

“A must-read and accessible guide for
any business concerned with delivering
profitable growth.”

Nathan King, CEO, AddVantage Strategy

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THE **7-STEP** PLAN FOR
WINNING MORE CUSTOMERS
AT BETTER PRICES

Mark Peacock

'Listening to a true domain expert is always a pleasure. In this book, Mark educates you on the power and importance of pricing. Strategies, tactics, methods, approaches, tips – everything. Pricing is the point where all of your efforts touch the customer, but it is usually less developed inside an organisation than marketing, sales or management. This means that Mark's impressive and timely book is almost certainly worth more to you than any from those other disciplines. A great and eye-opening read.'

– **Jim Irving, FCIM, FFISP, author of *The B2B Sales Top Tips Guidebook***

'Full of great case studies, frameworks, examples, quotes, and chapter ending summaries. This book, more than any I have read before on the subject, is both thought provoking as well as providing the reader with a practical toolbox of ideas and suggestions that overcome the fear factor we often face when discussing pricing with customers. With its easy reading style and compact chapters, you'll find a treasure trove of ideas that will undoubtedly increase the profitability of your business.'

– **Jim Kirkwood, CEO, TTC Group (UK) Ltd**

'Mark dissects the complex and often misunderstood world of pricing, and presents it in a clear and easily digestible way, providing valuable guidance, tools and techniques to get your pricing right. This book is a must for start-ups and established businesses alike. In fact, I'd go so far as to say it is a must for every manager and leader. As Mark says, pricing is often one of the last things we consider in a business, yet it has the biggest impact on our profits!'

– **Ian Windle, author of *The Leadership Map*, leadership speaker and coach**

'This is a book full of practical insights into why pricing strategy and execution is a driver of commercial success. It's a book about having the confidence, courage and foresight to use pricing as a competitive tool.'

– **William Wright, CEO/founder, Adaptomy Ltd**

'I wish this book had been around when I started my business! From the practical tips to the hard facts and real-life examples, this book should be handed out to all business owners. Being a non-financial person I find all this quite intimidating, but Mark makes this subject easy to understand and has put pricing in terms we can all understand and use to grow and enhance our businesses. This is a must-read!'

– **Susan Walsh, founder & MD, The Classification Guru**

'Learn how to convert more customers at higher prices – clear, actionable ideas, delivered in a concise and easy-to-consume way. It's a brilliant guide to a more profitable business through better pricing. Highly recommended!'

– **Chris Peak, managing director, Feelingpeaky Ltd**

'Mark is a pricing pro. In this generous book he lays out a wealth of pricing knowledge and experience with crystal clarity. It is packed with practical, actionable pricing information whether he is guiding you on pricing strategy, communicating value or tactical actions. Read it with a pen or highlighter.'

– **Richard Maybury, Attitude Solutions**

'*Pricing for Success* is an easy-to-read guide on pricing that will help you improve your business. The author successfully shows you why chasing easy wins over taking a more tactical approach can be damaging to your financial stability. It is filled with short case studies and action points that will allow you to transform your business and increase profits without the fear of losing clients. Whether you are an entrepreneur or an established business selling products or services, this book is definitely worth the cover price and more importantly the time you will spend reading it. It's a game-changer!'

– **Simon Childs, CEO, Optitude Business Solutions Ltd**

'As commercial landscapes become increasingly ambiguous, uncertain and disruptive, all businesses must innovate and adapt or risk failure. A coherent pricing strategy is essential for any organisation positioning new products and services. With continuous innovation now key to longer term survival, *Pricing for Success* is an essential resource for entrepreneurs.'

– **Cathryn Barnard, director, Working the Future**

'Well written and easy to follow, it is both educational and inspirational. By following the steps clearly set out in the book, SMEs will have the tools required to understand pricing and its key role in developing a financially sustainable, profitable future.'

– **Martin West, director, Ashton Allsop LLP**

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Mark Peacock

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Introduction

Why does no one talk about pricing?

When I left corporate life in 2017, I was struck by the lack of people who help businesses improve their pricing, especially in the SME (small and medium-sized enterprises) sector. I knew from my own experience after 25 years of working for large brands how important pricing was to the success of any business. Yet other than the major consulting firms, there seemed to be no one talking about pricing in a way that helped entrepreneurs and SMEs.

There are armies of advisors out there, all trying their best to help businesses grow:

-  marketing and PR agencies
-  financial advisors and accounting firms
-  IT consultancies
-  business and leadership coaches
-  sales experts and trainers
-  non-executive directors
-  and a million 'gurus' all promising people endless riches.

They might touch on the subject of pricing with a client but they never really focus on the underlying *pricing strategy* of the business. Probably because, like many people, they suffer from a lack of awareness of what can be done with pricing and tend to stick to what they know.

Why it matters

When you stop for a minute and think about it, it's obvious why price is so important. Every business has a price they want to sell at and every customer has a price they are willing to pay. Price is

the focal point of the transaction between a seller and a buyer, so it deserves serious attention. Yet all too often I think businesses (both large and small) will just set their prices at the lowest level they think they can sell at and hope to make enough profit from.

I believe good pricing can also be the difference between success and failure. It does upset me when I see owners of small businesses struggling to cover their costs and barely scraping a living because of poor pricing. Or they are running an apparently successful business with lots of customers, a great team and decent revenues, but profitability levels are low or non-existent because they have allowed prices to be suppressed in the belief that they can sell their way out of a bad situation.

Yet a small increase in price can make a massive difference to your bottom line. There's a well-known rule of thumb that says for every 1 per cent increase in prices, businesses can typically increase net profits by around 10 per cent. What other lever do you have in your business that can make such a difference to your bottom line? There isn't one, yet price tends to be the last thing people will look at when trying to grow their business.

What's holding you back?

So what's stopping you from trying to work out a better pricing model? Is it complacency, inertia, difficulty, not enough time, or is pricing not a high enough priority? In my experience of working with and talking to hundreds of different businesses on this topic, I always think that the underlying reason is fear:

-  fear of upsetting your customers
-  fear of not winning more sales
-  fear of not growing your revenues
-  fear of competitor reactions
-  fear of rejection
-  fear of change.

I think there is a perception that pricing is thought of as being analytical and scientific: ‘If you change the price of product X, what impact will it have on sales volume Y?’ While analytical thinking is an important part of pricing, don’t forget that people run businesses and people are largely driven by emotions when deciding what to do. I have seen business owners literally panic with fear when I suggest to them that reviewing their pricing can help them improve their business. Their reply is, ‘I can’t do that – I’m too scared to have that conversation with my customers!’

What if?

-  But what if there was a way you could increase your prices without upsetting your customers?
-  What if there was a way you could acquire more products, services or clients and do so at higher prices?
-  What if you could redesign your pricing model in a way that your customers actually like?
-  What if you could use your pricing to significantly differentiate what you do from your main competitors?
-  What if you could charge prices that put a proper value on your work?
-  What if you could be more confident with your pricing?
-  What if you could find a way to know what your customers are truly willing to pay?

I sometimes get asked for a ‘magic formula’ to help people calculate the best price. In other words, if I take my costs and add X per cent, and then adjust it by Y per cent for customer acceptance or competitor positioning, then my ideal price is Z. Unfortunately, there is no such magic formula – and don’t let anyone tell you otherwise. Just as your branding and marketing need to be unique to you, so does your pricing. This comes from understanding the range of pricing options open to you, working out which approach is going to suit your business best and experimenting. Thought,

effort, application, creativity and being willing to try different things are the magic ingredients to better pricing.

What next?

I've written this book to give business leaders and owners a framework for how to think about pricing and how to use it to work out a better pricing strategy. My goal is to inspire you and show you examples of pricing techniques that will change your understanding and your approach to pricing.

In Part 1, I will look at the importance of pricing and share numerous examples of how your 'pricing power' can make a big difference to the value of your business. I will explore some famous pricing mistakes and also show you some examples from the weird and wonderful world of psychological pricing so you can see how fascinating and inspiring this aspect of pricing can be.

In Part 2, I will take you through my seven-step framework for how to create a better pricing strategy:

1. **Company** – being clear on your price positioning and objectives.
2. **Customers** – understanding how your customers value what you sell and how much they are willing to pay.
3. **Competitors** – assessing competitive alternatives and justifying your price differences.
4. **Products** – defining your products to enhance and improve your pricing.
5. **Pricing** – designing a pricing strategy that helps you achieve your goals.
6. **Proposition** – presenting your prices to your market in the best possible way.
7. **Profits** – ensuring you achieve the value you want from your new pricing model.

By the end of the book, you should have all the tools you need to help you design and deliver a vastly improved pricing model. There are plenty of templates and examples you can use to help you work out a new approach, but if you need more help, then go to my website at pricemaker.co.uk for further information.

I'm hoping you will find this book useful whatever role you have, but I think it will be particularly helpful for anyone in the following roles:

-  business owners or leaders (MD/CEO)
-  board directors/functional directors
-  chief revenue officers
-  sales leaders and salespeople
-  product managers
-  marketing leaders and teams
-  finance leaders and advisors
-  business advisors and consultants.

As it impacts so many parts of the business, pricing is always a cross-functional activity, so it's always important to involve your whole team in any pricing decisions. Most SMEs don't have a dedicated pricing person (or function), so you may need to decide early on who owns pricing in your business. Hopefully this book will give you clarity on what needs to be done and how you should start going about it.

I wish you the best of fortune with your pricing activities.

Part 1

The power of pricing

Chapter 1

What is your pricing power?

Warren Buffett is one of the world's most famous and successful investors. He's worth more than \$100 billion and has shown great skill in picking the right companies in which to invest. You may be surprised to learn that there's one aspect of a business that he values more than anything else:

The single most important decision in evaluating a business is its pricing power. If you've got the power to raise prices without losing business to a competitor, you've got a very good business. And if you have to have a prayer session before raising the price by a tenth of a cent, then you've got a terrible business. (Buffett 2010)

It's a simple statement with huge implications. But other than the investor market, very few businesses truly understand what it means.

If you have strong pricing power, it almost certainly means you also have:

-  a strong brand and a great reputation
-  high-quality products and services that meet a real customer need
-  distinctive positioning in your market
-  high-performing people
-  fantastic customer service
-  strong financials.

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In other words, strong pricing power comes from having a business that excels on many fronts and is the key barometer for business success. Warren Buffett makes only a small number of investment decisions in a year and when he does, he makes big bets on those businesses. Apple, Amazon, Coca-Cola, Johnson & Johnson, Kraft Heinz and many other leading brands all have significant stakes owned by his company. You might imagine that strong pricing power is only available to the global giants that he invests in. But *any business*, no matter how big or small, can improve and strengthen their pricing power.

Whether you are a start-up, a sole trader, an SME or a large corporation, pricing power is achievable for any business. And greater pricing power will lead you towards the following:

-  customers who value what you do
-  customers who are willing to pay more for your products or services
-  increased revenue and profit growth
-  distinctive positioning in your market
-  stronger resilience against competitor pricing tactics
-  a financially sound business
-  long-term success.

Have you ever thought about the pricing power of your business? How would you describe it? Do you think it encompasses any of the items mentioned above?

Pricing is the profit multiplier

Marn et al. (2003) at McKinsey quote a famous rule of thumb that says, 'For every 1 per cent increase in prices, your net profits will increase by 8–10 per cent.' This is the key piece of insight that Warren Buffett uses when evaluating businesses for long-term profit growth. In other words, it only takes a small improvement

in your price to generate a significant increase in net profits. Now clearly, prices should only be increased as part of a well-thought-through strategy, and you need to have many of the fundamentals in place as mentioned above, such as a strong brand, great products or services, fantastic customer service and a high-performing team. But if you can improve your prices on a sustainable, ongoing basis, you will create a better business that generates more value in the long run.

A simple example

Imagine a manufacturing business with £10 million in revenue and after direct costs and overheads it generates a net profit of £1 million. If we increase the prices of all the products by 1 per cent (and let's assume for a second that this is achievable and there's no customer resistance), then revenues will increase by £100,000 to £10.1 million. As the increase in price is all additional revenue with no additional cost, then the additional £100,000 all falls through to the bottom line and increases net profits by £100,000. So for a 1 per cent increase in prices, we have now increased net profits from £1.0 million to £1.1 million, ie by an additional 10 per cent.

	Before	With 1% price increase	Net change
Revenue	£10.0m	£10.1m	+1%
Net profits	£1.0m	£1.1m	+10%

When you look at it like this, doesn't it seem a surprisingly easy way to increase your profits with a small increase in price? And just imagine what the change in net profit would look like if the increase in price was 2 per cent, 3 per cent, 5 per cent or 10 per cent.

Of course, the impact of a price change on your net profits will vary considerably depending on the financial structure of your business. If you have a manufacturing business like the example shown above, with a high level of direct costs and overheads, then you can expect a significant increase in your net profits from

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a small price increase. But if you have a service business with comparatively low direct costs and achieve a high gross margin for each sale (eg a software company or a consultancy), then the impact on net profits won't be as extreme. Imagine a service business with £10 million in revenue that generates net profits of £5 million. The example now looks like this:

	Before	With 1% price increase	Net change
Revenue	£10.0m	£10.1m	+1%
Net profits	£5.0m	£5.1m	+2%

A 2 per cent increase in net profits doesn't sound quite so impressive as a 10 per cent increase for the manufacturing company, but in cash terms it's still an extra £100K on the bottom line.

Boosting shareholder value

It gets even better than that if you're considering selling your business at some point in the future, or conducting a transaction to extract some shareholder value. When businesses are offered up for sale, the value that they command is usually based on a multiple of earnings as well as other factors, such as long-term growth prospects and the quality of the management team. If you take the example of the manufacturing business above, and let's say that they can achieve a multiple of 5 x their earnings, their business is therefore valued at £5.0 million (ie 5 x earnings of £1.0m). But with a price improvement of 1 per cent, they increased their net profits to £1.1 million, so the valuation has now increased to £5.5 million. In other words, a 1 per cent increase in price has generated an extra £0.5 million in shareholder value.

That's a spectacular return for such a small change in one aspect of your business. And this is what many investors like Warren Buffett, whether venture capital or private equity, are looking for in a business investment opportunity. Either before or after a transaction, they'll always be looking to improve the future

earnings of the business as part of a value creation plan because they know full well that improving the pricing is one of the fastest ways to generate higher profit growth on a long-term basis.

Case study: building pricing power

I worked for a client in the construction sector who designed and built balconies for apartments and high-rise buildings. They had a great reputation for high-quality products and fast installation. One of their USPs was that they could fit out a tower block with ready-made balconies using a crane in 24 hours as the balconies had all been specified to be slotted into the building's infrastructure. This saved a lot of time on site for the contractors and they also looked great for the future residents of the building. They'd designed an innovative new feature for the balconies that they believed would be in high demand because of incoming changes to building regulations. The MD of the business had a desire to spin off this new product as a separate business within his group and eventually sell it off to a third party to generate additional shareholder value for the business.

At this stage, most businesses would have got on with creating the new product and launching it to market, but this MD had the foresight to realise that he needed to get the pricing right for this new product to maximise future shareholder value. They wanted to find the right balance between pricing the new product at a premium to justify its enhanced performance but doing so in a way that wouldn't damage sales growth. We did some research on their competitors and spoke to potential customers to help us identify price points that were significantly higher than the business might have previously expected to charge. As a result of this work, we were able to put together a pricing model and a business plan that would generate millions of pounds of profit over five years.

The lesson from this story is that it's never too early to start thinking about your pricing power and working out how you can use it to improve future shareholder value and create profitable growth.

The key drivers of profit

If you get down to the basics of running a business you'll know there are only three key drivers of profit: price, volume and cost.

Revenue (Price x Volume) – Costs = Profit

It's quite simple. That's how your profit and loss statement is structured in your accounts. The volume of items you sell, at the price you charge for each item, minus the cost of producing each item, equals your profit. But my question to you is this: how much time do you spend thinking about each of these three aspects of your business? Either as a business leader or owner, or across your management team, how much time do you spend:

-  working out how to sell more volume?
-  finding ways to reduce your costs?
-  identifying ways to improve your pricing?

Take a moment to think about your answer by splitting the three items above across 100 per cent. When I ask this question at seminars, I usually find that small businesses spend most of their time focusing on how to sell more volume – sometimes up to 80 per cent of their time. This isn't surprising as the cost base for a small business tends to be quite low and the main imperative is to acquire new business to generate more income, cover your costs and grow the business. In larger businesses or corporates, the focus is more often on cost management. As one of my previous directors at a large corporate once said to me, 'We can control our costs, but we can't control our revenues.'

If you've ever been a budget holder in a large organisation, you'll know this situation all too well. The direction from the top is

usually to find ways to get your costs down, reduce your budget or do more with what you've got. Cost controls are extremely tight and rigorous in most large companies and a huge amount of time and effort is put into minimising costs and expenditure. A leading pricing expert (Simon 2015) estimates that in his experience of working with large organisations all around the world, they typically spend 70 per cent of their time managing costs, 20 per cent of their time trying to grow volumes and no more than 10 per cent of their time working out how to improve their pricing.

Time well spent

Whether large or small, it's my bet that most businesses spend no more than 5 to 10 per cent of their time trying to improve their pricing (and even that estimate may be high). What number did you write down in answer to the question above? It's understandable because we think that the best way to grow a business is to drive up revenues by selling more volume and keeping good control over our costs. But my argument is that if you accept that price, volume and cost are all important to generating profitable growth, then you should spend considerably more time on your pricing to achieve the business you want. My recommendation is that you spend 20 per cent of your management time working on trying to improve your pricing. Note that I do not mean calculating your prices using your existing methodology – I mean working out ways to improve your pricing.

You might consider this to be an extreme view. To spend one day out of every five on pricing? Well, given the examples of profit growth I shared above, why wouldn't you come to this conclusion? As you'll see as you read this book, there are many powerful ways in which you can improve your pricing and I bet you're not even scratching the surface in terms of what's possible for your business. And yet for most businesses, this would represent a significant increase in time spent on pricing. One client who heard me make this point at a seminar was really struck by it and

it made him realise that he was effectively spending no time at all on improving his pricing. He was just following the standard approach to pricing in his industry and was focusing on other ways to grow the business, ie gaining more customers, growing his team, managing his costs and so on.

Ten things a business will do to drive growth (before they look at pricing)

I find it surprising (and a little frustrating) that most business owners or leaders will look at many other strategies or plans to grow the business before they review their pricing:

1. redesign the website
2. rebrand their business
3. launch a new marketing campaign
4. create new products or services
5. enter new markets
6. cut costs and overheads
7. embark on digital or IT transformation
8. recruit more salespeople
9. invest in new systems
10. hire a marketing agency.

There's nothing wrong with any of these things if they're important to your growth plan. Yet pricing has the biggest potential for long-term profit growth. It provides a higher return on investment and a quicker payback period than any of the items shown above. But when it comes to pricing, most people think it's too risky to change anything, so choose instead to implement the latest shiny project (which will probably have a lower return on investment and longer payback periods).

Thinking back to my time in corporate life, I'm probably as guilty of this as anyone else. Before I fully understood the importance of

pricing, as a business leader I was always focused on finding new ways to increase sales and reduce costs – a new customer app, a redesigned website, a new sales promotion, a better-trained sales team, a new marketing campaign, a cost restructuring, a new IT system and so on. These projects would take massive amounts of management time as well as investment. Yet the biggest profit lever was always hiding in plain sight all the time.

What outcome do you want from your pricing?

Having worked with many hundreds of businesses on their pricing, I generally find that people start to think about doing something with their pricing when any of the following situations arise:

-  They're developing new products and services and need help with setting the price.
-  Their existing pricing is in a mess and they want some help sorting it out.
-  They're worried about rising costs putting pressure on margins.
-  They're nervous about increasing their prices and don't know how to achieve this.
-  Their core business is struggling and they need to increase revenues.
-  They don't know how to position their prices against the competition.
-  They're frustrated that their sales teams give away too much discount to win new business.

I conducted a small survey of business owners (in April 2021) and asked them which outcome was most important to them from a pricing review, and they answered as follows:

- | | |
|--|-----|
| 1. Increase net profits and margins | 58% |
| 2. Clarify our existing pricing strategy | 27% |

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3. Sell more volume and achieve higher revenues 8%
4. Design new prices (for new products/
opportunities/markets) 6%

OK, maybe the sample in the survey response was skewed because many of the respondents also followed my content. But I was still surprised that such a high proportion recognised that increasing net profits and margins was the most important outcome for them as a result of a pricing review. However, I think the second reason of wanting to get more clarity on existing prices is also a powerful motivator for change.

Case study: hot profits

I was referred to a business that manufactures hot food serving units for the retail sector. They are a family-owned company based in the Midlands and were growing fast because they had innovative products that created significant benefits for retailers and delivered amazing service to their customers. They'd designed their pricing using a cost-plus-margin approach and had tried to achieve a premium price in their sector. But they had no real strategy or structure with their pricing and the MD was pulling his hair out because every day a salesperson would knock on his door and ask, 'How much can I sell this unit for, boss?' He and his co-director were spending too much time trying to figure out prices for each new request that came in and his sales team were having a hard time justifying their high prices to their potential customers. He said to me, 'Mark, our pricing is in a mess and it needs sorting out.' His goal wasn't necessarily to increase profits from better pricing (although we achieved that as well); his goal was to have a clear pricing policy that everyone in the company understood and could apply to any new sales situation. We came up with a new pricing structure that had a range of new price options and created a clear discounting policy that rewarded larger order quantities so the sales team could use them without having to ask permission from the boss first.

The lesson from this example is that they achieved their primary goal of getting clarity on their existing pricing and empowered their sales teams to be able to respond to customer requests without having to go through a messy approval process. But we also achieved an uplift in their net profits and did this by designing some new price models that were easier to sell at a higher price. Reviewing your pricing can often have multiple benefits other than just an increase in your revenues and profit growth.

Four measures of pricing success

Utpal Dholakia, a professor of marketing at Rice University in Texas, is a leading pricing thinker. In his book *How to Price Effectively* (2017) he contends that there are four main measures of pricing success:

1. sales revenue growth
2. profit margin growth
3. customer satisfaction
4. employee satisfaction.

Which one do you think is the most important? Depending on your role in the company you might answer as follows:

-  The managing director believes sales revenue growth is the most important.
-  The financial director says it's profit margin growth.
-  For the sales director it's customer satisfaction.
-  The HR director thinks it's employee satisfaction.

In my experience of working with and in both large and small businesses, I generally find the top three measures are seen as the most important: sales revenue, profit growth and customer satisfaction. And no doubt they are, but I also think that if your employees (especially your sales teams) aren't happy about the prices they're being asked to sell at, then you won't achieve any of

the outcomes you want. In other words, my view is that employee satisfaction (regarding your prices) is the core enabler for the other three outcomes. If your employees aren't happy selling at your prices, you won't achieve the revenue and profit goals you want and you won't have satisfied customers.

Case study: the aggressive price rise

A client told me that, a number of years previously, his board of directors had commanded him and his team to increase prices by 10 per cent across the board. The board took this aggressive approach because they believed they had a high-value, premium product and that all their customers would pay up irrespective of the price being charged. Needless to say, when this instruction was passed down to the sales team to implement, they were nervous about it and worried about how their customers would react when they told them the news. They were given no extra training or briefing on how to manage this situation and were told to 'just get on with it'.

The outcome was messy, with lots of customers complaining and many of the sales team struggling to deal with the complaints. Although the team managed to deal with most of the issues, it created a situation that left a bad taste with both their clients and their employees. As a result, they were fearful of implementing any future price increases and resisted all pressure from the board to repeat these actions, thereby denying them the opportunity of ongoing price improvement.

The lesson from this story is that your employees are your most important asset, especially when it comes to pricing. It's essential they fully understand your pricing policy and know how to justify and explain your prices to any customer or prospect. Without this as an underlying foundation, you won't achieve the long-term growth you want in sales revenue and profit growth nor keep customers happy.

Price or volume?

Which is better: a 5 per cent increase in sales volume or a 5 per cent increase in prices? When asked to decide which outcome they'd prefer, most business leaders tend to choose a sales volume increase over a price increase. This is understandable because a sales volume increase means you're growing and becoming more successful. You're gaining market share, showing top-line growth and keeping your teams busy. And just having a 5 per cent price increase is a harder concept to accept because there are high perceived risks to this, including the potential loss of sales and customers. It also suggests you're not growing in the traditional sense, ie acquiring more customers and more volume. However, there can be a considerable difference in the profit impact between the two options.

Let's return to our manufacturing company, which is generating £10 million in annual sales revenue by selling 10,000 units at £1,000 per unit. If the direct cost of each unit is £500, then they are making a 50 per cent gross profit (which equals £5.0m). Assuming they have overheads of £4.0m (to pay for staff costs, premises, etc), then their net profit is £1.0m.

Metrics	Initial position	5% on volume	5% on price
Revenue	£10,000,000	£10,500,000	£10,500,000
Units	10,000	10,500	10,000
Price	£1,000	£1,000	£1,050
Gross Profit	£5,000,000	£5,250,000	£5,500,000
Net Profit	£1,000,000	£1,250,000	£1,500,000
Net Profit Increase:		25%	50%

-  A 5 per cent increase in volume will increase their net margin by 25 per cent to £1.25m.
-  A 5 per cent increase in price will increase their net margin by 50 per cent to £1.5m.

Note: I've assumed that there's no change in volume due to the price increase here. The point is to show that we tend to believe

that revenue growth is the ultimate goal for any business and when we follow this train of thought, we end up making bad decisions about pricing to achieve this goal.

The cost of discounts

Just think about the same situation in reverse. What's the impact of reducing your prices by 5 per cent? Let's say the management team at this company are struggling to grow sales in a highly competitive market and agree that the best way to maintain sales volumes is to lower prices by 5 per cent. The key question then becomes, 'By how much do we have to increase sales revenue to maintain our previous profit level of £1.0m?' In this case, the answer is that they'd need to generate additional sales of 43 per cent of volume just to maintain the same level of net profits. It's startling how few people realise the damaging impact that comes from discounting to increase sales. Do you know what impact a 5 per cent price reduction would have on your business? It's easy to do a simple calculation: just take 5 per cent of your total revenue off your net profit.

A note on price elasticity

In the example above, I assumed there would be no change in volume as a result of a price increase. This is unlikely to be the case in real life and most price change scenarios are affected by what economists term 'price elasticity'. For example, where a price rise of 1 per cent results in a decrease in volume of 2 per cent, this means that the price elasticity in this scenario is -2. When demand is inelastic, it means a change in price will have little effect on demand. I tend not to spend too much time on the concept of price elasticity with clients as I don't think most businesspeople understand it and therefore don't find it a practical tool for everyday use. Imagine trying to explain this to your sales teams! Instead, I prefer to think about the *price sensitivity* of your customers to your prices, which is a similar but more easily relatable concept.

It's far easier to ask yourself the question, 'How price sensitive are my customers?'

-  **High price sensitivity** – they're highly likely to switch to a competitor or not buy your product because your price is too high.
-  **Medium price sensitivity** – the price is an important factor in the purchase decision, but other factors are equally important (eg quality, brand service, features).
-  **Low price sensitivity** – they're unlikely to switch to a competitor or not buy because of price (ie price is less important than other factors, such as quality, reputation, service, features).

We can then use this concept to assess different price and volume scenarios when thinking about possible price changes. Having a good understanding of the price sensitivity of your customers is a cornerstone for better pricing, and I'll cover this more in Chapter 7.

The value of future prices

Most businesses will have a three-year business plan or financial projection. This normally entails producing fairly detailed forecasts and predictions about revenue growth and working out what costs you will need to support that revenue growth. Once you've worked out your projected increase in revenue and costs, you can identify your increase in profit growth. So far, so normal. But a trick I think most businesses miss is to forecast their price growth. And I don't just mean increasing prices in line with inflation (as you would do for your costs). I mean deliberately planning to increase prices year on year, even if you're not sure how you're going to justify those higher prices. This completely changes your outlook on price and instead of price being a function of the sales revenue target you want to achieve, it now becomes a key measure of the value you're trying to add to your products and services. It forces you to ask the question, 'How can we add more value to what

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we do to justify a higher price?’ Over time, you’ll have a far more valuable business than if you just focus on revenue growth.

Scenario 1

A simple approach to business forecasting might look like this:

Scenario 1	Current Year	Year 1	Year 2	Year 3
Revenue	£1,000,000	£1,050,000	£1,123,500	£1,235,850
		5%	7%	10%
Costs	£600,000	£618,000	£636,540	£655,636
		3%	3%	3%
Profit	£400,000	£432,000	£486,960	£580,214
		8%	13%	19%

The business has carefully worked out what revenue growth they want to achieve and has made some sensible assumptions about what cost increases they will have to accept. However, in this example, the business forecast is effectively assuming that there is no change in price at all over the next three years.

Scenario 2

Forecasting your price growth makes a big difference to your future profits:

Scenario 2	Current Year	Year 1	Year 2	Year 3
Volume	2000	2100	2247	2472
		5%	7%	10%
Price	£500	£515	£530	£546
		3%	3%	3%
Revenue	£1,000,000	£1,081,500	£1,190,910	£1,349,712
		8%	10%	13%
Costs	£600,000	£618,000	£636,540	£655,636
		3%	3%	3%
Profit	£400,000	£463,500	£554,370	£694,076
		16%	20%	25%

By taking the same forecast as in scenario 1 but adding a modest price growth assumption of 3 per cent, it makes a big difference to the company's future profit growth. Yet all too often, most businesses won't think about this key planning assumption in their forecast and will just focus on revenue growth and cost reduction as a way to grow profits. So make sure you always forecast your target price in the outer years of your business plan. If you have a large range of products, then it's fine to base this assumption on an average price, or an average price per product category if that makes the task easier.

Know your pricing power

Do you know what your pricing power is? Warren Buffett would certainly want to know this about your business. It's an assessment of your pricing strengths and capability across all the aspects of your organisation that may affect your price. Your pricing is intertwined with many different areas of your business, including:

-  your product range
-  your sales performance
-  customer satisfaction
-  your profitability
-  your business growth ambitions
-  your competitors' pricing
-  your market situation.

I've developed a simple questionnaire that allows you to work out your pricing power score by answering the 28 questions below (adapted from Liozu 2018). Based on the data from hundreds of businesses, I believe that these are the most important factors that affect the pricing power of businesses, especially in the SME sector. Have a go at working out your pricing power by thinking about all the questions below, and giving them a yes or no answer. For every 'yes' answer, give yourself one point and then refer to the section below to find out how well you perform.

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1. Have you grown your revenues and sales volumes in the past 12 months?
2. Have you forecast your target prices in your business plan?
3. Are you clear on your desired price positioning?
4. Do you know what your main pricing challenges are?
5. Do you know the full range of prices your customers are willing to pay?
6. Do you know by how much you could increase your prices without it negatively affecting sales levels?
7. Do you know how to segment your customers by different price levels?
8. Have you ever asked your customers what prices they would be willing to pay?
9. Do you know the price points of your main competitors?
10. Are you able to acquire new customers reasonably easily?
11. Do you know how to justify your prices versus a competitor?
12. Are you able to avoid giving away unnecessary discounts to win new business?
13. Do you have a clear specification of what's included in your product offering?
14. Have you asked your customers which are the most important aspects of your product or service?
15. Do you know the unit cost for each of your products?
16. Do you understand how customers perceive the value of your products and services?
17. Do you have a history of implementing price increases regularly?
18. Do you have good controls on how your prices are calculated and approved?
19. Do you use at least five different pricing strategies?
20. Do you have a wide range of different price points in your product range?

21. Do you have a clear value proposition that communicates the benefits of your offering?
22. Do you know how to apply psychological pricing tactics (eg price anchors, decoy prices, price thresholds)?
23. Do you have a clearly defined discounting policy?
24. Have you optimised the presentation of your prices (eg in proposals, documents, slides, websites)?
25. Is your business as profitable as you would like it to be?
26. Do you have a written pricing policy that is trained out to all staff who need to refer to prices?
27. Do you and your team have full confidence in your pricing?
28. Do you know what difference a 5 per cent increase in your prices would have on your net profits?

Your score

Strong – if you scored 21–28 (more than 75 per cent), you have strong pricing power. Congratulations! Very few companies are genuinely at this level.

Adequate – if you scored 14–20 (more than 50 per cent), you have adequate pricing power. Well done. Although there's still room for improvement in some areas, you're doing many things well and have the foundations you need to achieve strong pricing power.

Poor – if you scored 7–13 (more than 25 per cent), you have poor pricing power. There are a significant number of areas of your business where you aren't clear on your strategy, which results in poor pricing power. But don't worry! By focusing on those areas where you scored lowest, you can make a big improvement fairly quickly.

Weak – if you scored 0–6 (less than 25 per cent), then you have weak pricing power. There are serious issues with many parts of your business and how they impact your pricing power. Your

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business is probably struggling and may be at risk of long-term decline. You need to take urgent action to address the issues highlighted by your survey results if you're going to thrive in the longer term.

Having conducted this exercise with hundreds of companies, I've found that the following questions are the ones that most people score lower on and which affect their pricing power score:

- 6. Do you know by how much you could increase your prices without it negatively affecting sales levels?
- 9. Do you know the price points of your main competitors?
- 15. Do you know the unit cost for each of your products?
- 17. Do you have a history of implementing price increases regularly?
- 19. Do you use at least five different pricing strategies?
- 22. Do you know how to apply psychological pricing tactics?
- 26. Do you have a written pricing policy that is trained out to all staff who need to refer to prices?

If you scored yourself lower on any of these, then take some comfort from the fact that you're not alone. Most businesses in the world would struggle to score well on these statements and it's only those with a mature level of pricing capability that perform strongly in these areas. Once you've read this book and had the opportunity to apply some of the techniques in it, I hope that you'll redo the questionnaire and see how your pricing power will have improved in a number of key areas.

CHAPTER SUMMARY

In this chapter, I've looked at the concept of pricing power and why it's important to every company that wants to achieve profitable growth.

In summary, you should understand the following points and why they're important:

-  Companies with **strong pricing power** also have **highly valuable businesses**.
-  Price is the **biggest lever** you can pull to **increase profitable growth**.
-  A **small increase in price can make a big difference** to your net profits and shareholder value.
-  Increasing the **amount of time** you spend on **improving your pricing strategy** will reap huge dividends.
-  **Tackle your pricing** before you get sucked into starting another shiny new growth initiative.
-  Make sure your **people are fully on board** with your pricing strategy and that they **know how to communicate and justify** your prices to your customers.
-  Calculate **the difference a 5 per cent increase or a 5 per cent decrease** on your overall prices will make on your net profits.
-  Ensure you **forecast your desired future price points** in the outer years of your business plan.
-  **Know your own capabilities.** Assess your pricing power and work out what areas you need to work on to achieve a better outcome.

In the next chapter, I'll look at what happens when pricing goes wrong and share some more examples of why I believe pricing is the most important part of your business.

Perfecting your pricing is fundamental to the success of your business. It affects how your customers perceive you, it can make or break a sale, and it's the most powerful key to profitable and sustainable growth.

But how do you know your pricing is right? How do you approach making this most crucial of decisions with confidence and clarity?

In *Pricing for Success*, leading pricing expert Mark Peacock takes a fresh look at the power and psychology of pricing and walks you clearly through 7 essential steps that will improve your pricing, delight your customers, and create a more profitable business.

Through an illuminating and informative blend of straightforward examples, templates and real-life case-studies, presented alongside over fifty expert pricing tips, tools and tactics, you'll discover:

- Why pricing is your biggest lever for profitable growth.
- The persuasive pricing techniques that have the biggest impact.
- How customer-driven approaches make it easier to boost your bottom line.
- The surprising truth about premium pricing and how it's easier to sell.
- How to cleverly structure your offer so you can optimise your prices.
- How to avoid common pricing pitfalls and lose your fear of losing business.

The time you spend on getting this right is the best investment you'll make in your business. So, stop leaving money on the table, start taking control of your pricing and create a powerful new approach to pricing that will unlock higher profits and provide sustainable business growth.

“Relevant and practical! Packed with advice on why price matters and the importance of getting it right.”

David Pritchard, Managing Director, Sandler London East

“Excellent! Makes a difficult subject simple and explains the true power of pricing.”

Roy Newey, Chairman, CEO and Author of

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