



Answering RFQs, PDQ

New software helps companies optimize prices. One caveat: it often comes with an optimized price.

[John Edwards](#), CFO Magazine

March 01, 2004

A cynic, we're told, knows the price of everything and the value of nothing. Well, Michael Towe isn't a cynic, but he does know the price of everything—or at least everything sold by GE Transportation International Pool (TIP) and GE Modular Space (ModSpace). As CFO of General Electric Co.'s Equipment Management division, part of Towe's job is to set the prices on the company's buildings and over-the-road trailer services.

Crucial to the task: making sure the prices he sets max out profits—without sending customers packing. To help strike that delicate balance, and to do it quickly, Towe relies on a special breed of software known as price-optimization (PO) technology. "The benefits have been substantial," says Towe. "We are able to serve more customers with faster response times on pricing."

A kind of business-intelligence program, price-optimization software appears to be catching on with other U.S. companies as well. According to International Data Corp. (IDC), a technology research firm headquartered in Framingham, Mass., sales of PO software, which totaled \$86 million last year, will top \$133 million by 2007.

Certainly, there's no shortage of vendors marketing the stuff. IDC currently identifies 20 major companies (including i2 Technologies, KhiMetrics, Metreo, ProfitLogic, Rapt, Vendavo, and Zilliant) flogging PO software. "Pricing has historically been done in a very offhanded and intuitive way," notes Robert Blumstein, CRM analytics and marketing applications research director at IDC. Now, he says, "pricing has become part of a larger movement toward marketing automation and CRM analytics."

Secret Sauce

Essentially, PO software weighs scores of factors, including customer demand, desired sales velocity, and the amount of revenue a business needs to be profitable. Vendors offer either stand-alone PO applications or more-robust suites. The suites combine price optimization with other applications, such as demand-planning and pricing-execution programs.

The technique itself is not new. Airlines began using PO solutions in the 1980s to instantly price fares based on such variables as booking lead time, flight date, connections, time of day, service class, and customer preference.

Analysts say the arrival of faster and cheaper servers has piqued the interest of executives in other sectors. Indeed, companies are now able to run high-octane PO software without buying a supercomputer. Notes Paula Rosenblum, retail research director for independent research analyst firm AMR Research: "Advances in hardware have enabled [customers] to actually run these situations and forecasts in a reasonable time frame."

Even with the rapid advancement in software and hardware, price optimization remains an inexact science. Various applications are likely to churn out different results. Why? Because PO programs are driven by proprietary forecasting engines. These engines are based on sophisticated mathematical algorithms originally developed for scientific research and military planning. "It's almost like rocket science," says Kosin Huang, a senior business applications and commerce analyst at The Yankee Group, a technology research and consulting firm. "It's like the secret sauce that's behind the whole thing."

For her part, Rosenblum says potential customers shouldn't be overly concerned about finding exactly the right software. "Wherever [the programs] have been put into use," she asserts, "they have proven results."

Maybe so, but better pricing doesn't come cheap. PO vendors, which clearly use their own software, have affixed some pretty high price tags to their products. Analysts say license fees for the software range from \$300,000 to \$1 million. Rosenblum says vendors can charge nosebleed prices, however, "because the return on investment is so high."

PO'D

Managers at Essex Electric Inc. no doubt hope that's true. The Fort Wayne, Ind.-based maker of cable and wire is about to begin a two-month trial of Metreo's PO software. According to Brad Thomas, Essex's vice president of sales, the application will automate the company's existing manual pricing process. Currently, Thomas says, he establishes Essex's pricing parameters each day, based on the plans and forecasts that the company puts into place. Specific pricing decisions are then made for individual requests for quotes. "We basically quote just about every inquiry, RFQ, one by one as they come up," he says. "It's a very fast-paced, volatile type of operation, and

our needs and wants can change on any given day."

Thomas believes that by automating approximately 75 percent of Essex's pricing decisions, the overall impact of the PO system will improve the margin by 1 percent. "One percent doesn't sound like a lot," he notes, "but we're dealing in major volume so it's very significant to us." The Metreo application also promises another benefit. "This system will allow us to collect data so that we can spot trends," says Thomas. "We're looking to do a better job of analyzing our business."

But IDC's Blumstein cautions that price-optimization software works only as well as its available data sources. "It's the familiar situation of garbage in, garbage out," he says. He counsels adopters to keep a sharp eye on data integration and cleanliness. He also says PO software users should take great care in selecting external data sources.

Even with slightly skewed data, however, price-optimization software promises to improve the RFQ process. Before deploying Zilliant's PO software two years ago, GE TIP/ModSpace's price-setting structure was a decentralized, ad hoc effort. Local pricing, notes Towe, was done manually by individual associates. "This made it very difficult to ensure that the best customers received the best prices, especially with national contracts," he recalls.

The GE TIP/ModSpace software not only pinpoints the best possible price points, but it also helps managers act and react more quickly. The numbers tell the tale. Towe says the unit's cycle time for matching the appropriate price to a particular deal has dropped by 97 percent, with deal response time halved. "The investment has more than paid for itself," he says. "It allows us to be very competitive with almost any player in the market."

Swelling, Tapping

Despite the raves, price-optimization backers warn potential adopters to carefully plan their PO strategy. Software is only part of the game, notes Towe, who advises users to match technologies with long-term strategies for a particular customer base. His advice? "Bring in the pricing professionals to understand your environment and educate you on the appropriate solution."

The ranks of pricing professionals will likely swell in the next few years. Analysts say it's probable that CRM and ERP suite vendors will eventually want to integrate PO technology into their product lines. "A large suite vendor, like an SAP or an Oracle, might buy up one of these vendors and just take over the industry," predicts Huang.

Until then, existing vendors should see a steady—if modest—rise in business. Blumstein believes makers of PO software have just begun to tap the market's potential. But he adds: "The market isn't going to grow as fast as it could if it had lower price points."

Oh, sweet irony.

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