the Entrepreneur's Survival Guide

How to Maximize Revenue *(How to value-price your products)*

This chapter addresses a valuable method of maximizing revenue through value pricing and focuses on how to price your products and services.

How do you currently price products? Do you review your competitors' prices? Do you "cost out" your solution, then add a mark-up? Do you talk to a few customers and ask what they would be willing to pay?

The first two methods, though essential in understanding your competitive positioning, don't give you a true understanding of how customers will value your product or service. And the third method can yield misleading results. Often, *lower* than what the market will really bear.

And when do you figure out the price? *Before* you develop a product, or afterwards?

Many people say that marketing is an art, not a science, and that you have to feel your way around the situation to determine the best price for your product or service. Typically, companies are so focused on the product that they'll develop it and release it to the market only to find out it's not selling. Perhaps it's too expensive. But maybe, it's price is so low ("To gain market share.") that it is viewed as too cheap, such that prospective customers question its quality.

None of these approaches will maximize your revenue. In fact, without performing the right pricing process before you even start developing your product or service, you may well be spending time and money you don't need to. Worse, your released product may cause you more cash-flow problems than it solves.

Before the process is outlined, there are some examples to share:

> [1] Initial price too low: By "talking with" several prospective customers, a client of mine had determined that the selling price needed to be $295 per year, for a recurring-fee product (*like* Turbo-Tax, only not). After several informal discussions over about three or four months, my client (while continuing to "talk with" prospects), raised his price to $695 per year, without serious pushback. Right before launch, I was able to help them implement the process described above. The "sweet spot" was $1495 per year. 115% over the last "good" price, and over 400% more than his starting price. There were a couple customers who would have paid $20,000 per year. But that would have limited my client's market to about 2%.
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> And some prospects considered anything under $1000 as too cheap, such that they would not buy it. This means that my client would have sold fewer products, at a lower price had he stuck with his gut, and those

of a few vocal prospects. Bottom line: He asked the wrong question: "“hat would you pay?" yields too-low a price. Every time.

[2] Licensing fee too low: Another client had developed a product and was talking with one of the twelve OEM house in the world - to license their product. No production was required on the part of my client. Only developing a licensing contract, then watching the money roll in. The discussions between my client one the one OEM producer had the price settling on $8 per unit that the OEM house produced & sold. The OEM doubled the licensing fee to their end user, and planned on selling the option represented by my client’s product.

I helped my client perform the pricing research - with the end-user. Not the OEM company. We found that the pricing sweet spot was $25, at list. This means that my client’s customer was going to leave $9 on the table. When presented with that information, my client negotiated an agreement with the OEM for a $12 licensing fee. My client’s effective net profit increased 50%, from $8 to $12. And, his customer also won. Subsequently, my client received an order for $250,000 worth of product licenses the first year. The additional revenue (and effectively their additional profit) was $83,333. The ROI on that pricing activity was over 10 to 1. And that is just for the *first* year.

[3] Price too high: A client had developed an idea, and asked that I join them in an interim executive role as CEO. The first order of business was to determine if there was a “there”, there. That is, what would the market bear, and could we afford to launch into this market? Investment capital would be required, so we would need to make a case that we did our homework, and *knew* we could build a company.

The system was fairly complex, and had hardware, software and sensors to be developed. Through “manufacturing engineering”, we determined that an installed solution that could save customers up to $200,000 a year would cost about $50,000, which meant we needed to sell it for about $70,000 to build a profitable, growing company.

When we performed the pricing research, we uncovered the true value prospective customers would place on it. Although one customer said he would pay more then $200,000 for our solution, the sweet spot for pricing was $6,500. Clearly, the market didn’t value it, even though it would save serious money. Instead of sticking with an eventually-losing enterprise, we folded operations. It would have been unethical and immoral to try to raise any capital knowing this. And it would have been a terribly frustrating process - to try to sell to 5% of the market, and only (try to) build a $10 million a year company instead of the $100 - $200 million a year company we thought we could.

[4] Product re-defined: Another client of mine had developed a product with 18 features. The short version of this story is that - through pricing research - we found that 6 of those features were not valued at all, while an additional 3 features would *double the price*. (We performed pricing research with the 18-feature product,

then updated the description, deleting reference to the 6 low-requirement features while adding the 3 most-mentioned features.)

Through this process, my client learned that he should have performed the pricing research before he ever wrote one line of code. He would have then concentrated on the most-wanted 15 features. He would have save himself time and money, and would have had a product worth twice as much.

There are plenty of other examples, most of which point to the fact that people tend to undervalue their products. Or worse, miss out on a unique opportunity to learn what else the market would value even more. Before developing the product or service.

The process described below is designed to help you determine your product's *value from your prospective customers'* perspective *before* you even start your design.

1) First, determine your product's features, functions and performance. Figure out what *you* think its benefits would be for customers. Then write up a *brief* description of this product.

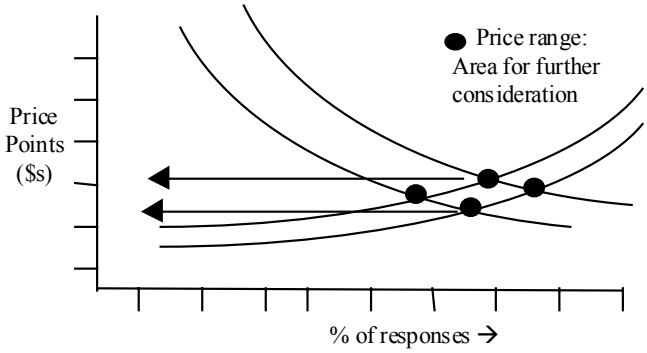
2) With your product description in hand, choose five to ten potential customers in your market. With each of them, explain that you are doing market research and will need no more than four or five minutes of their time (and keep it to that.). After reading the product description ask them these five questions, *in this order*: [1] At what price would you consider this product expensive? [2] At what price would you consider this product *in*expensive? [3] At what price would you consider this product *too* expensive, such that you would not buy it? [4] At what price would you consider this product too cheap, so that you would question its quality? [5] What features would you add to increase the product's value to you?

3) Now, plot out the data points from the four pricing questions in Step 3) so that the four curves have the largest gap at one end and converge at the other. Look at where the four lines cross. The graph should look something like the figure, below.

4) Now determine if the prices named by these potential customers are anywhere near the range you thought. If not, you have *lots* of work to do to determine your potential customers' needs. Then look at the answers to the fifth question to see if there are features you could add to your product to increase its value. Refine your product description to reflect this.

5) If you need to, repeat this several times. Each time refine the product description until the price points that customers mention are high enough to yield your target margins. If they are consistently lower, then rethink your entire product or service.

6) Once you are sure customers will pay what you feel the product is worth, formalize your market research and do Steps 2) and 3) with enough potential customers to "smooth out" the curves.



Congratulations. You have just defined how the market perceives the value of your product. You now have a clear roadmap on how to price your product and maximize your revenue. Give it a try – you may be surprised by the results.

Author's Biography

Mark Paul has over thirty years of executive level leadership experience - including 11 years at Global 500 companies (Ford and Northrop Corporations, where he built a 250-person business unit in two years) and over 22 years of business leadership consulting and interim executive work as Managing Partner at Synergy Consulting Group – an interim executive / business development consultancy. Synergy Consulting (www.synergy-usa.com) helps companies attract more customers, increasing their revenue, profitability and company value. Mark has run companies (start-ups through public), raised capital and built and served on boards of directors and advisors for several companies.

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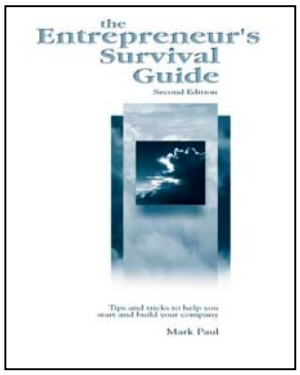

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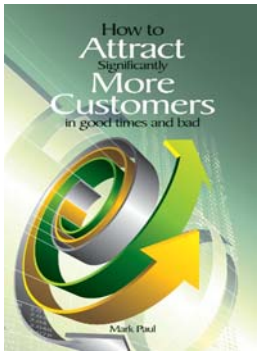

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