heather (2022, April 29). McDonald's Price Increases Help Boost Sales in the U.S. Wall Street Journal, B3

[2] Butler, Sarah (28th Jukly 2022) Double Digit price increase pays off for Heinz and reckitt, The Guardian, p33

Finally, give some thought to the following:

- accepting a customer on a lower-priced product is a better outcome than losing them altogether.
- Revisit your terms and conditions. T&Cs are how you get the prices you set. Revisit clauses such as payment terms, upgrades, downgrades and cancellations, for example.
- Are there extras or value-adds that you can provide without increasing your own cost base (like electronic data interchange, advice or research, for example)?

- If you have a pricing forum/council/committee, this should now meet a bit more frequently, changing prices accordingly. If you don't have one, you should.
- Introduce temporary surcharges, for example to reflect the higher price of fuel, while leaving the price of your own products and services at their current levels. This associates the price change with factors unrelated (or less related) to you and outside of your control, preserving margins on your own product. They are easier to withdraw later, without diluting your own pricing when the time is right
- Unbundle products and services. Offering them individually priced will create cheaper perceived price points.

The other pricing opportunities for SMEs is to apply some of the learnings from Behavioural Economics, a body of thought that combines economics and psychology. It looks at how humans actually behave in markets and how they make choices and decisions, rather than how orthodox, neo-classical economics has thought humans should behave. It is the difference between what a rational, selfish and independent (wo)man says they will do and what they irrationally actually do.

A series of heuristics has evolved from this body of knowledge that can be applied not only to the pricing of products and services, but also the acquisition of customers, sales generation or market segmentation (to name a few). Here are some of those "hacks" that have the potential to further assist NGIV members through the current difficult trading conditions.

The Weber-Ferschner Law: Tell customers they are getting a discount. If you're at your local nursery and you see two Phoenix Canary Isle Date Palms, one for $349 and the other for $399 with $50 off, which one do you buy? Despite both offers being identical, more customers will buy the latter. Why? Because they can see they are getting a bargain.

Consumers today love "the thrill of the hunt" (finding a deal) and "the thrill of the kill" (greeting the deal and the accompanying bragging rights that accompany a discounted purchase).

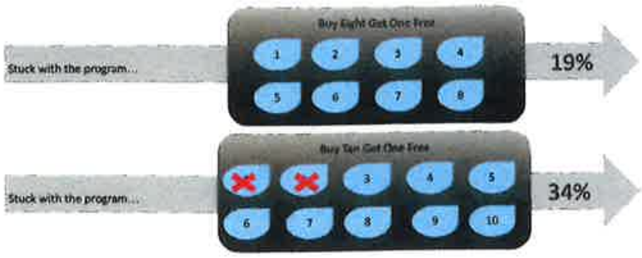
Decoys: Consider introducing a "decoy" offering, with a high "shock price" that makes alternatives look more attractive. Norma's restaurant at Le Meridian Hotel in New York has a $1,000 omelette on its menu to make the $100 omelette look good. Many fine dining restaurants have an $800 bottle of wine on their menu which few, if any, diners purchase. But it helps sell the $80 bottle of wine.

Offer a Five Star Experience: Invest in the context in which your prices appear, whether it's in your store, on your website or in your quote or business proposal.

In the 1980s, Nobel Prize winning economist Richard Thaler conducted the famous "Beer on the Beach" experiment. Your best friend, with whom you are enjoying a day at the beach, offers to get you an ice-cold bottle of your favourite beer from the run-down grocery store at the end of the beach and asks what you're willing to pay. Changing his mind, he then asks what you'd be prepared to pay for the same beer purchased from the five-star hotel at the other end of the beach. Like the Canary Isle Date Palm above, the offers are identical, but Thaler's research found the willingness to pay is higher at the five-star hotel than the run-down grocery store.

Having improved the context in which your prices are seen, how about improving the ambience? An 8-week restaurant study found that customers spent 11 minutes more at a table when slow beat music was played (compared to fast beat music), resulting in their beverage spend increasing by 41% and total gross margins increasing by 15%.

But staff in a data input centre processed 12.5% more vouchers when listening to fast music (compared to no music) and 22.3% more vouchers when compared to slow music.



The first two washes on the loyalty card are crossed off pro bono.

Choice architecture: Always offer customers three options, with the equivalent of (but better names than) "Good/Better/Best", or "Small/Medium/Large". If you offer customers one choice, you've got a 50:50 chance of closing the deal, and that's it. If you offer two choices, you will force the customer to make a price-based decision (and in the majority of purchase decisions, that will be the cheapest of the two). But when you offer the customer three choices, two things happen: firstly, you force the customer to make a value-based decision and secondly, they ask themselves "which one do I buy?" not "should I buy?".

Help the customer reach their goal: In an experiment conducted at a Los Angeles car wash, 19% of drivers visited 8 times, enough to earn a free car wash. But when the first two washes on the loyalty card are crossed off pro bono (once again, making both offers identical), 34% of customers visited the car wash eight times, earning the free clean.

Finally, some other ideas to tick of the list:

- Mention the daily equivalent price, rather than a weekly, monthly or annual price.
- Remove the dollar symbol from price list (it reinforces that customers are parting with their money).
- Count the syllables in your price points. Prices with more syllables are perceived as more expensive than those with less.
- Focus on the price difference: if the price is $200 and the customer wants to pay $150, focus the discussion on the $50.
- Provide social proof: this is our most popular product.

As Churchill once said: 'Never let a good crisis go to waste.' For many SMEs, getting their pricing in better shape during this difficult trading period would be a Churchillian achievement.

About the author

Jon Manning is the Head of Pricing at a SaaS tech company based in Melbourne, the founder of **www.PricingProphets.com**, a start-up mentor (at MAP, AIM, Blackbird Giants & River City Labs), a micro and behavioural economist, and the author of "Overcoming Floccinaucinihilipilification: Valuing and Monetizing Products and Services". This book is a guide to value-based pricing for start-ups, entrepreneurs, and side-hustlers.

Jon has around 30 years' experience in pricing strategies, pricing models, business models, monetization and the use of behavioural economics and pricing psychology.

National Nursery Survey

Nursery growers across the country are being urged to participate in a nationwide census, which aims to accurately assess the value and volume of wholesale greenlife production in Australia.

In addition to growers, the industry will also be surveying retail nurseries and landscapers to validate production data and gain further insights into how the supply chain operates.

Funded by Hort Innovation using industry levies and funds from the Australian Government, this project is being led by Greenlife Industry Australia (GIA) in conjunction with ACIL Allen Consulting and Down To Earth Research. Survey data will be gathered through a series of quantitative interviews with greenlife businesses, with the aim to produce a reliable and robust snapshot of the size, value, production, employment and sentiment of Australia's thriving nursery industry.

Crucially, the data collected in the surveys will be provided back to industry participants in the form of the nursery industry business benchmarking tool. The tool is an easy to use and functional program which uses industry data to provide businesses with information to inform short-term decision making and long-term strategy based on trends amongst peers.

Joanna Cave, Chief Executive of GIA, encourages all growers to participate in the survey in order to build the most accurate and reliable picture of the industry.

'This is the fifth year that we are carrying out this survey and with each year, the data becomes more clear and we become more capable of drawing trend-based conclusions,' she said.

'We would love to see an increase in respondents this year to better reflect the diversity of our growing industry.

'With each completed survey, we are able to add another piece of the puzzle when it comes to determining the true value of our industry. The more input we get, the better we can understand trends and make strategic investment decisions accordingly.

'Additionally, the more accurate the data is, the more valuable the benchmarking tool will be, meaning our growers will get greater value from the tool and be able to make more informed decisions about the future of their business.'

Last year, the industry generated $2.8 billion in sales, increasing over 8% on the previous year. Growers also reported making decisions on investment in education and technology, based on insights that other growers were prioritising investments in their businesses.