

Why Lowering the Price May Be A Bad Decision?

AS THE UNITED STATES AND GLOBAL ECONOMIES CONTINUE TO STRUGGLE, MANUFACTURERS ARE UNDER INCREASING PRESSURE TO GENERATE SALES. THIS ADDED PRESSURE ALL TOO OFTEN RESULTS IN A RUSH TO LOWER PRICES IN THE UNREALISTIC EXPECTATION THAT THE LOWER PRICES WILL SPUR LARGE INCREASES IN DEMAND OR AT THE VERY LEAST PREVENT LARGE LOSSES IN DEMAND.

Price is the easiest thing for you to change in response to changing market conditions but unfortunately it is also the easiest thing for your competitors to match. Unfortunately many manufacturers are learning that large knee jerk price reductions in competitive markets coupled with weak demand may only accelerate sales losses – thus creating pressure to lower prices even more.

Why does lowering the price often backfire?

1 PRICE IS EASIEST THING TO MATCH. Price is the easiest thing for you to change in response to changing market conditions but unfortunately it is also the easiest thing for your competitors to match. The argument usually has an element of variable costs vs. fixed costs as the method of justifying large price reductions, but rarely does anyone mention the competitive response. If price reductions actually resulted in a substantial change in demand for your brand as compared to your competitor's brand – then your competitor would likely be quick to match the price. The net result is both you and your competitor lose profitability and in most cases suffer lower sales because the increases in demand were minimal.

This strategy only works if you are the low cost producer and you can reach a price point your competitor will not match.

While it may be obvious in today's bad economic climate that some price rationalization is inevitable – it does not mean the significant or broad price reductions are justified.

2. BRAND VALUE IS DIRECTLY RELATED TO PRICE.

Even if you are the low cost producer, price is a reflection of your brand value and recovering lost brand value is difficult. Obviously some adjustments in pricing are necessary to reflect changing market conditions, but broad price reductions may injure your brand value long after the economy recovers. Price will always be the easiest way to react to changes in the market, but other measures such as alternate product bundling, reducing features, or offering added services at reduced prices may be far more effective.

3. MARKET DEMAND CHANGES ARE NOT UNIFORM.

Changes in end user demand in a down market are rarely uniform across all products, applications or customer segments. Uniform price drops which result in little or no change in end user demand only lower profits. Providing more aggressive special pricing for specific products, applications or customer segments often makes far more sense than across the board price reductions.



Mike Kelly



Difficult economic conditions can provide manufacturers a powerful window of opportunity to thoughtfully rethink not only your overall pricing strategy but all of the incentive and rewards built into your discount structure and marketing programs offered to channel partners.

4. PARTNERS DO NOT ALWAYS PASS ON THE LOWER PRICE. Channel partners demanding competitive price reductions are under no obligation to pass the price reductions to the end user, and often simply keep the extra margin. If the channel partner's customers don't benefit from price reductions, there will likely be no resulting change in market demand.

5. LARGEST CHANNEL PARTNER USES UNIQUE PRICE CONCESSIONS TO STEAL SHARE. Manufacturers often feel the greatest price pressure from the largest channel partners. This often results in negotiation of special big partner price concessions not available to other channel partners. The large channel partner then will use the price concession to steal business the manufacturer already had won from competing distributors. This alienates the remaining channel partners and causes an overall loss in channel commitment to your brand.

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SUMMARY

To arrange a complimentary half-day session to discuss your channel pricing programs, call Mike Kelly at 312-558-4832 or email mkelly@franklynn.com