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Become a value merchant

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Become a value merchant: A plan for prospering in modern-day markets

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Let's begin with a brief story:

A supplier of integrated circuits (ICs) for correcting power input was competing for the business of an electronic device manufacturer, which was projecting a demand of five million units for incorporation into its next-generation device. In the course of the negotiation, the supplier's salesperson learned that he was competing against another firm whose price for the integrated circuits was 10 cents lower per IC—45 cents versus 35 cents.

The customer asked the salesperson from each firm what the source of the superior value for his offering was relative to the competing offering. This salesperson replied that it was his personal and dedicated servicing of the account.

Unbeknownst to him, the customer had built a customer value model, in which it had found that his offering, though 10 cents per IC higher in price, was actually worth 15.9 cents more per IC than the alternative supplier. Further, the electronics engineer who was leading the development project had recommended to the purchasing manager supporting the project that he purchased those ICs, even at the higher price. The salesperson's personal and dedicated servicing as a favorable point of difference was indeed worth something in the model: .2 cents!

Unfortunately, the salesperson overlooked the two value elements providing the greatest differential value, apparently unaware of the magnitude of the differences and what those differences were worth to that customer. As expected, when push came to shove in the negotiations with purchasing, perhaps suspecting that his superior service was not worth the 10-cent difference in price, the salesperson gave a 10-cent price concession to match the competitor's price and "win" the business. The result? The firm just lost $500,000—five million units at 10 cents each—of potential profit on a single transaction!

Purchasing managers in business markets are becoming increasingly sophisticated in their strategies and tactics. Increasingly held accountable for reducing costs, purchasing and other customer managers don't have the luxury of simply believing suppliers' claims of cost savings. A relatively easy and quick way to obtain savings is for purchasing managers to focus on price and obtain price concessions from suppliers. To enhance their negotiating power, purchasing managers attempt to convince suppliers that their offerings are the same as their competitors, so that they could be easily replaced.

In the face of such pressure, as the IC example illustrates, suppliers cave in and match competitor prices.

It is a rare commodity in business markets to find firms that do business based on demonstrably superior value.

Value merchants versus value spendthrifts

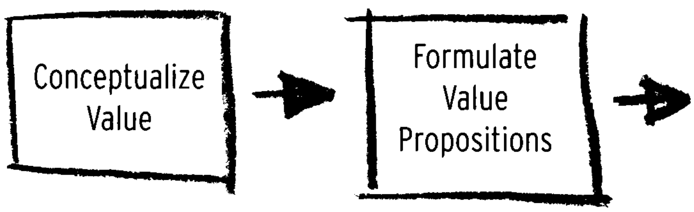
A value merchant recognizes the supplier's own costs and the market offering's value to the customer and works to obtain a fair return for both the supplier firm and customer firm. The value merchant stands in stark contrast to the all-too-common value spendthrift, who squanders the superior value of the supplier's market offerings while getting little in return. Below, you'll find a series of paired statements that contrast value spendthrifts and value merchants. By candidly picking the statement in each pair that best describes your salespeople, you can construct a profile of them that indicates the extent to which they are value merchants or value spendthrifts.

Your salespeople:

1. Routinely trade more business for lower prices, or routinely gain more business at the same price.
2. Make unsupported claims about superior value to customers, or demonstrate and document claims about superior value in monetary terms to customers.
3. Focus on the revenue/volume component, or concentrate on the gross margin/profitability component of their compensation plan.
4. Give price concessions without changes in the market offering, or only give price concessions in exchange for cost-saving reductions in the market offering.
5. Complain that our prices are too high, or else complain our proof of superior value is lacking.
6. Give services away for free to close a deal, or strategically employ services to generate additional business.
7. Prefer to give quick price concessions to close deals and go on to other business, or are willing to "hang tough" in the negotiations to gain better profitability out of each deal.
8. Believe management pursues a capacity-driven strategy, or believe management pursues a value-driven strategy.
9. Sell primarily on price comparisons with competitors, or sell primarily on customer cost of ownership comparisons with the same competitors.
10. Tell us customers are only interested in price, or tell us customer insights to improve the value of our offerings.

Customer value management explained

Doing business based on demonstrating and documenting superior value is, indeed, a rare commodity. Yet it doesn't have to be so. By adopting the customer value management approach presented below, value merchants can prevail when they encounter challenges of the type that the IC salesperson faced. The accompanying figure places the processes in sequence.



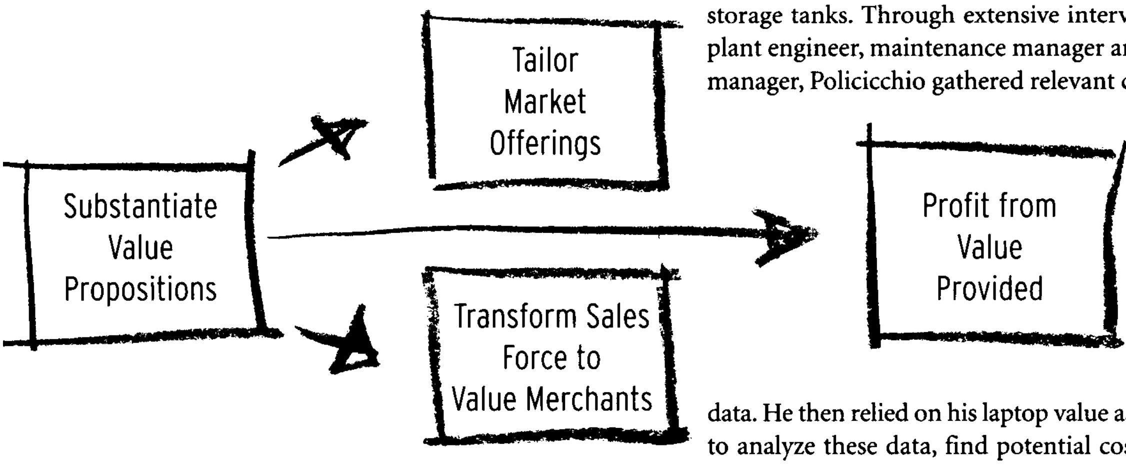
Conceptualize Value focuses on the fundamental building block of the customer value management and addresses questions like these: What do we mean specifically by "value" in business markets? How does one define points of difference, points of parity and points of contention vis-à-vis the next-best alternative? What are the three types of value propositions suppliers use in business markets, and why is a value proposition with a resonating focus preferred over the other two?

Formulate Value Propositions begins with analyzing what potential changes in the market offering customers would value most vis-à-vis the next-best alternative. This is used to develop a value proposition to aspire to, and qualitative research is conducted to refine the value proposition. Finally, value word equations are developed to capture the points of difference in terms that customers can readily understand.

Substantiate Value Propositions provides a methodology for persuasively substantiating value propositions to customers. The value word equations are brought to life with data that is gathered in a customer value assessment. They are then used to construct value calculators that demonstrate the value to customers. Finally, value case histories and value documenters help prove to customers that they did indeed receive the value that the supplier promised them.

Tailor Market Offerings demonstrates how a deep understanding of customer value can be used to construct segment-specific market offerings as naked solutions with options. Instead of the usual vanilla approach that provides the same bundle of products and services to all customer firms, a supplier can offer these flexible market offerings. This allows more refined targeting through various levels of service and enables suppliers to capitalize on differences between customers.

Transform Sales Force to Value Merchants challenges suppliers to transform their sales forces from selling on price to becoming value merchants. While getting sales compensation aligned with selling on value and profit is critical, it is not enough. Businesses must foster value merchants and put a value-selling process and value-based sales tools in place. They must ensure initial and ongoing value-selling experiences with customers while instilling and invigorating a value merchant culture.



Profit from Value Provided is all about how companies can profit from the superior value they provide customers. Although it is natural to think first of price premiums, there are also three other means of obtaining a fair return from customers for value provided in business markets: a more profitable mix of business, a greater share of the customer's business, and the elimination of value drains and value leaks. [Editor's Note: Value drains and value leaks were detailed in the *Value Merchants* Book Excerpt, which appeared in the March/April issue of *S&MM.*] But getting a fair return requires the supplier to manage pricing as if profitability depended on it! To accomplish this, a value-based approach to pricing at the strategic, tactical and transactional levels is necessitated.

A value merchant delivers profit

A recent experience from Rockwell Automation exemplifies how value merchants gain profitable growth. A condiment producer hastily summoned Rockwell Automation sales representative Jeff Policicchio to participate in a "Continuous Improvement Conference" at one of its major plant sites. Facing considerable pressure from Wal-Mart to lower its condiment prices, the producer decided to invite its incumbent suppliers, as well as competing suppliers, to a meeting designed to find ways to dramatically reduce its operating costs. Along with competing supplier sales reps, Policicchio was given full access to the plant and its personnel for one full day.

From discussions with plant personnel, he quickly learned that a major and recurring problem stemmed from lost production and downtime attributable to poorly performing pumps on 32 huge condiment storage tanks. Through extensive interviews with the plant engineer, maintenance manager and purchasing manager, Policicchio gathered relevant cost and usage data. He then relied on his laptop value assessment tool to analyze these data, find potential cost savings and construct the best pump solution for the customer.

The next day, Policicchio and his competitors were called back to the plant; all were given one hour to prepare a solution proposal and present it to plant management. Following the presentations, he learned that he was the only one to demonstrate tangible cost savings for his proposed solution. Everyone else made fuzzy promises about possible benefits. Stated simply, Policicchio's value proposition was, "Through this Rockwell Automation pump solution, your company will save at least $16,268 per pump—on up to 32 pumps—relative to our best competitor's solution through the elimination of most downtime, reduced administrative costs associated with procurement and lower spending on repair parts."

Plant management was so impressed with Policicchio's value proposition that they immediately purchased one pump solution for a trial. After a suitable period, plant managers audited its performance and discovered it to be even better than predicted. Based upon these findings, they placed orders for the remaining pumps, which will be installed as the existing pumps wear out.

James C. Anderson, Nirmalya Kumar and James A. Narus are the authors of *Value Merchants: Demonstrating and Documenting Superior Value in Business Markets* (Harvard Business School Press).