Capturing the value of innovation in a multinational organisation

- A case study of pricing strategies across four different countries

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Abstract

Title: Capturing the value of innovation in a multinational organisation -
A case study of pricing strategies across four different countries

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Company: “Global Processes”

Key words: Innovation, Strategic pricing, Profitability, Unique selling
proposition, Price leadership.

Purpose: To demonstrate the importance of innovations for becoming
competitive and profitable and to illuminate the importance strategic
pricing to capture the full value of innovation.

Methodology: A qualitative approach is chosen where interviews have been the
main source for the collected data.

Theoretical perspectives: Profiting from innovation, Innovation premium, Strategic pricing,
Price leadership, Transactional level, Market level, and Industry
level.

Empirical foundation:

Conclusion: Innovations together with strategic pricing are two important
aspects for Global Processes to reach profitability.
“In 1999, the company Arthur D Little undertook a study that involved 700 companies worldwide, as well as a number of Wall Street analysts. It came to the conclusion that Wall Street places a higher premium on innovation than on any other approach to generating bottom- and top-line growth, and that more than a change of leadership, more than a merger or an acquisition, more than a renewed commitment to cost reduction, investors consistently reward - and pay a premium for – innovation.”

(Professor Calie Pistorius, Vice-Chancellor and Principal, University of Pretoria)

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Global competition forces companies to squeeze unnecessary cost out of every part of their business, while simultaneously increasing customers’ willingness to pay (Burgess, 1982). The willingness to pay increases if the company can sell a good or service with new and outstanding characteristics, such as an innovation (Spulber, 2004). Several companies have been able to charge premium prices on their innovation efforts. Porsche has developed the ceramic brake which is sold as a luxury choice of extras and they are thereby able to charge price premium. The iPod from Apple is another successful story. In just over four years, the iPod/iTunes product and business strategy has helped Apple double its market cap, establish over 80% market share in two very profitable industries, and drive almost $3 billion per year in revenue (Lefkow, 2005). Canon has managed to achieve extraordinary results by relying on own researchers and business innovations. The success of reaching almost 1 billion a year in 1997 on revenues of 21 billion is directly tied to its innovation strategy (Jonash and Sommerlatte, 1999). The Polaroid camera, Microsoft’s Windows and the Walkman from Sony are examples of products which have made its innovators enviable.

In the book *The Price Premium* (Jonash and Sommerlatte, 1999), it is concluded that “Wall-Street places a higher value on innovation than on any other approach to generating bottom- and top-line growth...More than a change in leadership, more than a merger or acquisition, more than a renewed commitment to cost reduction.”

But all innovations don’t end up a success story. The safety match was in the beginning too expensive to produce, and when it finally were made cheaper the patent was expired. This meant that several other companies were able to profit from the innovators efforts. Another innovation is the digital pen made by Anoto. The company has now barely managed to turn their losses into profits after several years of heavy expenses and negative bottom lines. The future will tell if the investment was worth it.
In concluding, it is not enough to come up with a new product or service to become successful. In order to maximize revenues, an understanding of what the product or service is worth in the customer’s eye is critical to make her pay as much as possible. This phenomenon of selling at prices on the perceived value to the customer, rather than on production cost, market price, competitor price or historical cost is called value-based pricing (Marn, Roegner and Zawada, 2004). The phrase value-based pricing has become widely used within companies and is popular to mention in the company’s strategic objectives to demonstrate management’s awareness of its importance. Unfortunately, although it seems to be a common goal for managers, applying value-based pricing in practice is problematic. Companies wrestle with the fact that value-based pricing remains one of the most misapprehended and poor-managed functions (Duke, 1994). Not only are the small or low performing companies well acquainted with this reality, but also the giant top performers on the market. Adding to the dilemma is the fact that product life cycles continue to shorten due to high speed of innovation as well as faultless imitation of products, which makes it problematic to achieve price premiums on novel products (Klepper, 1996). This “problem” is something all companies must be aware of and make use of. If a company can develop a new product or process and protect it well from being copied by competitors, an enormous amount of money can be earned that will make the company profitable for several years ahead (Scherer, 1998; Geroski, Machin & van Reenen, 1993).

To be able to profit from innovation, a company must be able to understand value-based pricing to achieve price premiums. Unable to do this, the cost of creating the innovation can never be justified, thus, innovation activities within the company will diminish or stop. Especially in high technology markets, it is critical to set the right price. Hence, the market is very transformable, consists of shorter products life cycles and is dependant on technological breakthrough (Grunewald and Vernon 1988).

This thesis will cover both advantages and disadvantages of innovation. We will follow a multinational company to see how it can become more successful by focusing on its innovations. But we will also undertake an analysis on its pricing efforts and demonstrate why strategic pricing is crucial for companies who want to become truly profitable. The study is of interest since there are, to my knowledge, no previous studies that have dealt with the relationship between innovation and pricing in any sense making way (Weick, 1995).
1.1 Background

The company studied in this research, *Global Processes (GP)*, is a specific division within the incumbent company “Global”. Its main task is to assemble and sell processing equipment. “Global”, is a well established privately owned company with over 20 000 employees in more than 150 countries. It consists of independent divisions responsible for their own budgets (Global Processes is one on them), and may be defined as an internal market, having inter-company prices or transfer prices (Reger, 2003).

GP’s customers are the largest in its kind, but they also have several small customers. The smallest customers however, do not afford to buy from GP. The company has two global competitors, as well as some small and local ones.

The thesis is the result of a project which took off in March 2008, aiming to create a starting point for a new strategic pricing initiative within the whole organisation. The purpose of the project was to make sure that GP where getting as high margins as possible of their products and services. One of the reasons for a new strategic pricing initiative was the fact that GP were unsatisfied with their margins. They were afraid they were giving their margin away “for free”, not taking advantage of the profit which could be generated by innovations and other attractive advantages of the company. This conclusion was reached when realizing that competitors had the same expenses, but still were able to charge lower prices to their customers. Adding to this problem is the fact that GP was perceived as a high price alternative compared to its competitors. The company was afraid that their customers would leave them if they increased prices, implying that price sensitivity was high among customers.

1.2 Purpose

The purpose of this case study is two-fold. First, this thesis aims to empirically examine how GP can make use of innovations to reduce customers’ price sensitivity and become more profitable in the long run. Second I will analyse which factors that are affecting the sales and pricing process, both positively and negatively. The result will be used for an analysis of how GP can make sure to capture the full value of innovation by making their customers more willing to buy. Based on this analysis, suggestions on how GP can decrease price elasticity towards zero are made on three different company levels.
1.3 Problem statement

In order to reduce price sensitivity, Global Processes must find out what their customers find important and make use of this knowledge to stand out from their competitors. Hence, the research question of this thesis is following:

*How can an incumbent company in a mature market reduce price elasticity through innovation?*

To answer the question above, two specific topics must be addressed. *First*, the term innovation needs to be defined and its nature and effects on the company must be explained. *Second*, pricing issues must be outlined in order to demonstrate how a company can use them for strategic purposes. Therefore, two additional sub-questions must be asked to support and explain the main empirical question.

- *How can innovations help Global Processes reduce customer’s price sensitivity?*
- *How can Global Processes become more profitable through a new pricing strategy?*

1.4 Target audience

The complex nature of decreasing price elasticity through innovation makes it difficult for managers to apply it in their organisations. However, it becomes more and more important to develop competitive resources, and innovation as a strategic resource is one area where many organizations are underdeveloped. This thesis is mainly intended for those who wish to achieve greater comprehension about innovation and pricing as a strategic resource. By understanding the advantages it brings, its complexity and difficulty to apply it may not be as threatening in the end.

1.5 Delimitations

The ambition of this thesis is to keep a strategic point of view rather than viewing it from a marketing approach. The thesis does not include a customer analysis, nor does it fully describe the competitors or the competitive situation. Customer’s attitude has been pointed out by questioning account managers, which are the ones who have direct contact and receives feedback from customers. *It is important to have in mind that both customers and*
competitors are equally important to analyse when using pricing as a competitive source. Unfortunately, time and space constraints have made an analysis of these two areas impossible to perform.

1.6 Structure & Disposition

Chapter 1 opens this study by introducing its background and its purpose.

Chapter 2 then continues with a clarification of the methodological approach.

Chapter 3 begins with an explanation of the definition on innovation and assesses risks and advantages for innovating firms. Second, the chapter continues with the theoretical framework for understanding strategic pricing issues in terms of complexity, performance enhancing effects and managerial difficulties.

Chapter 4 presents the case and provides the empirical findings on the four different markets that represent the investigated company of the research.

Chapter 5 provides an analysis of the empirical data based on the theoretical framework of both innovation and strategic pricing.

Chapter 6 summarizes the main findings and discusses its implications.
2 Methodology

This chapter describes and explains the chosen research methods in relation to the collected and worked up empirics. It then continues with describing the empirical area of investigation and ends with an overview of validity and reliability of the research.

2.1 Qualitative research methods

While quantity is about statistics or numbers, quality is about the characteristics of these statistics or numbers. The objective of qualitative research is to explain a certain phenomenon instead of seeking its frequency as in the quantitative research. In order to answer qualitative research questions e.g. explaining phenomenon, empirical research is required. There are several different methods in order to acquire empirical research (Widerberg, 2002). The two most common methods are observations and interviews. If the aim is to illuminate the phenomena by studying what goes on “in real life”, then observation is the best method. If the aim is to bring forward peoples understanding of the investigated phenomena, interviewing is the best way to proceed. In this study, observation was used but interviews were selected as main research method.

2.2 Choice of research method

This analysis is a result of the managements wish to investigate how prices are set within the companies and what consequences it has for the company’s financial results. A project group consisting of three consultants, one of whom was a pricing expert, was put together to perform the analysis. During the whole project focus has been on those employees who are in charge of setting prices, both transfer prices within the company, as well as customer prices. An interview guide was put together in consultation with the product owners (those who are in main responsibility of the products). This guide was then used as a guideline when interviewing employees in the different countries. The project group found it necessary to perform an empirical investigation to be able to form an opinion about the pricing occurrences within the organisation. Further, the group also wanted to understand how the current pricing
process was carried out. We found it important to interview all employees affecting the pricing process; both management and sales staff, in order to hear their own words. This would in turn make us able to find a conclusion based on experience from observations and investigations, which is a basic condition for empiricism. The empirical analysis follows a case-study research design (Yin, 2003)

2.3 Case study

2.3.1 The Scientific Benefit of Case Studies.

According to Shaughnessy and Zechmeister (1990), the scientific benefit of the case study method lies in its capability to find new ways for discoveries, and in being a breeding ground for insights (Berg, 2004). Another benefit is its proximity to real-life which was the main reason to use this particular design. Creswell (1998) points out that case study is appropriate when one aims at studying something limited by time and space with multiple sources of data. As a consultant it is important to quickly be able to get deep knowledge about the condition of the problem that will be analysed. Concerning the very limited time frame of this project, the case study design fitted very well to our needs. It also gave us the chance of obtaining both language and voice of the participants (Creswell, 2003). Further, the case study approach meant that the consultants were able to understand the particular problem in great depth, as well as getting rich information, by only analysing a few cases. As Patton (1987) argues, the case study helps to learn a great deal about how to improve a program by studying select dropouts, failures, or success.

When carrying out a case study, two important problems may arise (Berg, 2004). The first problem is that of creating objective results. A case study may involve too many subjective decisions made by the interviewer. Second, there is a discussion whether the research method really offers information that can be used in other cases as well, eg. if the result can be generalized. This is something that will be further discussed in the chapter about validity.

2.3.2 Case study design type

According to Yin (2004) and Tellis (1997), there are several different designs for case studies. In this analysis the design type used is called exploratory case study (Berg, 2004). The exploratory case study helps to plan for a larger and more comprehensive undertaking.
In this analysis, four different markets within the same company have been analysed. The different markets are treated separately as “cases”, why this project will be regarded as a multiple-case study (Yin, 2004). The primary reason for choosing this design is that it was judged to be the most accurate design for this analysis.

However, the cases will generate general answers for Global Processes to relate to. Since a case often has many things in common with other cases within the same category, the more similarities within the cases, the more reasonable it will be to generalise. To judge similarities between different cases, I have showed the common details, so the reader can judge whether the results can be generalized.

2.3.3 Interpretation

Kvale (1984) mentions three different ways of interpretation. The first one consists of an interpretation process, where the researcher tries to understand/interpret the world of the person she analyses. This process can be seen as a dialogue, where the researcher and the respondent gradually change their understanding of each others worlds by correcting their preconceived notions and eliminating their biases. This way of interpreting is also called *hermeneutic circle* (Sjöström, 1994). Within the hermeneutics, the researchers own background and pre-understandings plays a critical role in his or hers interpretation (Ödman, 2007).

The second way of interpreting is called the “*common-sense*” interpretation (Kvale, 1994). This form for interpretation means that the interpreter “reads between the lines”, or interprets the unspoken (Kruuse, 2001). Finally, the *theoretical interpretation* is the interpretation of a certain theory used on the respondent.

In this thesis, focus has been on interpreting from a theoretical point of view to achieve a result as objective as possible. However, it is not possible to argue that the other ways of interpretation was totally excluded.

2.3.4 The Abductive Approach

There are three different methods that can be used for connecting theory and reality; the inductive approach, the deductive approach and the abductive approach (Patel and Davidsson, 2003). The inductive approach can also be called the discovering approach (Andersen, 2002). The inductive approach starts off in the empirics and leads us to general knowledge about the
theory. The deductive approach on the other hand, starts off with a specific theory in order to draw conclusions about occasional events. This research is based on an abductive approach. The abductive approach is a combination of the inductive and the deductive approach (Dubois and Gadde, 2002). During the collecting of empirical data such as interviews, general theory and scientific articles have successively formed an understanding of the research material. During this iterative research process, earlier theoretical and empirical data can be re-interpreted (Alvesson and Sköldberg, 1994).

2.3.5 Empirical area of investigation

Employees from four different market companies within Global Processes have been interviewed. These four markets have been selected exclusively by the management in GP without further explanations. The selected markets are named Market Company A, Market Company B, Market Company C and Market Company D. Further, the headquarter which also is known as the Business Unit (BU), are included in the research. Two specific products have been chosen, also exclusively by GP’s management, to constitute the base of our research. These two products, Alfa and Beta, were chosen primarily due to its simplistic and common traits, but also since they were the most frequently goods sold across the markets.

A graphic description of the organisation structure can be viewed in the appendix.

2.4 Data collection

2.4.1 Interviews

When performing interviews, Yin (1998) has identified five researcher skills that are important when conducting a good case study (Berg, 2004). These five skills are:

- An inquiring mind – meaning that the interviewer is curious and willing to ask questions not only during the interview but before and after as well. It also means that the interviewer asks challenging questions about what is happening and why.
- Ability to listen, observe and sense
- Adaptability and flexibility – this is particularly important to be able to handle new and unanticipated events and to be able to change strategy if necessary.
• Ability to understand the issues being studied in order to react correctly to the collected data.
• Being unbiased in the interpretation of the data.

To cope with the last skill, Yin suggests reporting preliminary findings to colleagues who may be able to put critical questions that would require further investigation. In this project there has been high focus on obtaining all five points throughout the research.

2.4.2 Respondents

Between five to nine respondents from each market company was interviewed. The project group where free to choose which one to be interviewed. However, time limits forced us to interview those employees who where available at the moment.

2.4.3 Semi-structured interviews

A semi-structured interview can be defined as a conversation partly consisting of structured subjects and questions (Denscombe, 2000). In this project this kind of interview is highly relevant since it made it possible for us to develop a structured interview guide which we used as a starting point. The employees interviewed in this research where asked similar questions, based on a questionnaire put together by the project members in consultation with the marketing director. The questionnaire was constructed to minimize risk of misunderstanding. According to Bryman (2002) it is important to think of as if being in the position of the respondent and always try to capture the information concerning what is of interest in the study. However, after the first round of interviews, which took place on Market A, the interview guide was reflected on, in order to control whether the questions answered to the projects objectives. Many interesting answers came from the discussions which arose between the interview questions. Being aware of this, the interview guide evolved gradually as the interviews proceeded, highlighting new questions that had been brought up in earlier interviews. This resulted in that the first and the last interview rounds were slightly different, the last one including more discussions and answers than the first one.

2.4.4 Documenting interviews

All interviews where written down by one or two interviewers in order to make sure that no answers would be forgotten after the interviews. In some cases, especially when more than
one respondent were interviewed at the same time, a recorder was used to secure higher validation.

2.4.5 Other types of data
The respondents where asked to show documents that could validate their statements. Typical documents asked for were lists of margin contribution, sales statistics and tools helping the selling process.

2.5 Quality of research
There are different ways to judge quality in a case study. Maxwell (1998) argues that the different test strategies should not only verify the conclusions but also test the probability in order to analyse any existing threats to the conclusion.

2.5.1 Validity
Case research findings are sometimes argued not to be statistically generalizable (Yin, 2003; Cavaye, 1996). However, this is not the intention with this study. Instead, focus has been on describing a situation and from there generalize the result to similar cases.
When measuring validity, the measurement can be divided into measuring inner validity (or logic validity) and construct validity (Svenning, 2003). The inner validity deals with the project itself and the direct connection between theory and empirics, while the construct validity deals with how the whole project (including theory and empirics) is rooted in a larger scale.
In order to grasp reality and gain validity, many factors need to work out well. Observations, interviews and the openness of the respondents should build an overall picture that is consistent (Svenning, 2003). By using a case study approach with semi-structured interviews the interviewees in this project has been able to talk freely about their opinions in between the interview questions. The first interviews in Market A were, however, less semi-structured than the ones on the other markets. The reason is that the interviewer at this point was more objective and didn’t have any preconceived notions that could form the interview questions. Therefore, validity may differ between the results from the investigated markets.
2.5.2 Reliability

A qualitative research is generally not as reliable as a quantitative one. Qualitative investigations are more exemplifying than generalizing according to Svenning (2003). This means that the demand for being generalizable is higher when it comes to quantitative research than of qualitative research. In order to raise the reliability in this project, the project group has focused on using very clear definitions as well as comprehensible questions when interviewing. This resulted in straight answers from the respondents. All respondents were able to read and think about the questions a few days before the interview took place. Those respondents who carefully read through the questions came up with more straight answers than those who did not consider thinking about the questions.

2.5.3 Methodology reflections

During most interviews, a recorder was used which may have affected some of the respondents in their answers. However, recording the interviews has made it possible to listen to the interviews several times to make sure a thorough review of the answers. Due to time limits, it has not been possible to review the survey results together with the respondents, which may have help to resolve any misunderstandings. Since the empirics gathered in this study are both valid and relevant for the purpose of this analysis, I believe that the requirements of validity are fulfilled. However, there may be shortcomings in regards to the reliability due to respondent’s different answers regarding information on pricing and innovation strategy, which concerns the degree of reliability in a future identical analysis. Nevertheless, I believe that the conclusions emerged in this study remains, since indications received during the work has been so legible that they are not assumed to be influence by respondents’ possible lack of reliability.

In this research employees have been the voice of the customer of Global Processes and their perception of customers’ price sensitivity. It would be interesting to interview customers as well
3 Theoretical frameworks

This chapter examines and clarifies the theories chosen for this thesis. Further, both positive and negative aspects of the theories are discussed.

3.1 Innovation as a strategic resource

An innovation is often seen as a strategic advantage which can help its owner earn money and set industry standards. These advantages are for example, first-mover advantages (Teece, 1986), entry-barriers (Reitzig, 2004) and superior network positions (Kogut, 2000) to mention a few. It becomes more and more important to develop competitive resources, and innovation as a strategic resource is an area where many organizations are argued to be underdeveloped. In the next section, I will present a more detailed explanation of innovations and how it can affect the company both positively and negatively.

3.1.1 The definition of innovation

For many people innovation is positively loaded term. It stands for something new and exiting and most customers are willing to pay a premium price to get their hands on it first. But what many people don’t know is that the company behind the innovation faces large challenges and risks in the developing process. Developing an innovation usually means investing a lot of money while facing great insecurity of whether the innovation will be successful or not. It is therefore of great importance that the innovating company captures full value of their innovation, meaning squeezing as much profit out of it as possible before competitors do. To use a definition sufficiently broad to cover most traditional definitions of the term “innovation”, it can be argued that an innovation is defined as “a new or different solution to a new or existing problem or need” (Davis and Devinney, 1997). However, it does not mean that innovation has to be a technical term. As Drucker (1985) points out, “innovation may be a social or economic term as well.” Hence, “innovation” can be defined as changing the yield of resources or in demand terms rather than in supply terms, that is, changing the value and satisfaction obtained from resources by the consumer. Another great researcher of innovation studies is Schumpeter (1934). He defines an innovation in five different ways:

1) the introduction of a new good
2) the introduction of a new method of production
3) the opening of a new market
4) the conquest of a new source of supply, or
5) the carrying out of a new organisation of industry

In contrast to Drucker’s definition, Schumpeter argues that it is too simplistic to define innovation as demand driven, since consumers may not know that there is a need to be satisfied, or that the new need can be fulfilled in a new way that are presented by a producer. Moreover, an innovation is often defined as either a product innovation or a process innovation (Davis and Devinney, 1997). However, the complexity of its nature sometimes makes it difficult to draw a fine line between the definitions.

3.1.2 Innovation opportunities

Drucker (1985) mentions four sources that give rise to innovation opportunities. These sources are

- The unexpected – for example unexpected success or failure, or an unexpected outside event.
- The incongruity – between actual reality and reality as I “ought to be”
- Innovation based on process need
- Changes in industry structure or market structure that catch everyone unaware

However, there are also sources stemming from outside the company, for example changes in demographics, changes in perception and new knowledge, both scientific and non-scientific (Drucker, 1985).

Next to the opportunities of innovation, different drivers push companies to innovate in order to stay competitive. Baker (2002) points out different drivers of innovation. These are financial pressures to decrease cost, shorter product cycles, stricter regulation and rising customer expectations regarding service and quality to mention a few. Although cost reduction has been a major driver of innovation, companies increasingly feel they must promote their image which has become a major driver of environmental innovations. A good image can help increase both customer loyalty and a company’s growth strategy.
3.1.3 Different types of innovation

Innovations can come in various forms and shapes but also in various degrees of novelty. The classic distinction is between three major types of innovation, product, process/service and business concept, but current scholars now distinguish levels of innovation (incremental to radical and sustaining versus discontinuous), no longer restricting the term to break through innovations changing the world (Baker, 2002). A *product innovation* can by definition be described as new if it “combines old attributes in a new way” (Davis and Devinney, 1997). This phenomenon is called product differentiation. However, a product innovation can also be defined as bringing new attributes that were previously available. This implies a fundamental redefinition of the product and is called a substantive innovation.

Whereas product innovation focus on the constituents and the composition of the product, *process innovation* focus on a new or improved way to produce or provide the product (Davis and Devinney, 1997). A process innovation can be either large or small, and even the simplest one can lead to greater profitability from a sale of an identical product now produced at a lower cost.

The degree of novelty involved is another dimension of innovation. Most important, it is the perceived degree of novelty that counts (Tidd, Bessant and Pavitt, 1997). An *incremental innovation* means a minor improvement and constitutes most part of what is defined “an innovation”. Even though incremental innovations may not seem very exciting or dramatically, they are of high importance. Studies of incremental process development suggest that the cumulative gains in efficiency are often much greater over time than those which come from radical changes.

If incremental innovation means “doing what you do better”, a *radical innovation* means “new to the world”. The radical innovations aren’t very common and only consist of around 6-10% of those projects labelled innovation (Tidd et.al, 1997).

Because radically new innovations do not always have a significant impact, Christensen (1997) differentiates between *sustaining* and *discontinuous* innovations. While sustaining innovations improve the performance of established products or services, discontinuous innovations bring very different products or services to market, that typically undermine established products and services in the particular market. As an example of discontinuous innovations, Christensen mentions the computer industry. For every generation of computers - from the big main frames to the laptop - there was a successful supply industry providing the drives. But when the generations changed, the suppliers went to the wall.
3.2 Capacity to innovate

The capacity to innovate is seen by an increasing number of scholars and practitioners as the new competitive competency of organisations (Baker; 2002) Instead of being something that just happens, most researchers argue that organisations can be designed and managed in ways that are conducive to innovation (Kanter, 1998; Amabile, 1988; Jonash and Sommerlatte, 1999; Hamel, 2000). Factors that either enable or hinder a company’s capacity to innovate has been identified at each of following levels; individual, project, organisation and environment (Baker, 2002). Nonaka and Takeuchi (1995) further point out, that organisational performance depends on how well the organisation manages internal knowledge. Leonard-Barton (1992) argues that a company’s core capabilities can also be core rigidities and thereby hinder innovation. This occurs when values, skills, managerial systems and technical systems that served the company well in the past are not be suitable for today. Still, these knowledge sets are deeply embedded and can create problems in new projects. This phenomenon is especially common within large established firms which suffer from high organizational bureaucracy and is also described as core incompetencies (Doughtery, 1995). Hamel (2002) suggests that, to develop innovation competency, a company must have both an internal and external organisational perspective. For example, partnerships can be a useful strategy to promote innovation. Cohen and Levinthal (1990) stress the importance of utilizing external technology, an ability they termed “absorptive capacity”. Knowledge transfer and absorption are maximized by processes that maximize social and technical interaction between the firms, such as sending employees at the other firm and repeated interactions (Dyer and Singh, 1998). Hamel (1996) also points out that strategic planning is often antithetical to promoting radically innovative business models and strategies and therefore has to be transformed into a more innovative friendly strategy. Further, strategic thinking must not only be encouraged but also sponsored and rewarded. When innovative ideas do not succeed, employees should not be sanctioned in any way. Hamel also suggest how to handle risk. Low-risk experimentation is key – it is important to invest in many ventures but to start out small Thomke, 2003). Most ventures will fail, but valuable knowledge can be obtained from each. Finally, Hamel advocates a culture and structure that promotes innovation. Senior executives should spend time on searching for opportunities outside the boundaries of their company. Dominant mental models regarding business mission, market scope, relevant products and target customers should be deconstructed. Innovation opportunities should be
opened up to all employees and engage customers and other stakeholders to develop new approaches to generating new ideas (Baker, 2002).

3.3 Profiting from innovation

Existing theories about innovation are continuously arguing about whether it is more profitable to be an innovator or an imitator. Teece (1986) mentions different implications for profitability of technological innovation. In what he call \textit{tight appropriability regimes}, where the innovating company has a solid patent, it can make sure that it will translate the innovation into market value. It will not matter if the company doesn’t possess all necessary endowments of up-coming costs, since a strong patent will give time and space for these developments. Similarly, it will not matter if the design isn’t perfect in the beginning since a company with a tight appropriability regime will afford to work on details. However, even though companies strive for tight appropriability, the truth is that this is seldom occurring in reality. On the contrary, innovators must often rely on business strategy to keep the hands of the imitators away from the innovation. But even if there is a so called “tight appropriability regime”, the innovating company must be able to assess what price to sell the innovation for. Marn et al (2004) points out six elements of what is called “new product pricing”. \textit{First}, it is important to assess and quantify the benefits being delivered, in order to understand the full value to customers. \textit{Second}, a definition must be made of the potential market at the product’s level of benefits. \textit{Third}, a price floor or “walk-away position” must be determined. Here, the cost-plus method can be an effective aid. Although the cost-plus method has many drawbacks as I will discuss later on, it is an effective method when needing to find out the absolute lowest economically viable price level. \textit{Fourth}, a release price must be settled. A release price is the price you want the market to associate with that product. \textit{Fifth}, the company should be able to predict competitors’ response. Hence, competitors may start a price war if the release price is to low, since this is the only parameter they can compete on. Finally, the company must be able to clearly demonstrate the benefits of the innovation to make sceptical customer understand the value.

Having a tight appropriability regime and the right price on the innovation, Teece (1986) further points out that firms which control important complementary assets are clearly advantageously positioned relative their competitors. Factors like know-how, service and complementary technologies are important to capture the full value of an innovation.
3.3.1 First-mover advantages

Davis and Devinney (1997) argue that there are two possible gains to a strategy based on innovation. First, they argue that there is an ability to identify the structure of the market and current competitors with barriers to entry or expansion. Second, it is possible to get supernormal profits due to intrinsic cost and pricing advantages or due to limited competition that may exist as the market increases. However, as noted above, pricing of new products can be quite complex (Marn et al, 2004). For radical innovations for example, there is no convenient market reference for guidance. For incremental innovations there may be an internal strategic conflict of whether to maximize margin or to make a rapid share growth. Lieberman and Montgomery (1988) add another implication for profitability of technological innovation which is that of scarce assets. By pre-empting its rival in the acquisition of scarce assets, an innovator may be able to gain advantage by controlling assets that already exist. These assets may be either physical resources or “space”, like geographic space or shelf-space. They also point out that a first-mover advantage may rise from buyer switching costs. If there are high switching costs, late entrants must be able to attract customer away from the first-mover, which will involve further expenses. Hence, many new products require an additional investment by the customer. This investment does not necessarily have to consist of pure money, but can consist of learning when and how to use the product effectively as well. Sometimes the investment is so extensive that the customer doesn’t want to switch to a competitors product since it would require too much new investment in both money and time of learning (Davis and Devinney, 1997).

Another first-mover advantage is that the innovator can shape the preferences of the consumers. Early entrants play a significant role in defining how it “should be”. Later entrants are then forced to define themselves around this norm which has become the “psychological standard” of the product.

Network effects are another major advantage that may not be as obvious as the other advantages (Davis and Devinney, 1997). Choices made by a customer may spill over and begin to influence choices made by other customers. Especially, late adopters may be affected by the knowledge of what is the leading product, even though it wouldn’t have been their primary choice. A good example of this is computer standards. Computer operating systems sometimes mimic old and unusable commands simply because they are known by so many customers. For example, would QWERTY (the compilation of the typewriter and computer keys) have been chosen again if the typewriter was invented today?
3.3.2 How to capture innovation premium

Jonash and Sommerlatte (1999) mention two fundamental principles that are important when creating a successful innovative environment within the company. First, managers of the company must drive innovation across the entire organisation to create value. This includes creating an environment for high-speed learning and network building to be able to align the skills of employees with a particular project. It is also essential that employees are able to learn and influence the organisation since innovation shouldn’t occur in isolation. Second, a company must leverage technology and competency to drive sustainable innovation and capture competitive advantage. This means creating technology and competency platforms consisting of a blend of skills, competencies and state-of-the-art technologies, which can be used for improvements for growth or performance.

Another discussion close to that of capturing innovation premium is the discussion of open innovation (Chesbrough, 2003), which is gaining momentum in the research field. The central argument is that organisations must open up their innovation processes, which entails allowing for both external inflow of innovation to occur as well as enabling active outflow of non-relevant innovation spill-overs through external commercialization (Chesbrough, 2003; 2006). The key concern of the concept is to create and capture value as companies treat R&D as an open system.

According to the consulting firm Arthur D. Little, providing valuable new products and services are critical to achieve high level of customer satisfaction. Regardless of the technique being used, innovation in any form translates into greater customer satisfaction and a favourable image for the innovative company in the market place. Furthermore, innovation leadership often translates into customer loyalty, brand equity, superior price premiums and margins, and a dominant market share (See picture below).
The central argument in this chapter is straightforward. Innovation enables an opportunity to improve a company’s competitive position. However, it should be noted that there are arguments to the dark side of innovation as well.

During the 1980s, American corporations lost billions of dollars when their innovation efforts failed (Jensen, 1993). According to Steven and Bruley (1997) there is evidence that it takes around 3,000 ideas to create one single commercial success. In his book “The innovators dilemma”, Christensen (1997) notes that even companies that have been successful innovators over a long period of time can, and do, fail. The dilemma refers to the problem of rational business practises focusing on the most promising markets and listening to one’s customers. This can blind a company to discontinuous innovations that may transform the market in a way that progressively displaces the incumbents. For example, the emerging or transforming market is incompatible with the incumbent’s business requirements regarding size of projects, price, profit levels, facility characteristics, staff skills (Baker, 2002)

The arguments in the earlier chapter imply many advantages being a first mover. But benefits of a first-mover may be counterbalanced by different disadvantages. For example, there is the free-ride effect, where competitors take advantage of the innovator in several ways (Lieberman and Montgomery, 1988; Aaker and Day, 1986; Golder and Tellis; 1993;
Schnaars, 1994). Free-riders are not able to copy the innovator for a period of time due to patent protection, but shorten the durability of the innovators profit.

Another disadvantage is that of insecurity and risk. The innovator has to face a certain degree of risk when entering into a new market with a new product. Incumbent inertia is a third disadvantage which may have root causes in a lock-in to a specific set of fixed assets, or the firm may be reluctant to cannibalize on existing products, or the company may have become slow and inflexible organisationally (Lieberman and Montgomery, 1988). To avoid incumbent inertia, managers need to guard against complacency and arrogance while constantly giving attention to shifts in technology and customer needs.

Farell and Saloner (1986), argues that a good is often more valuable to a user, the more others use compatible goods. As a result, innovation is inhibited. Hence, if an installed base exists and transition to a new standard must be gradual, early adopters bear a disproportionate share of transient incompatibility costs.

Instead of being an innovator, Markides and Geroski (2004) suggest that the big, established companies should leave the task of innovation to the small start-up firms that have both skills and the entrepreneurial attitude that is necessary to in order to succeed. The established firm should instead be working with consolidating young markets into a big mass market. They compare the approach to that of a book publisher, who identifies a couple of potential authors and sign them up to deliver a book. Working this way means that the process of innovation can be done outside the bureaucracy of the firm and the innovators (the small firms) get financial help to launch and market their products. However, if there are a lot of tacit and “sticky” information, it may become expensive and difficult to transfer this knowledge to outside companies (Aurora, Fosfuri and Gambardella, 2001; von Hippel, 1994). Another option is to buy small innovative firms. Pharmaceutical giants continue to do this, particularly in biotech (The Economist Newspaper, 2004).

Below, a table is made to clarify some of the advantages and drawback of innovation according to different researchers.
<table>
<thead>
<tr>
<th>Advantages</th>
<th>Drawbacks</th>
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<tbody>
<tr>
<td>Jonash &amp; Sommerlatte – &quot;The more innovation the more value capturing&quot;</td>
<td>Christensen – The innovators dilemma - &quot;even companies that have been successful innovators over a long period of time can, and do, fail&quot;</td>
</tr>
<tr>
<td>Davis &amp; Devinney – “supernormal profits, switching costs”</td>
<td>Steven &amp; Bruley - “it takes around 3,000 ideas to create one single commercial success.”</td>
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<tr>
<td>Chesbrough – “open innovation, spill over effects”</td>
<td>Lieberman &amp; Montgomery – “free ride effects, incumbent inertia”</td>
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<tr>
<td>Teece – “first mover advantages”</td>
<td>Markides &amp; Geroski - “leave the task of innovation to the small start-up firms”</td>
</tr>
<tr>
<td>Kogut – “Superior network positions”</td>
<td>Teece – “Innovation only advantageously in combination with proper appropriability regimes”</td>
</tr>
<tr>
<td>Reitzig – “Create entry barriers for competition”</td>
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<tr>
<td>Lieberman &amp; Montgomery – “Scarce assets”</td>
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Table 3.1
3.4 Pricing as a strategic resource

Pricing as a strategic resource has got extremely little attention from researchers, although the word “price” probably is one of the most commonly used terms within the business industry today. The number of empirical studies investigating pricing as an organisational capability is severely limited. Many articles outlines more general ideas, but few articles present a theoretical structure.

In this analysis, Marn et al.’s (2004) “The Price Advantage” is used as a guideline throughout the thesis. In their book, it is pointed out that “price” can be viewed differently by different people. An economist would argue that price is interesting from an overall industry level, looking at the intersecting supply and demand curves. The marketer views price from the eyes of the customer, and focus on whether charging a price premium or worrying about what discount an inferior product requires. Hence, this view can also be referred to as a “value-based view”. The third view is that of a sales person, whose concern is to get the price right when negotiating with his/her customer. The economist, the marketer and the seller all operate at different levels within the company. To understand the word “price” one must use an integrated approach when addressing price issues within the company.

Marn et al. (2004) refers to three different strategy levels for pricing within a company. These levels affect the company’s pricing strategy in the short, the medium and the long term. From a short term perspective, pricing at the transactional level is what influences the company’s success. Looking at the medium term, the market level is the influencing factor. Finally, the industry level is what affects the long term achievement of the company. These levels are interrelated and thus an integral part of the broad pricing dynamic. Further, it is crucial for managers to understand the connection between these three levels of pricing in order to manage a full pricing strategy in a long term perspective.

The model below is a graphic illustration of the theoretical model from which this study departures, and which includes the industry, market and transactional level. Next, the three strategy levels will be explained and defined.
3.4.1 The industry level

Pricing strategy at the industry level is the most general of price management (Marn et al, 2004). At this level, it is of great importance of knowing and predicting industry wide price levels as well as influencing them in a constructive way. Being unable to do this, a worst case scenario would be price wars or pointless pressure on industry prices. However, if the company is capable of managing industry wide price levels, chances for success are significantly more probable. Superior understanding of the industry’s microeconomics enhances the company’s capabilities of adjusting tactics ahead of the market. It will help the company to avoid long-term, fixed price deals just before an expected upturn, or add extra capacity before an increase in customer demand.

To be able to profit from price prediction, Marn et al (2004) highlights three areas that need to be constantly observed in order to spot shifts in industry price levels. The first is cost changes, that can appear due to shortage in raw material or new manufacturing approaches. The second area is supply changes, which can change when plants close or patents expires. Finally, the third area that needs to be observed is demand changes. Customer demand may change due to new complementary products or new regulations.

**Price leadership**

Price leadership refers to a situation where prices are established by a dominant firm, or a firm accepted by others as the leader, and which other firms in the industry adopt and follow (Khemani & Shapiro, 1993). At a high level, price leadership refers to sensible pricing strategy that considers customer price sensitivity and understand that competitors may follow a price move instead of undercut it (Marn et al, 2004). Price changes are often matched to the penny even when the products are differentiated, and it is common for a long time to elapse.
between price changes (Rotemberg & Saloner, 1990). Furthermore, price leadership also involves clear and consistent communication of the pricing strategy and the value it brings.

**The transparency challenge**

Marn et al mention different elements which a company must be able to influence to become a price leader. One of these elements is their *transparency in pricing*. To become a price leader, it is important to undertake pricing actions that are fully visible to both customers and competitors. Not being able to do this, company prices will easily get misinterpreted. This does not mean that a company must give access to all prices in detail, however. In companies were each order is unique and price depend on various features and assemblies, hypothetical standard models can be used instead to give customers a rough appreciation of costs.

Another very important aspect for a price leader to consider is that of having *transparent rationale*. If there is no logic behind the price changes, they are likely to be misinterpreted by customers and stakeholders and may lead to distrust. Finally, it is not enough to have full transparency of own prices if the company are unaware of competitors prices and price changes. Even the clearest pricing action can be missed out if nobody pays attention.

**The challenge of common motivation**

A price leader must be able to motivate its competitor to make price changes last. If there is a common motivation, for example profit growth, this will be easier to achieve (Marn et.al, 2004) Successful price leaders are able to put focus on price increase and profit growth instead of on market shares.

Another aspect of motivation is to understand that competing companies actually do act rationally and are likely to be driven by profit instead of market share. Companies aiming for price leadership too often fail to understand that competitors may increase their prices as well. When it comes to understanding customers’ willingness to pay, a successful price leader must be able to challenge their assumptions. Too often price elasticity is measured based on false assumptions and companies hesitate to increase prices due to fear of loosing market share (Nagle and Hogan, 2001).

**Creating resolve**

Since the result of price leadership actions seldom comes immediately for companies who are striving for price leadership, it is of high significance that the company has a strong organisation behind it which supports every decision (Marn et al, 2004). It must be possible to
pervade the whole company with a “price leadership spirit” in order to make employees act according to decisions made by management. This “pervasion” can be made through different approaches which are all equally important. These approaches are: strong internal controls, continual and consistent communication as well as active monitoring of competitive actions.

**Internal controls**

A company striving for price leadership must have full support from its employees. If employees act opposite to the organisational goals, large consequences can be expected. For example, if the company tries to maintain a price increase, it will be mistrusted by customers and competitors if a key account manager gives its customer large rebates in order to win the deals. To avoid this kind of situation, a proposed approach is to practise strong internal control to align employees’ actions with the strategy.

**Communication**

It is important that price leadership is communicated as a long term strategy and not as a one-time tactic. Managers have to make sure this message reaches employees at all levels within the organisation. All employees must be able to explain a detailed explanation of a price increase to customers, competitors and shareholders.

**Monitoring competitors**

Sometimes disruptive behaviour occurs when an industry tries to reach a better pricing conduct. It is therefore important that leaders continuously monitor the situation on the market and act correctly to maintain the price leadership strategy. For example, if a company gets its strongholds attacked by a competitor by offering discount, it would be appropriate to make an aggressive price promotion in that market. Another example is to promise customers always to match prices offered by competitors.

### 3.4.2 The market level

At the market level of price management, focus lies on a more general level than that of the transaction level. This level includes publicly communicating prices set relative competitors. More specifically, decisions at the market level include setting list prices, base prices or manufacturer’s suggested retail prices (Marn et al, 2004). The main objective is to position
each product at the best level to capture the best return for the value delivered. This means that managers must be able to handle the crucial trade-off between perceived value and perceived price. One should also have in mind that a price is more than just what the customer pays for a product or a service; it is a means for building relationships, supply quality and help creating long-term profitability for the company (Fisk, Grove and John, 2000; Lovelock, Vandermerve and Lewis, 1999).

**Value-based pricing**

The main challenge at this level is to understand how customers perceive the benefits of the product compared to those offered by competitors (Marn et al, 2004). The benefits of the product are also called “unique selling proposition” (USP) of the product and defines the uniqueness of the product or service (Andersen and Poufelft, 2006) Being able to understand customers’ perceptions, the company will be able to seek justifiable price premiums and reduce price sensitivity among segments. Examples of factors leading to less price sensitivity are according to Kotler and Keller (2006):

- The product is more distinctive
- Buyers are less aware of substitutes
- Buyers cannot easily compare the quality of substitutes
- The product is used in conjunction with assets previously bought
- The product is assumes to have more quality, prestige or exclusiveness.

To set prices according to customer’s price sensitivity is also often referred to as **value-based pricing** and is a term which lately has become commonly used within the field of business strategy. As Monroe (2003) argues, companies should aim for setting the price equal to the perceived value for the customer rather than the economic value. The ambition is to focus on the customers and in accordance with the customers’ values, set the price. Most customers wish for a fair price but also mean that the company should be able to reach a reasonable profitability (Kahneman, Knetsch and Thaler, 1986). Furthermore, it is important to prioritize those customers whose value exceed the cost for having a relationship with them (Rust, Zahorik & Kenningham, 1996).
Setting prices according to customer’s price sensitivity is also called “price discrimination”. The advantage with price discrimination is that customer segments with low price sensitivity must pay a higher price compared to those who are highly sensitive.

One main issue with value-based pricing is the managers’ mental barrier since the method is often regarded as difficult to accomplish in practice (Nagle & Hogan, 2002). Richards, Reynolds and Hammerstein (2005) have further shown that senior management doesn’t see pricing as their responsibility and they often leave this important decision to mid-level technicians who often don’t possess the understanding of pricing. To achieve value-based pricing, marketing managers, sales managers and financial managers must work together. Marketing managers are those who are able to anticipate the value for customers while sales managers must be able to communicate the value to customers. Finally, financial managers must focus on incremental profitability and understand how costs change with changes in sales in order to develop appropriate incentives for marketing and sales to achieve their objectives (Nagle & Hogan, 2002). Further, one should have in mind that the value perceived by customers may differ between segments and thus, different prices in different segments can be applied (Mohr 2001).

So why then is value-based pricing so difficult to apply in practice? Marn et al (2004) outlines a couple of explanations that help us understand why value-based pricing hasn’t become more widely applied in practice. They argue that companies have had little incentive in the past to develop advanced pricing skills due to less tough competitive climate. Second, they claim that pricing is thought as of being unmanageable, and set by customer or unreasonable competitors. Third, the fact that there are no or poor data tools within the companies to support pricing decisions makes it difficult to practice value-based pricing. The problematic of uncovering and detecting pricing errors is mentioned as a fourth reason. This has to do with the difficulty of proving that a customer was willing to pay more when the business deal is completed. As a fifth example they mention that there are low incentives for frontline price setters to charge an additional percent in price. Instead, they could be tempted to sell on volume or other parameters than price. Finally, and maybe the most important reason to why value-based pricing has been so difficult to apply in practice, is the little engagement and involvement by management in pricing issues.

However, there are two other important aspects which I would like to add to the reasons above. First, it has been almost impossible to find a clear and useful template for companies
to follow or relate to. This of course relates to the first argument, that there has been little incentive in the past to develop advanced pricing skills. The pricing area has not been deeply explored in the past and as a result there are no superior guides within value-based pricing. Secondly, a change from cost-plus pricing to value-based pricing requires large effort which may deter companies from jumping on to a new strategy.

The two reasons above form a circle since the implementation of one of the steps makes it easier to carry out the other and the other way around.

**Measuring value**

Business-to-business customers are more sensitive to the quality of the product, less price sensitive and normally hold more information on the product than business-to-consumers customers. These facts normally make the price setting process more complex for industrial products (Forman and Lancioni, 2002). To be able to sell on value, management must be able to understand both *perceived value* as well as *perceived price*. Being able to accurately measure these factors, a proper equation can be made which is perceived value minus perceived price. This equation shows that either increasing perceived value or decrease perceived price, (or doing both) will add value in the mind of the customer (Marn et al, 2004). However, the fundamental problem in this equation is to justify what the perceived value or benefit is since many benefits are subjective and defy measurement. Adding to the difficulties is the fact that even when metrics are clear, there still can be gaps between perception and reality.

It is important to point out that, even if the product in question has greater value for the customers than that of the competitors, the value must be communicated to the customers in a convincing way, in order to charge a higher price than competitors (Kotler & Keller, 2006).

To understand value, Marn et al (2004) suggest that the company draws a value map. The value map is a tool that can help managers to gain insight into how to manage the price/benefit tradeoffs that comprise value in the market.

In a stable market where market shares are not shifting between competitors; and the perceived benefits and costs are measured accurately, the competitors will all align along the *value equivalence line* (VEL) (See figure 3.3 Company β). However, if shares are changing across competitors, some companies will be positioned off the VEL, for example in a *value-disadvantaged position* where it is loosing its share (Company α), or in a value-advantaged position where it is gaining share (Company γ). Accordingly, a company would always strive
for staying at the right side of the VEL where the perceived benefits are higher than the perceived price.

Figure 3.3

**Cost-plus – The easy way out?**

To most companies, cost plus pricing is the easiest method of pricing their goods or services. Hence, it is also the most commonly used approach historically (Nagle & Hogan, 2002; Noble and Gruca, 1999).

The benefit of this strategy is that the company will always cover its production costs (Forsman and Hunt, 2004). The downside is that it doesn’t give companies room to set a price which will reflect their special capabilities or expertise which makes them superior in the market (Lantz, 2000). The method does not take competitors’ prices into account either.

When the entire market uses the cost-plus method the prices are usually more “fair” to buyers and sellers, and the prices will be more similar between different competitors (Kotler, Wong, Saunders and Armstrong, 2005; Cannon and Morgan 1991).

However, the method has more fundamental problems. It is impossible to determine a product’s unit cost before determining its price since unit costs change with volume. The unit cost changes because a large portion of costs are fixed and must therefore be allocated to determine full unit cost. However, since these allocations depend on volume which changes in price, unit cost is moving. Cost-plus pricers end up assuming that they can set prices without affecting volume, which means a failure to account for the effects of price on volume and of volume on costs. It results in managers making pricing decisions that undermine profit. For
example, increasing price to cover higher fixed cost will reduce sales further and make unit cost rise. Price increases will therefore usually reduce profits instead. This phenomenon is known as “the death spiral” in which fixed costs are spread over continuously diminishing unit volume as prices rise even higher (Nagle & Hogan, 2002).

**Knowing your competitors**

Knowing your competitors, or possessing *competitor intelligence*, is crucial for companies who wants to predict competitors price points, product benefits and over all cost structure (Hallberg, 2008). There are four important reasons which can explain why information about competitors is important (Nagle & Hogan, 2002). First, knowing competing products’ price and benefits is essential when evaluating a customer’s willingness-to-pay. Second, the effectiveness of a certain pricing policy is dependent on the competitors pricing policy. Third, information about competitors’ price can be useful in negotiations with customers, diminishing the risk of being intentionally misled by customers trying to bring down prices. Finally, information about competitors is useful when predicting competitive responses to a certain pricing policy or price change.

Competitor intelligence is particularly important since companies seldom are alone about selling a certain product or service. Instead, the modern company is fighting against tough competition from global players. Hence, the competitive environment is very dynamic and competitors are constantly changing their supply and customers their demands. Marn et al (2004) emphasizes the importance of managing the company’s value position proactively in order to get optimal returns from new products as well as be ready to capitalize on economic swings and market cycles. If a competitor changes a products position, by either price cut or feature improvement, other players need to react. They can choose between staying on the VEL, or moving off it, for example into value-advantaged territory.

**Taking account of price elasticity**

When analysing market pricing, price elasticity becomes relevant, especially when changes in prices and benefits are considered (Perloff, 2004). A simple explanation of price elasticity is that elasticity shows how volume changes when price increases or decreases (Marn et al, 2004). However, price elasticity can be far more complex than this straightforward explanation. For example, price elasticity can show the indifferent zone, meaning the width of the zone where purchasing behaviour are unaffected in spite of changes in price or benefits. It
can also vary by segment, meaning that different customers are diversely sensitive. Furthermore, it is important to be aware of variance over time. Customers can quickly change their elasticity when their needs change.

\[
E_d = \frac{\Delta Q_d}{Q_d} \cdot \frac{P}{\Delta P_d}
\]

where \( Q \) is the quantity demanded and \( P \) is the price

\( E_d = 0 \), the demand is perfectly inelastic
\( E_d = \infty \), the demand is perfectly elastic
\( E_d = 1 \), the demand is unitary elastic
\( E_d (0; 1) \Rightarrow \) demand is relatively inelastic
\( E_d (1; +\infty) \Rightarrow \) demand is relatively elastic

(Source: Kotler & Keller – Marketing Management 2006)
3.4.3 The transactional level

In order to find and develop company specific advantages that can be used for lowering customer’s price sensitivity, managers must have a well-considered strategy that covers the transactional level where the company interacts directly with customers. As Dutta, Zbaracki and Bergen (2003) argue, pricing can be explained as a capability of the firm. By creating capabilities in their pricing process, the company will be able to capture value. This argument is in turn based on the resource-based view where the purpose is to develop or obtain valuable resources in order to gain a competitive edge (Barney, 1991).

At the transactional level, decisions about base price, discounts and other adjustments are made. The objective is to achieve the “best” price for each transaction at an almost granular level. At this level, price management can be very time-consuming and is in fact the most energy intensive level of pricing (Marn et al, 2004). At complex companies, thousands of price decisions can be made daily. Best practice at this level is to gain a superior understanding of each customer, meaning that companies must know the types of customers that are the best for them and forcefully seek their business. They must know which customers are low-performing and why, to be able to actively improve them. Furthermore, Mauri (2007) argues that information about the pricing process is an important factor to customers in order for them to decide whether the price is reasonable relative to the price of competitors.

Problems of incentives and control

The exercising of internal control within a company provides management with a reasonable assurance that the company will achieve its goals. In an age of empowerment, managers face a fundamental problem trying to exercise adequate control of their employees’ actions (Simons, 1995). Especially in complex companies, high level managers have to rely on their employees to capture opportunities and respond to the needs of the customer since managers may have no or little insight in each individual transaction. Managers tend to get information about average selling numbers but miss out on capturing the important opportunities in different transaction. The long distance between managers and employees may therefore result in moral hazard, which typically appears when the management for different reasons can’t control all activities at the lower levels of the company (Eisenhardt, 1989). Crucial for this kind of companies is to have a well working incentive system e.g. a Balanced Score Card (BSC), to make employees at the transactional level act in the interest of the company as a
whole. As agency theory implies, there may be conflict of interest when desires or goals of the principal and agent differ. Incentive approaches commonly emphasise total sales volumes instead of rewarding deal-by-deal excellence. As Brickely et al (2005) suggests, it is important that the incentive programme matches the strategic objectives of the company. If the company’s objective is to get higher margins out of their transactions, they must design an incentive programme that rewards their employees whenever this is achieved.

**Negotiation capabilities**

As mentioned above, communicating and negotiating with customers takes place on a daily basis within large companies at the transactional level. If an account manager is able to communicate the benefits of the product, the company is more likely to be successful than if not (Marn et al, 2004). Studies show that good bargaining and negotiating skills will vary between diverse companies (Brandenburger and Stuart, 1996).

Furthermore, customer’s reaction of the company’s pricing policy is dependent on the policy’s credibility. Hence, having a consistent pricing policy towards different customers will help to gain credibility and strength towards other parties in different negotiation situations (Hallberg, 2008). Further, the price must be presented to the customer in a way that seems reasonable or fair (Ng, 2008). For example, a certain price will be easier to accept if it is called a “discount”, than if it is called a “fee” (Kahneman & Tversky, 1979).

Nagle & Hogan (2002) give two advices regarding management of communication and negotiation. They argue that it is important to use a fixed pricing policy in order to avoid opportunistic customer behaviour where the customer tries to exaggerate its price sensitivity or disapprove the benefits of the products. They also emphasize the significance of showing the customer that the selling company truly understands the value of the product, making customers understand that the company is aware of the benefits of the product.

**The price waterfall problem**

When a customer buys groceries in a shop she normally end up paying what is on the price tag of the product. The process is quite simple. In “business-to-business” transactions this process can be far more complex. For example, a customer can be given order size discounts, competitive discounts and annual volume bonuses etc. When these transaction-specific off-invoice items are subtracted from the list price, what is left is the company’s remaining revenues called the pocket price. A serious problem arises when the organisation is unaware of revenue leaks like this and uses the list price against defined target prices. By becoming
aware of the factors that contribute to a price waterfall, companies can start controlling and managing them and thereby increase its earnings (Marn et al, 2004).

3.5 The (lack of) integration of innovation and strategic pricing

In the theoretical framework I have now explained and defined two important strategic weapons that companies can make use of in their struggle towards profitability. It is interesting that although innovations can be important aids to reach price premiums, the two streams of innovation and pricing as a strategic resource seem not yet to have been integrated in any sense making way, (Weick, 1995).
4 Empirical Findings

This chapter describes the collected empirical material that will serve as basis for the discussion in the following analysis. It begins describing the findings within the Business Unit and continues with the findings from each market company. A summary of the findings concludes the chapter.

4.1 The Business Unit

The Business Unit (BU) is located at Global Processes headquarter. This is also where the product owners are located. A product owner’s responsibility is to make sure that market companies are informed of the technical characteristics and functionality of the specific product. They function as a retailer who sells the products to each market company. The price they set is called a “transfer price” which refers to the price on assets transferred within an organization (Kotler and Keller, 2006).

The pricing process is quite complex with many steps of margin adding. First, the BU buys the product parts from the manufacturer. When the product is compiled they put on a margin and sell it on to one of the market companies. The margin on the transfer price is seldom revealed to the market companies. Further, there are no clear guidelines of how to determine a margin on a product. When asked how margins were determined, one product owner told that it was more or less based on a gut feeling (Product owner, Product Alfa, April 2008). None of the product owners mentioned “cost-plus” as a pricing method. However, during the research it became evident that this was the primary used method, in combination with the “gut-feeling”. We also found that transfer prices where negotiable. Hence, different market companies can negotiate the price which means that they end up paying different amounts for the same product. The transfer price on different goods was then exposed in a book together with the “world market price” (WMP). The WMP is supposed to work as a guideline for the market companies when setting prices to end customers. However, most market companies set their own prices based on own premises, arguing that the WMP are out of date being far too high to be competitive.

The BU displayed a surprising lack of cost transparency and profitability control. For example, costs where not divided into fixed and variable costs, which made it impossible to
calculate the marginal cost on an extra unit produced. As a result, no one really knew how much was earned on a certain product in a certain market. It took several weeks to find the right person that could answer the questions about cost. Product owners did not know the fixed and variable cost, nor did they know where it could be found.

Complaints were made towards the BU by the market companies for setting different prices on the same product depending on which purpose it would serve. Market companies who where using it for one customer segment could buy it cheaper than those market companies who would use it for another segment.

From the interviews with the account managers in the market companies, a strong divide between an isolated BU and the highly empowered disconnected market companies was found. Quotes like “our enemies in the BU” (Account Manager, April 2008) and “the BU see market companies as competitors as opposed to customers” (Account Manager, May 2008) were stated frequently. Good ideas that pop up in one market company where not or very seldom passed on by the Business Unit. Therefore, the “wheel” was often re-invented at different market companies which stole both time and effort that could have been used for more important activities.

4.2 Market Company A

4.2.1 Innovation characteristics

In order to generate the knowledge needed for discovering innovations that will attract customers, Market Company A suggested cooperating with Global Processes Equipment (GPE), the part of Global Processes which produces certain equipment, since “countries with more integrated sales with packaging generate better margins” (product manager, April, 2008). But top management had given order not to get involved with GPE. The reason was that GPE is known for their high margins, and since customers cannot separate Global Processes from GPE they believe Global Processes has large margins too and tries to squeeze the price even more.

Another finding was that account managers must sell a whole range of products and can’t know all benefits of all the products they sell. This meant that even when Global Processes products were better e.g. had better energy savings, customers were not always given that information and may therefore choose a product from a competitor.
When asking account managers and product owners about which factors, beyond lower prices, would enable them to capture higher margins, three main points were emphasized:

- First, sales people must have good knowledge of the products and good relations to the customer. Also they must know the customers’ installations thoroughly. Customers are willing to pay a little extra since the communication gets better and thereby safer.
- Second, the product must be unique and customers must feel/think that the product is better.
- Third, account managers must be able to perform more value based sales. They must become better to explain and sell customer value.

Without solid knowledge of the product and the need of the customer, it is difficult for account managers to contribute with knowledge that can be used for innovative purposes. Furthermore, it becomes evident during the interviews that the account managers only answer on customers’ requests, rather than work proactively and find new and different solutions to customers needs. This way of working may prevent possibilities for new product development.

4.2.2 Pricing characteristics

At Market Company A, there was great insecurity of where to put the price, since there were no benchmarks or guidelines to help account managers setting prices. As a consequence, account managers were using the cost-plus pricing method instead of value-based pricing. When trying to set price according to the value-based pricing model, it often ended up at random. Also, there were no different segments or other benchmarks to take in consideration; hence the pricing strategy was very similar across markets and customer.

Another finding was the claim made by account managers that customers poorly understand the value of the products and services, hence only focusing on price. Normally customers start bargaining on the price before even knowing what the price is. Only when the product characteristics are proven to be better than those of the competitors, price became less important.

When asking account managers about the walk-away position, which is the lowest limit for taking a deal, the answer is: “The word “walk-away” doesn’t exist in our world.” (Account
Manager, March 2008). Account managers claim they feel pressured by top management to get every deal they can which often result in very low margins. Account managers also claim that there are no clear guidelines for when to leave a potential business deal. Also, a common way of thinking is the "good enough" thinking, meaning that account managers too often settles with an “acceptable” margin, as opposed to always striving for maximal profits. When asking about the reasons for accepting low-margin deals, the most common answer where to avoid the loss of market share, meaning avoid letting the deal go to a competitor. Another influencing factor was to secure spare part sales and other after sales business. Aspects like maintaining old well-establish customer relationships and “behind in order received target where other reasons for accepting low margins.

Some account managers also emphasised the importance of strategic sales, for example blocking a new competitor from entering the market, or get visibility in a new area or segment. However, there is no clear definition of a “strategic sale”, nor does anyone know what a strategic sale is allowed to cost in terms of low margins. Account managers also point out the underestimation on risk-cost. In every project there is a specific amount of money that is dedicated to cover possible risk that may appear along the project. The risk cost is usually underestimated which means that Global Processes must pay more money than expected, decreasing the end margin.

Account managers also explain that they rather sell high volumes than with high margin. A good incentive for selling on margin is lacking. A balanced scorecard is used in order to measure account managers performance. Here, selling on volume is higher weighed (25%) than selling on margin (15%).

4.3 Market Company B

One of Global Processes main competitors has its home base in Market Company B’s home country. As a result Global Processes faces tough competition being a foreign company on the market.

4.3.1 Innovation characteristics

Just as in Market Company A, there is no cooperation with Global Processes Equipment, although they sometimes find it advantageous. Account managers explain that they must have better performance criteria on their products to help them clarify benefits of the product
to the customer and thereby be able to sell more or with higher margins. Additionally, they argue that the more unique the product, the easier it is to sell. Many products once had this uniqueness. Today however, competition has erased their advantages.

At Market Company B’s market, many of Global Processes products are comprehended to be the luxury versions compared to the products of their competitors. Without proper documentation on the specific benefits of the product, customers will choose a cheaper product offered by competitors.

The account managers at Market Company B where also asked about which factors, beyond lower prices, that would enable them to capture higher margins. Three main suggestions where given;

- Outstanding products. Account managers also emphasized the importance of innovations to reduce for example the running cost, which in turn can justify a higher price.
- Better documentation. The best way for account managers to win sales and get high margins were the ability to show customer black on white documentation on energy saving and product capability.
- Delivery time. If the delivery time can be shortened, customers are willing to pay a premium price to get their equipment up and running as soon as possible.

Regarding the last point, one of the account managers explained “We have managed to deliver a machine in 3 days to a very large customer with a margin of 28.%”

Another problem faced by the sales force which had an impact on the sales processes was the BU’s lack of routine to pass on important information they come across. If the BU was aware of a problem in one country, this information was not automatically passed on to other countries. This meant that market companies in different countries always had to “re-invent the wheel”, or discover the same problems since there was no premonition from the BU.

Most account managers agreed on the importance of innovations. Global Processes needs to bring something new on the market which will out conquer competition. Just as within Market Company A, account managers in Market Company B worked reactively on customers’ requests, instead of proactively.
A specific problem brought forward on Market Company B was lack of high quality products. Too many incidents have occurred where equipment has proved to have poor quality, which in turn have affected Global Processes image among customer. As a consequence, it became more and more difficult to argue for high prices.

4.3.2 Pricing characteristics

Regarding the pricing process, strong complaints were made at the BU for setting too high transfer prices, making it difficult to compete on Market Company B’s market. The BU was thought to conceal the margin level from the market company. The two margins, one on the transfer price from the BU, and one on the customer price in the market company, could end up in a very high margin totally, which made it difficult for the market company to stay competitive. Competitors were claimed only to have one margin which made it easier for them to keep prices low.

As opposed to Market Company A, Market Company B seemed to have clearer guidelines of where to set their walk-away margins. However, these margins tended to be very low in some cases (around 7-8 %). On the other hand there was great inconsistency when setting margins. Customer wondered how Global Processes suddenly could drop their prices drastically as soon as competition got tough.

The account managers at Market Company B also believed they had a fairly good idea of competitor prices. Furthermore, they tended to price differently between segments. When it came to pricing strategy, they started the negotiation based on the competitor’s price. The smaller the unique selling proposition (USP) was, the closer to competitor’s price they would start.

The fear of having to dismiss good employees due to lack of work, has resulted in decisions to take a low margin order just to keep them busy. The argument is that idle work force is expensive and may result in important employees with valuable know-how leaving the company.

4.4 Market Company C

One of the reasons why the Market Company C was chosen as research field, was that it was viewed as prominent within value-based pricing by the Business Unit. Market Company C is
a unit with great autonomy, very proud of “managing by its own” without much help from the BU. The account managers consist of people with very long experience within Global Processes. Unfortunately, the workforce are growing old and many of them will retire in a couple of years which means that know-how may get lost if no effort is done to prevent it.

4.4.1 Innovation characteristics

During the interviews, we found that, unlike Market Company A and Market Company B, Market Company C often made use of its contacts within Global Processes Equipment to reach possible new customers. They also made use of the existing customers to work as references for new customers. They claimed to have excellent references which helped them win new business deals.

Account managers explained that they compete on value, not on cost and additionally increasingly on environmental factors. Another selling criterion was the long duration and safety of the machines. Similar to the other countries, innovations e.g. outstanding products was the best way to out conquer competitors. A clear evidence of this was a specific model of one of the products called “the Extra”. The Extra was originally created in Market Company B but was never successful amongst account managers. Instead, one account manager brought the concept to Market Company C where it was very successful. The Extra made factories save up to 40% of energy reduction compared to the standard product, and were sold with a 25% margin compared to around 18% for the other. When account managers were able to show high energy savings to customer, the potential of reaching a high margin was good. But most of the time they were unable to show energy savings, since no tests and documentations have been done.

To the question on which are the best ways to capture higher margins, two approaches was emphasised as being very important.

- The need for being different. By different, account managers meant that they needed to have access to tools and products that could help them make a different approach to their customers, compared to their competitors.
- Reduced delivery-time
As in Market Company B, the account managers at Market Company C complained about the long lead-times. Short lead-time was especially vital for key-components. If the customer needed a product in 2 weeks and Global Processes can deliver – then they would be able to get a very high margin.

4.4.2 Pricing characteristics

The proud at Market Company C became evident in the pricing process. Here it was very important being consistent on price to customers. Margins do not change from time to time with the same customer, since this approach was believed to be the most professional in the long run. Furthermore, account managers are said not to be interested in customers who tries to play off Global Processes against a competitor to get a lower price. Hence, margins are never lowered to unknown or new customers accept when there was a unique opportunity to enter a customer of strategic importance. Then the margin could be low or even zero. The final price was a bit higher compared to competitors.

At Market Company C, no evidence of using value-based pricing to any extent was found, which was contradictory to what the BU informed of. In the table below, an example is given by one of the account managers on how they set prices.

<table>
<thead>
<tr>
<th>Current Practice on Cost Plus Approach – Example from Market Company C</th>
</tr>
</thead>
<tbody>
<tr>
<td>Product Alfa (Transfer price from Business Unit)</td>
</tr>
<tr>
<td>Transportation</td>
</tr>
<tr>
<td>Engineering hours   (10x€90)</td>
</tr>
<tr>
<td>Total landed cost</td>
</tr>
<tr>
<td>Quoted price to get 25% margin:</td>
</tr>
</tbody>
</table>

Table 4.1

As a complement to the example above, account managers typically gave the customer some kind of price adjustment. There were three possible options:
– The customer is very close e.g. very eager to buy, and know Global Processes is the best: low reduction: ability to keep 25% margin
– The customer is close and lets Global Processes know what the competing offer is: 20% margin
– The customer is closer to competitors than to Global Processes: Global Processes are ready to go down to 15% margin (especially if this gives Global Processes an opportunity to get a new customer)

The lacking incentive for selling on margin instead of volume was also a problem at Market Company C. Hence, volume was counted 20% and margin only 15 % on the balanced scorecard.

4.5 Market Company D

4.5.1 Innovation characteristics
In order to make a high margin, Market Company D emphasised some different approaches:

• Value adding factors like strong performance data of products. One of the most important factors was to have outstanding performance guarantees and be able to differentiate themselves from their competitors.
• Short delivery times. For spare parts they have been able to deliver within 2 hours, any time of the week.

To be able to meet requirements of the customer on a higher level, joint product development had shown to be another good approach. This was especially important in plants which were producing new types of material with specialized consistency. However, just as in the other market companies, there was a wish for working even more proactively together with customers.
Today, one of the largest problems was poor product quality which leads to customer claims and had a large negative impact on the margins.
4.5.2 Pricing characteristics

At Market Company D, a good relationship with the customer was of high importance. The Market Company therefore accepted high expenses to build a strong client relationship. Typical customer activities were golf and track car racing events. The Market Company also arranged training programs for their customers that include social events. The account managers had long tenure within the company which signals that “they are going to be here tomorrow as well”, denoting that Global Processes is to rely on.

The pricing process within Market Company D seemed to be the most sophisticated among the investigated markets. A matrix was used compiled by one product specialist and one person who was specialized on the specific customer at hand. The margin typically went up over time with one and the same customer and usually started around 15%.

The sales force had developed its own quotation/pricing computer system. To find the right starting price, one must type in different parameters, for example the steel price. The system then calculated a starting price based on pure cost. The price was then modified based on the value-based pricing method according to the account managers. However, no clear guidelines of how they determined the value to the customers where showed during the interviews.

The sales force commission was also based on the after sales revenue (e.g. spare parts). This meant that sales people were incentivized to drive down the price, in order to earn money later on. Another factor eroding the margins was the common belief that "it is always better to get the order than not to get it at all", which was claimed by one of the sales directors.

Account managers were incentivized by a bonus program on top of the commission (individual objectives). It highlighted certain accounts/sales, new sites, introducing and selling new technologies. Just as in the other market companies, the account managers explained they were incentivized to drive down cost/price, not to capture value.
Table 4.2 shows an overview of the empirical findings across the investigated market companies.

### Innovation characteristics

<table>
<thead>
<tr>
<th>Market Company</th>
<th>A</th>
<th>B</th>
<th>C</th>
<th>D</th>
</tr>
</thead>
<tbody>
<tr>
<td>Performance data on products</td>
<td>Poor</td>
<td>Poor</td>
<td>Strong</td>
<td>Strong</td>
</tr>
<tr>
<td>Cooperation w. GP Equipment</td>
<td>No</td>
<td>No</td>
<td>Yes</td>
<td>No</td>
</tr>
<tr>
<td>Proactive vs Reactive work</td>
<td>Reactive</td>
<td>Reactive</td>
<td>Reactive</td>
<td>Proactive</td>
</tr>
<tr>
<td>Knowledge of prod. characteristics</td>
<td>Poor</td>
<td>Poor</td>
<td>Poor</td>
<td>Good</td>
</tr>
</tbody>
</table>

| USPs across products | No | No | No | No |
| Knowledge management | Poor | Poor | Poor | Poor |

### Pricing characteristics

<table>
<thead>
<tr>
<th>Pricing strategy</th>
<th>No clear model to follow when setting prices</th>
<th>No clear model to follow when setting prices</th>
<th>Focus on consistency with customers</th>
<th>Matrix customer/products</th>
</tr>
</thead>
<tbody>
<tr>
<td>Clear walk-away position</td>
<td>No</td>
<td>Yes</td>
<td>No</td>
<td>No</td>
</tr>
<tr>
<td>Pricing method</td>
<td>Cost-plus</td>
<td>Cost-plus</td>
<td>Cost-plus</td>
<td>Cost-plus/Value-Based</td>
</tr>
<tr>
<td>Most frequent reasons to accept 0 margin</td>
<td>Avoid the loss of market share</td>
<td>To develop new business with new customer</td>
<td>Acquire new large customer to get visibility</td>
<td>Secure spare part sales/after sales business</td>
</tr>
<tr>
<td>Requirements for higher margin</td>
<td>Innovations that creates a more stable and cost-efficient solution;</td>
<td>Innovations that reduce operational cost/delivery time</td>
<td>Delivery time/Innovations</td>
<td>Outstanding performance guarantees/Delivery time</td>
</tr>
<tr>
<td>Selling incentive: Volume vs margin</td>
<td>Volume</td>
<td>Volume</td>
<td>Volume</td>
<td>Volume</td>
</tr>
</tbody>
</table>
4.6 Price elasticity on the different markets

In order to get an idea of the customer’s price sensitivity, account managers in all markets were asked to answer three questions regarding their apprehension of the customer’s price sensitivity on their market.

Account managers were first asked to define the highest and the lowest price point to which the product could be sold. Then they were asked to define how much of the current total volume they could sell if they only sold at the highest price point, which was defined as 25% margin. The same question was asked for the lowest price point (10%), as well for a price point which were just between the lowest and the highest price point (17.5%). The table below shows the results on their thoughts.

<table>
<thead>
<tr>
<th>Market Company</th>
<th>A</th>
<th>B</th>
<th>C</th>
<th>D</th>
</tr>
</thead>
<tbody>
<tr>
<td>What percentage of the current total volume would be kept at the highest price-point? %</td>
<td>25</td>
<td>25</td>
<td>30</td>
<td>50</td>
</tr>
<tr>
<td>What percentage of the current total volume would be kept at a price-point between best and worst case? %</td>
<td>60</td>
<td>100</td>
<td>70</td>
<td>65</td>
</tr>
<tr>
<td>How much more than the current volume would be achieved at the lowest price-point? %</td>
<td>10</td>
<td>25</td>
<td>17,5</td>
<td>10</td>
</tr>
</tbody>
</table>

Table 4.3

The results show extremely high price elasticity. The average price elasticity based on the survey was following:

- A: 7,5 linked to price increase, and 1,2 linked to price decrease
- B: 7,5 linked to price increase, and 3,0 linked to price decrease
- C: 7,0 linked to price increase, and 2,1 linked to price decrease
- D: 5,0 linked to price increase, and 1,2 linked to price decrease

This can be compared to the price elasticity from the automotive industry, which is 0,5-5 depending on brand equity and innovation leadership. The result of the account manager’s apprehension of the price-elasticity will be further analysed and discussed in the analysis.

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1 According to estimation made by Professor Sigvald Harryson
4.7 Empirical findings summary

The empirical findings show that both innovation and pricing characteristics has many similarities within the different market companies. The findings further show that both market companies and the business unit has many shortcomings and faces many challenges in order to profit from their existing strategy. It is evident that all market companies lack a consistent pricing strategy and have poor or no guidelines of how to set prices in regard to the value-based method. This goes hand in hand with the fact that the market companies are poorly equipped with knowledge about both customers and products, which is a requirement for value-based selling. The pricing method used instead is the cost-plus method. The market company closest to value-based method is Market Company D, which have developed their own matrix and computer system to find the right starting price. Also, they always use two people when determining a price, one product expert and one customer expert.

It could also be seen that walk-away positions are unclear, as well as the definition of a strategic sale as an excuse for allowing a low margin sale. As a result of these obscure directives, margin becomes inconsistent among customers. Moreover, proper sales incentives are lacking, making the account managers rather sell on volume rather than price. This, in turn, may be a result of the “must get the order” way of thinking which is claimed to be imposed by management.

The empirical findings also show a strong divide between the BU and the market companies, leading to an adverse atmosphere rather than strong cooperation and commitment.

A common trait among the investigated market companies is the need for selling unique products, showing a great need for both product and process innovations. Unique selling propositions are utterly important to get customers to focus on value as opposed to price i.e. making the customers less sensitive to price. Market Company C has been successful at this, having managed to deliver “the Extra”, which made them able to increase their margin.

Also, it is essential to be able to show good performance measures and energy savings so that customers can see what they are buying “black on white”.

Another unique selling proposition is the delivery time. Three out of four market companies claim delivery time to be essential for reaching higher margins. Customers are prepared to pay extra money if they get their products faster. However, the BU argues that delivery time is unimportant.
In the analysis below I will discuss the contributions of innovations to make Global Processes capture the full value of a new pricing effort. I will also explain why Global Processes existing pricing strategy is insufficient, and come with suggestions on how they can profit from a new pricing strategy together with innovations. The analysis of Global Processes innovation and pricing strategy is built upon Marn et al’s (2004) three distinct levels of price management, the transactional level, the market level and industry level.
5 Analysis

The analysis presents the main empirical results related to the key concept highlighted in the theoretical section. The main intention is to provide direct comparison between empirical results and existing literature. Pricing strategy and innovation opportunities at three different levels are discussed in relation to the theoretical model.

In this analysis, an extended version of Marn et al’s model on the three levels of price management is applied, in order to explain both innovation and price management within Global Processes (see figure 5.1).

To demonstrate how to capture the full value of innovation, the three levels of strategic pricing has been supplemented by distinct innovation objectives. The result is an extended model which helps to clarify the way of thinking and reasoning and will work as a guideline in the following analysis.

Figure 5.1

5.1 The industry level

The study of Global Processes current approach to pricing has indicated three resource-related problems: (A) lack of a clear (central) pricing organization, (B) lack of systems for product costing and market intelligence, (C) and lack of appropriate skills/knowledge among employees involved in the pricing process. In addition to, and partly as a result of, the
resource-related problems briefly outlined in the empirical section, the study indicates that Global Processes lacks a distinct pricing strategy apart from the very simple cost-plus profit reasoning observed in the studied markets. In the following analysis, I will make suggestions on how Global Processes can improve its capability to capture the value of innovation, starting with the industry level and then moving on to the market and the transactional level.

**Figure 5.2**

**Factors affecting the industry level**

At the industry level, the objective is to gain knowledge about and influence industry wide price levels to become a price leader in the long-term. Marn et al (2004) points out that a successful price leader are able to put focus on price increase and profit growth instead of on market shares. When interviewing account managers at the different market companies it was evident that they felt a pressure to sell, hence focusing on volume instead of price. Two comments from the Market Company A and D were: “We must get the deal no matter what” or, “It is always better to get the order than not to get it at all”. This indicates a clear desperation to get sales and may well be a result of how the Balanced Score Card is composted. The desperation may be a result of top management allowing low margins to keep employees busy rather than allowing them to leave due to lack of work. As Marn et al argues, a price leader mustn’t hesitate to increase prices due to fear of loosing market share, or in the case of Global Processes, keep prices and avoid lowering the margins. However, top management seems to signal the importance of selling no matter what and to any cost.

The desperation to get the orders also leads to a pricing inconsistency. One account manager explains: “Customer wonders why we have been getting 20% margin for years and then can
Marn et al argues that a company will be mistrusted by both customers and competitors if an account manager gives its customer large rebates in order to win the deals. The fact that there is a false perception by customers that Global Processes has high margins is also a dilemma. Customers are aware of the high margins of Global Processes Equipment and believe that Global Processes has large margins too. They simply can’t separate the two divisions from each other.

**Lacking knowledge management**

Another problem discovered is that the BU often neglects to pass on important information from which they have come across. If they get aware of a problem or something that can solve a problem in one country, this information is not automatically passed on to other market countries. For example, the Extra concept had reached great success at Market Company C, but the other market companies were not aware of it. According to Market Company C, the fault lies within the business unit, since nobody there were interested in spreading the word. A well-functioning system for passing on knowledge affects the possibilities for creating innovations, since management has the responsibility to pass on knowledge that can enhance creativity and encourage experimentation.

**Centralizing pricing organisation**

For Global Processes to get rid of the unstructured way of setting prices and become a price leader in the long-term, they must develop a centralized pricing organisation that secures ownership of pricing and margins at a senior organisational level. Additionally, the centralized pricing organisation must be able to monitor and evaluate current price/margin trends within the own company and in the industry as a whole. To make this possible, the centralized pricing organisation must have full access to market intelligence and costing systems. This information is a prerequisite to become a price leader.

**Define segments**

Another precondition is to have identified the most and the least attractive segments on the market. Focus must be on those areas where Global Processes can make money. In the most attractive segments, unique innovation advantages must be developed, or ideally, develop USPs for all products in all attractive segments. If this is achieved, Global Processes will be able to reach a top position towards competitors. Regarding the least attractive segments, they
should either exit them, or, as a minimum, reduce their service level and other expenses that today are offered to them “for free”.

**Collaborate more extensively and systematically with GP Equipment**

Further, Global Processes should exploit these easily accessible contacts they have with GP Equipment in order to make contact and gain knowledge about customers. As a minimum, systematic updates on and cross-invitations to individually planned client events is required. Ideally, Global Processes should proactively plan and run major joint client events to enhance the industry leadership position. Hence, combining customer intelligence to define seminar topics and target participants will be advantageous.

Additionally, Global Processes should make better use of Equipment’s high-level relationships to reach the strategic decision makers in target-customer organizations.

**Professionalize and harmonize workload management:**

Since low margins where accepted just to keep employees busy, a solution must be found to make these employees work anyway or to let them go. Ideally, the implementation of job-rotation practices across functions, between Business Unit and market companies, and across market companies will keep employees busy. As an alternative, other value-adding activities for employees should be traced, who are idle when sales volumes are low (so as to avoid that margins are squeezed just to get jobs to idle installation people.

5.1.1 **Innovation leadership**

A survey made 2004 on the same industry that Global Processes belongs to, showed that innovation in this industry is not as strong as the innovation occurring in other industries. The survey revealed that only 37% of the 800 respondents reported that they had launched product innovations during the past three years. As a positive consequence, 64% of these inventors managed to achieve higher margins on their innovative products in comparison with their regular product lines. Furthermore, the study found that 55% of the companies that developed innovative products did so by adapting, improving or modifying existing products, whereas only 36% developed completely new products. This means that it is not necessary for Global Processes to “reinvent the wheel”, but simply to make changes to the established way of doing things, which can result in a new product or new process.

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2 Statistics Canada; The Daily (Monday, August 15, 2005):
As could be interpreted from the empirical section, account managers are in great need of unique selling propositions for their products. Hence, having innovations may be very important to stand out among competitors and get higher margins on sales.

**Keeping track of trends**

It is important that Global Processes keep track of trends that can offer exciting opportunities for them and their customers. For example, develop equipment that can create healthier products that not only offer convenience, but also a sensory appeal. Other suggestions are equipment that can produce products containing more “natural” ingredients.

As a suggestion, Global Processes must become more proactive when working with customer to be able to find and catch new opportunities. *All four market companies say that they almost only work reactive today, meaning they only responds to customers requests.* Market Company D had a positive experience of working proactively leading to a higher margin when they did a joint product development together with a special customer which lead to a high margin.

Being able to spot trends and bring new innovations to the market makes it possible for Global Processes to shape customers preferences, thereby using innovation as a strategic resource. Later entrants are then forced to define themselves around this norm which has become the “psychological standard” of the product (Davis and Devinney, 1997).

**First or second on the market?**

Even though innovation can be seen as very risky and expensive, there is a lot to win for a company such as Global Processes. The so-called “free-ride effect” that Lieberman & Montgomery (1988) mentions, can be excluded if the company has a tight appropriability regime, such as strong patents. Moreover, switching costs within the industry are extremely high. Customer personnel are trained to manage specific installed machinery within the factory. If changing supplier, the personnel needs to get new education on the new machinery. Additionally, if changing supplier, the whole plant must be switched, since competitors’ machinery aren’t compatible with each other. According to Lieberman and Montgomery (1988) high switching costs is a good argument to focus on innovation to create high USPs. Due to high switching cost, Global Processes also has the advantage of reaching ahead of its competitors before the patent period ends.
The other disadvantage mentioned by Lieberman & Montgomery (1988) is that of insecurity and risk. However, Global Processes is a strong economic organisation and has the ability of facing possible risks.

The largest threat is probably that of incumbent inertia. So far, we have experienced that Global Processes is a rather slow and complex organisation. Communication between the divisions is poor and there seem to be internal competition and lack of cooperation and understanding. Liebermann and Montgomery (1988) mention incumbent inertia as one of the possible disadvantage of being a first-mover.

Markides and Geroski (2004) argue that large and established companies like Global Processes should leave the task of innovation to small start-up companies due to their flexibility and entrepreneurial attitude. However, if there are a lot of tacit and “sticky” information, it may become expensive to transfer this to outside companies (Aurora, Fosfuri and Gambardella, 2001).

**Poor innovation advantage**

A common denominator on the market companies found in the interviews was that the smaller the unique selling proposition (USP) is, the closer the negotiation is based on the competitor’s price. Hence, it is of high importance to have products that stand out among competitors. However, customers’ perception of product performances are poor due to lack of ability to visualize or demonstrate product performance as well as a lacking ability to offer performance guarantees. The Business Unit is responsible to produce and pass on this kind of knowledge about the products but seem to fail. But more important is the lack of innovations. Account managers all agree on that innovations has the largest effect on customer’s price-sensitivity. As soon as they can show a more effective product which can save them money in the end due to efficiency or energy saving, the easier it will be to demonstrate value and to get a high margin (Davis and Devinney, 1997). The “Extra” concept is a good example of this.

To increase its capacity to innovate, Global Processes should run systematic client events on strategic issues in order to better communicate the importance of industry leadership to customers, but also to be able to “get into the minds” of their clients. This should be done in cooperation with GP Equipment. Customer Intelligence, Consumer Intelligence and Technology Intelligence will support continuous identification and selection of central themes for the large-scale customer events. Such events would also build better networks (superior network position), and partnerships within as well as outside the boundaries of Global
Processes. The importance of the intra-corporate networking dimension cannot be stressed enough in this report. Rather, it deserves a focused dialogue with the Human Resource Director.

**Take central initiative to drive price and innovation leadership**

At the industry level, a centralized pricing organization that secures ownership of pricing and margins at a senior organizational level (Strategic Pricing Director and Pricing Council) must be realized. Further, integrated market intelligence and costing systems that allow responsible senior executives to monitor and evaluate current price/margin trends within the own company and in the industry as a whole is necessary. In general, having better information and being able to act on this information is a prerequisite to lead. Also, differentiation through innovation for more unique value propositions is essential to become a price leader in the long run. Finally, top management must create an environment which is conducive to innovation.

5.2 The market level

![Diagram](image)

**Figure 5.3**

**Factors affecting the market level**

Pricing at the market level or in the medium term has the objective to position each product at the best level to capture the best return for the value delivered. This means managers must be able to manage the crucial trade-off between perceived value and perceived price (Marn et al, 2004).
To be able to undertake value-based pricing, the company needs to have large insight in both customers and competitors’ minds. As seen in the market companies, value-based pricing is a method that is very often mentioned, but not applied. Marn et al (2004) argued that the main issue for undertaking a value-based pricing method is the managers’ mental barrier since value-based pricing is often seen as difficult to accomplish. This could be an explanation to why value-based pricing is often talked in favour of but never really implemented in the business. Everybody talks about value-based pricing, but no one can demonstrate any clear evidence on how value-based pricing is applied in practice.

As an example, we could see in the empirical section, Market Company C’s way of pricing its products. At first, the account managers said they always use value-based pricing, but when they were asked to demonstrate their pricing method they showed a typical example of the cost-plus method. It can be argued, that the main reason for not being able to apply the value-based method is lack of knowledge about both customer and competitors, but also a lack of understanding what value-based pricing really stands for.

In Market Company A, it was argued that there was a lacking understanding of the customer’s true needs. For example, quotations are developed too fast – without first understanding the customer’s true needs. The customers were also offered too sophisticated solutions, when they actually needed simple ones. This meant that money and time has to be spent on a new modified offer since the first one didn’t match customers need.

As mentioned above, account managers have weak understanding of product performance. One account manager say that “Sales people in the market companies don’t know all benefits of all the products. They must sell a whole range of products and can’t have the specific and detailed expertise that is needed in order to win a sale”. Having weak knowledge about the products, customers and competitors, it is no surprise that cost plus is the most common method used when setting prices.

Factors decreasing price-elasticity at the market level (Value Pricing)

So far, it has been evident that Global Processes must create a deeper understanding of the customer’s true needs. As a suggestion, the market companies must invest in an extensive customer research. To be able to implement value-based pricing strategy, systems for measuring delivered customer value across products and customers (customer-value files based on key value drivers aggregated to segment and product level) will be required.
Preferably, a full update on the customer segments to clarify where to simplify and sell on cost versus where to innovate and sell on differentiation

Further, the organizational structure and sales processes must be simplified and adapted to customer value information. Today, there is an astounding confusion of both pricing, costing and product performance.

It is also necessary to build up resources to perform systematic analysis of the incremental profitability effects of the chosen price structure, and the risk of price waterfall. To make the sales force able to understand value-based selling, sales organization training is a good way to develop skills on value-based pricing as well as a common understanding of the importance of sustaining margins. In turn, this must be supported by proper incentives/ Balanced Scorecard. Incentives must be implemented which have a genuine focus on actual margin – as opposed to volume.

Furthermore, a system to make market companies able to share customer and product insights across countries and businesses must be developed. For example, there could be more job rotation to increase joint know-how. Additionally, people from the Business Unit should visit the market companies to get better insight of the sales processes.

Regarding competitors, there seems to be little knowledge of their pricing strategies today. Preferably, Global Processes should develop a system to get better insight into competitors’ way of pricing, but also to get better knowledge of the performance of their products.

5.2.1 Capturing the premium of innovation

In order to enhance employees skills on pricing, trainings must be arranged to clearly communicate the importance of value-based pricing as opposed to ‘cost plus’ pricing. Further, the company must be able to demonstrate the benefits of their products and innovations to make skeptical customers understand value.

Capturing knowledge about customers, competitors and costs

At the market level, it is important that the company aiming for price leadership creates a system for measuring delivered customer value across products and customers as well as undertakes a full update on the segmentation to clarify where to simplify and sell on cost versus where to innovate and sell on differentiation. Further, the company needs to create
customer-value files based on key value drivers aggregated to segment and product level. Another important aspect is to simplify the organizational structure and make pricing process adapted to customer value information. It is also essential to build up resources to perform systematic analysis of the incremental profitability effects of the chosen price structure, and the risk of price leakage (price waterfall). Additionally, it must implement incentives with a genuine focus on actual margin – as opposed to, for example, margin dollars.

**Couple distinct innovation leadership with the development of clear performance data**

To be able to develop more unique selling propositions like the “Extra”, value drivers need to be gathered from lead-customers using products with a distinct innovation advantage such as the “Extra” option. The fact that this option can be convincingly linked to customer energy savings of 40% enables customers to enhance the sales price equivalent to more than one year’s energy saving. The average margin for a system with this option is 25%. This kind of innovation advantage is believed to capture yet more significant profit margins with proper degrees of training and customer fact-based value sheets.

### 5.2.2 Global Processes on the value equivalence line

With a well-functioning pricing and innovation strategy, Global Processes will be able to decrease its perceived price and increase its perceived benefits. Although the positions on the map are not exact measurements, it is most likely that Global Processes will move in the direction illustrated below.
5.3 The transactional level

Recalling from the theory, at the transactional level the objective is to achieve the “best” price for each transaction at an almost granular level. Price management at this level can be very time-consuming and is that level of pricing which is the most energy intensive (Marn et. al, 2004). In the empirical section we saw that the market companies in general lack necessary knowledge about the customer and the product in order to set the right price in each individual transaction. Market Company D lies ahead of the other market companies however, using a matrix consisting of one product expert and one customer expert who work together when setting the price.

Unclear pricing strategy

It can be argued that the overall pricing strategy is very unclear. An example of this is the fact that walk-away positions are flexible – as opposed to firmly defined. Also, both Market Company B and D let us know that transfer prices from the business unit are negotiable. Hence, it may be concluded, that the end transfer price is dependent upon the market companies negotiation capabilities, instead of from a thoroughly calculated price based on what is best for the company as a whole. Another example that demonstrates an unclear pricing strategy is pricing of strategic sales. Since there are no strict guidelines to define a
strategic sale, account managers seem to be getting away with down to 0 margins (for example in Market Company C) in some cases. This shows an example of moral hazard, which according to Eisenhardt (1989) typically appears, when management can’t control all activities at the lower levels of the company.

Another example of moral hazard is the fact that account managers justifies a margin with the argument that it is “good enough”, as opposed to always striving for a maximal profit. But this lacking moral must, however, not exclusively be blamed on the market companies. The poor incentive structure stems from the Balanced Score Card, which in turn is decided on by top management at the Business Unit. Since the Balanced Score Card focuses on volume instead of margin, account managers have no incentives to do other than sell as much as possible instead of focusing on the margin. Furthermore, account managers often feel pressured by top management that they “must get the deal”. If account managers don’t sell, key personnel with important know-how may leave the company for competitors due to lack of work.

As Hallberg (2008) points out, the customer’s reaction of the company’s pricing policy is dependent on the policy’s credibility. Since there are poor evidence of a consistent pricing policy, customers may apprehend Global Processes as having a weak negotiating capability, thus trying to lower margins further. An exception to this is Market Company C, which emphasises the importance of having a consistent pricing structure, to get credibility in the long run.

Nagle & Hogan (2002) emphasised the importance to be able to communicate the benefits of the product, in order to explain the value for the customer. All market companies argue that they need better performance valuation of their products to justify its prices. It is not always essential that the performance is better than that of competitors’ products, but account managers must be able to show that they know the product they are selling in order to gain credibility with customers.

Not only is it important that customers find the account managers at the market companies credible. It is just as important that account managers find the Business Unit credible. Transfer prices are negotiable, but far worse it the fact that a product can cost different depending on which purpose it will serve. Market companies who are using it for a certain segment can buy it cheaper than those who use it for another segment. The differences can be up to 15-20 %. If the BU, who is representing the headquarters and works closely with top
management, signals that inconsistent pricing strategy is allowed, the market companies will act in accordance to their behaviour.

All the factors above together show typical examples of what Marn et al define as “the waterfall problem”. It can be seen that there are many small “waterfalls” that together has a large impact on the final price. In addition, there are several factors that tear on the ”final” margin after the product is sold. An example of this is the claims processes in Market Company B. When a product fail just after being delivered by the business unit, the cost of repairing it should be laid on the business units budget. However, the business unit handles these claims very slowly. Therefore, the market companies often end up repairing the products locally, which is tearing on the market companies’ budgets instead of on the business unit. Another example which tears on the margins is the underestimation of project risk.

When comparing to the theoretical arguments above, it can be argued that Global Processes clearly suffers from an insufficient pricing strategy at the transactional level. Below, an analysis on how these insufficiencies can be translated into a pricing strategy that is sustainable and profitable for Global Processes will follow.

**How to decrease price-elasticity at the transactional level**

The transactional price has effect on the short-term success of the company. Today, prices are set with in accordance to the cost-plus pricing method. Rebates are given both to market companies and to customers there is no control of the “waterfall” problem or how much a specific product actually contributes to the company in terms of income. Further, the internal price structure is complex and needs to be clarified. Walk-away positions must be firmly defined – as opposed to free floating. Transfer prices must be fixed and basic data for calculating actual product cost must be easily accessible. Additionally, clear criteria must be applied to define when a sale is strategic.

To solve this problem, the suggested *Strategic Pricing Director*, should tightly control the pricing process and decide on why and when rebates are allowed for.

To make it possible for account managers to set prices in accordance with the value-based pricing method, they must have full access to knowledge about customers and products. As a minimum, integrated and IT-supporter interfaces for account managers to access customer value files and profitability information on order level must be set up.
Another way to enhance the transactional price is to implement new incentive structures that avoid excessive focus on volume. With the Balanced Score Card used today, it is impossible for account managers to focus on margin. The new Balanced Score Card must be thoroughly planned and develop by top management to align with the overall strategy of the company.

5.3.1 Communicating unique selling propositions

**Product innovation – “The Extra”**

At the transactional level, account managers must be attentive to each customer’s true needs. As we saw in earlier chapters, customers are very sensitive to both energy savings and delivery time. Account managers explained that they were able to get a higher margin if they could save energy or deliver machines faster.

As we could see in the empirical section, Market Company C was able to get a high margin when selling “the Extra”, a specific model that could spare up to 40% of energy savings for Global Processes customers. Global Processes was therefore able to get up to 25% margin instead of 18% for the ordinary model. “The Extra” is a good example of a product innovation, which has effect on the customers’ willingness to pay.

The account manager at Market Company C who has worked hard to promote “the Extra” told us that “Nobody at the Business Unit knows about it” (April 2008). Despite persistent pressures on the Business Unit to spread the word about “the Extra”, the reputation about the successful model has not reached outside Market Company C.

**Process innovation – Lead-times**

We found that shortened lead-time is a desire by all market companies and can result in increased margins. Developing this area can help Global Processes getting in an advantageously position compared to their competitors. Not only is it profitable due to the increased margin on the specific sale in question, but also from the after sales and spare part sales for many years ahead.

As we could see in the empirical section, delivery time can have enormous affect on the margin. A machine delivered in 3 days from Market Company B got a margin at 28% instead of the normal 10-15%. This is more than double margin only by doing what you do faster. Reduced delivery time is therefore an important strategy to focus on.

However, when discussing this dilemma with the Chief Financial Officer CFO at the Business Unit, the answer was: “It is not necessary to have shorter lead-times” (CFO, May, 2008). The
answer indicates low interest from top management to listen and adapt to customers need. This shows a gap in the cooperation between the Business Unit and the market companies and can be seen as an example which can explain the comment from an account manager at Market Company B who referred to the Business Unit as “our enemies”.

As a suggestion, the most popular machines could either be on stock, or another system could be developed which makes Global Processes able to deliver goods faster than competitors.

5.3.2 Global Processes Price Elasticity – possibly over-estimated by the interviewees?

As could be seen in the empirical section, price elasticity was estimated to be very high across all markets. The result of the survey can however, not be seen as true fact since the results are measured purely on opinions and beliefs, but can give an estimation of how account managers apprehend their customers’ behaviour. The result may be interpreted as a warning from the account managers, saying “do not increase our prices – then we will loose almost all our customers”. But the fear of loosing customers may not be legitimate.

The result can also be interpreted as a message saying that account managers feel that they don’t have enough unique selling propositions (USPs), which can help Global Processes to stand out among competition.
6 Findings and conclusions

In this concluding chapter findings and conclusions are presented with reference to the purpose of this research. Furthermore, a discussion of the effects of the result in practice is held. Suggestions for further investigation conclude the thesis.

The aim of this study has been to analyse how an incumbent company in a mature market can reduce price elasticity through innovation. The company analysed was Global Processes, a multinational company struggling to become more profitable. Specifically, two areas have been investigated to discover possibilities for becoming more profitable by decreasing customers price sensitivity. These two areas are innovation and pricing. *I found that in the case of Global Processes, innovations with unique selling propositions are essential to stand out among competition and reduce price elasticity among customers.* Respondents from all market companies agreed on the need for differentiating themselves towards competitors. I suggested that value-drivers need to be gathered from lead-customers to be able to develop more unique selling propositions.

Existing evidence on innovations within the company proves the importance of innovations for earning high margins or price premiums. With this in mind, top management must create an environment within the company which encourages innovations.

In this research, one existing product innovation and one great process innovation opportunity were found where Global Processes can meet its customer’s needs within two important areas; *reduced energy consumption and reduced delivery time*. Regarding reduced energy consumption, Global Processes has already developed “the Extra”, which can save the customers up to 40% energy. However, due to lacking knowledge management, the Extra concept has not been successfully transferred to all market companies across the world.

But it is not enough to come up with innovations. Hence, *innovations can be devastating for a company if the pricing capacity is insufficient due to the high expenses and risks that follow innovating companies.* Global Processes must be able to capture the full value of existing and future innovations, why it is a prerequisite that Global Processes improves its pricing skills.

We have seen that Global Processes lacks several important factors in order to become a price leader.
Suggestions were made on how to decrease price-elasticity on three different price levels or time horizons. The levels were the transactional level (short term), the market level (medium term) and the industry level (long term). As a result of the research, we suggested different measures in the short run involving employing a Strategic Pricing Director. Additionally, a new incentive structure that avoids excessive focus on volume must be implemented.

To enhance profitability in the medium term (market level), it was recommended that:

- Global Processes must implement systems for measuring delivered customer value across products and customers.
- Global Processes need to provide sales organisation training to develop skills on value-based pricing as well as a common understanding of the importance of sustaining margins.
- A system to make market companies able to share customer and product insights across countries and businesses needs to be developed. For example, there could be more job rotations to increase joint know-how.
- Finally, develop a system to get better insight into competitors’ way of pricing, but also to get better knowledge of the unique selling propositions of their products.

In the long run, it is suggested that

- Global Processes develops a centralized pricing organisation that secures ownership of pricing and margins at a senior organisational level. This centralized pricing organisation must have full access to market intelligence and costing systems, which is a prerequisite to become a price leader.
- Second, Global Processes must identify the most and the least attractive segments on the market. In the most attractive segments, USPs for all products must be developed.
- Third, Global Processes should exploit these easily accessible contacts they have with GP Equipment in order to make contact and gain knowledge about customers.
- Fourth, workload management must be professionalized and harmonized which means to find ways to keep idle people busy instead of lowering the margins just to make these employees work.
6.1 Conclusive comments & implications

The result of this study shows that Global Processes have possibilities to reduce price elasticity of customers to enhance margins and becoming more profitable. Further, it shows that innovation is a fundamental weapon to arm against competitors and make customers dependent, both in the short- and the long-run. But most important, this study shows that a company’s pricing capacity must be strong and well-defined in order to put the right prices on its products.

In the case of Global Processes, the fundamental strategy must be to innovate, since customers are only willing to pay more if the products and services are better than those of competitors. The result of this study can help encourage other companies to innovate, but also to review their pricing strategy. The lack of pricing consistency within the company should be seen as a warning to other companies, as well as a goldmine where companies can find many possibilities to enhance their skills within pricing and catch price premiums.

If companies start focusing more on innovation strategies, demands for more specialized and better educated employees will increase. Requirements for more educated people on innovation and pricing means that education within this two areas must improve in order to satisfy the need of knowledge of the labour market.

The financial advantages in this research can be counterbalanced by other advantages and disadvantages. New technological discoveries can influence other companies to innovate in order to become more profitable. Innovation is essential to develop our society and increase living standards. Reduced energy consumption is something that the world is striving for every day in order to save money and to protect the environment. However, there will always be a risk when machines take over peoples work tasks.

6.1.1 Suggestions for further investigation

This research has had a financial point of view, although it has not presented any specific numbers on how much the gain could be if Global Processes implements the strategy suggested above. Even though precise numbers would be difficult to get, an approximate sum would probably encourage other companies who are in the same position as Global Processes.
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The company structure of Global Processes

Business Unit
- Top management
- Product owners

Market Company A
- Account managers

Market Company B
- Account managers

Market Company C
- Account managers

Market Company D
- Account managers