

Consumer Goods TECHNOLOGY



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Special Report

The world may never know the formula behind Coke Classic or why a box of cereal costs more than a bushel of bananas, but there is one closely guarded secret in the consumer goods space that is beginning to unfurl: price optimization. A rising number of consumer goods firms are now in on the secret that price management software yields an impressive ROI, upwards of 5 percent to 11 percent, according to a report from The Yankee Group. In addition, 48 percent of 456 respondents say they currently use technology to manage pricing while 25 percent plan to invest in technology within the next year to handle customer specific pricing electronically (see chart).

"Companies other than those in retail, travel or hospitality are beginning to take charge of pricing and are proactively optimizing, executing and analyzing pricing opportunities, however, these companies are still in the minority," says Kosin Huang, The Yankee Group. Huang says the market for price optimization technology is slowly keeping pace with the recovering economy, however, it won't be long before pricing software becomes the next killer app du jour.

Why? According to Larry Warnock, vice president of Sales and Marketing for Zilliant, a software firm that captures real-time purchasing data and organizes it into analytical models to determine optimal price, it's an untapped source of cost-savings.

"Most costs have already been ripped out of organizations business models," says Warnock. "This is the last knob to turn but it's not a knob to turn lightly."

Warnock says price optimization is about bringing science and analysis together to answer the age-old question of what the market will bear.

"It's the last bastion of guesswork in American business," says Warnock. "But it involves fine tuning with a scalpel as opposed to coming in with an axe."

Warnock also says that the first step in understanding the importance of price optimization involves avoiding the common pitfalls practiced today to determine the price of products:

- Relying on anecdotes "from the field"
- Cost Plus — What it costs to make a product plus the addition of a default margin
- OTA — "Out-of-the-air" pricing where companies watch and match competitors

Since most Tier 1 consumer goods firms spend hundreds of millions of dollars on brand-bolstering initiatives alone, one would think the aforementioned tactics would be a thing of the past and that a higher degree of investment would be allocated towards price optimization tools. The other argument in favor of price optimization is that it's not just about cutting costs but increasing margins.

"Ideally, price optimization is all about getting the price as high as a brand will allow," says Warnock. "Take a product like Morton Salt. They are charging a premium price for a product that can be found on a beach."

While many industry experts believe that price optimization software will not establish itself as a stand-alone market, the impressive ROI it delivers indicates that it is here to stay. Over the next five to seven years, The Yankee Group predicts that large enterprise application vendors like SAP, Oracle, PeopleSoft and Siebel will want a piece of the pricing software action.

"The challenge for the suite vendors will be in replicating true price optimization and analytics in their product offerings," says Kosin Huang of The Yankee Group.

Consumer goods firms must be able to quickly adapt to prices and proactively manage changing market conditions and competitive price moves. As more success stories surface, expect to see a glut of key verticals in the consumer goods space cash in on price optimization.