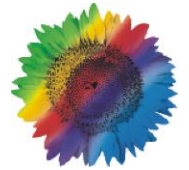


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HERE THERE BE DRAGONS

Steering Your Pricing Program to the Right Destination



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Executive Summary

For many of the centuries that ocean travel was the basis of the world's commerce, ships operated half blind. The navigation instruments available to them could give them their location on a north-south axis (latitude), but were unable to clearly pinpoint east-west position (longitude).

Many corporations are managing pricing programs like ship navigation of yesteryear. They are navigating half blind, trying to steer the ship without one of the necessary navigation axes. Strategy consultants are often "pricing sirens," enticing many enterprises onto the rocks with promises of great returns on pricing strategy investments. They fail to mention that successfully steering to the desired destination requires the right transaction level infrastructure.

But there be dragons on the route. Pricing initiatives can be complicated by a pricing strategy which proves extremely difficult to implement. In our experience the most common elements that hinder strategy implementation are:

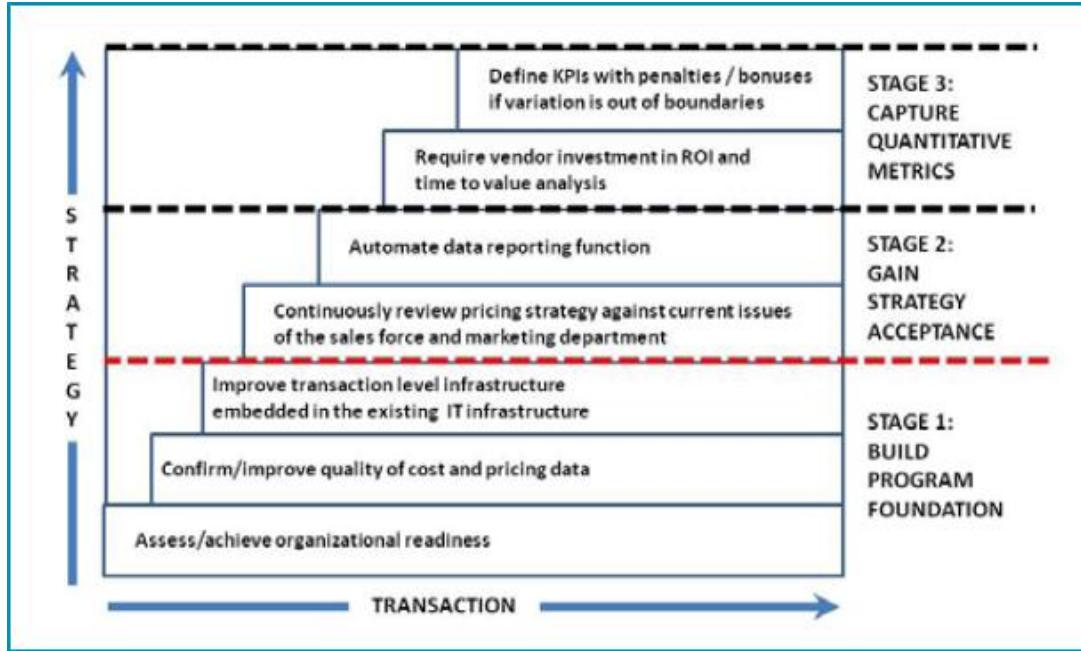
- Limited or no organisational readiness for pricing improvements.
- Lack of strategy acceptance across the sales force or strategy overruled by discounts.

- Difficulties in quantitatively measuring the return on investment and time to value.

We have identified leading practices to address each of these "dragons" that will provide positive business benefits.

Either on the advice of an outside consultant or because of a transactional "blind spot" among decision makers, many enterprises skip all or part of the foundation building stage, favouring investment in the other two, more strategic stages. And like a ship navigating only with accurate latitude measurements, they do not reach their destination.

In order to achieve the desired results and return from a pricing improvement initiative, foundation building is critical. Though this stage is almost completely transaction-based, it is a prerequisite for the second and third stages. If built effectively, the pricing function's foundation "seeds" the success of the other two (more strategic) leading practices:



- Confirming and/or achieving organisational readiness should be conducted in a way that facilitates strategy acceptance.
- Ensuring good data quality ensures that automated reporting will deliver accurate and actionable information to decision makers.
- Work on the IT infrastructure will require selection of a third party software vendor who will be heavily engaged in and impacted by capturing quantitative metrics, and this should be kept in mind both in selection and management of vendor during foundation building.

To get the full business benefit of a pricing improvement initiative, an organisation must start at the transactional axis and build up along the strategy axis. Like mariners of today and yesterday, navigating in this two-dimensional frame ensures success.

Here There Be Dragons

For many of the centuries that ocean travel was the basis of the world's commerce, ships operated half blind. The navigation instruments available to them could give them their location on a north-south axis (latitude), but were unable to clearly pinpoint east-west position (longitude). The fortunes of companies and individual investors rose and fell according to the ability of a ship laden with merchandise to avoid ending up on the rocks due to longitude calculation errors. It wasn't until the late 18th century that sea captains could pinpoint ship location with an acceptable degree of accuracy, which greatly reduced the risk to seaborne entrepreneurial ventures.

Technology has made accurate navigation commonplace. Global positioning systems provide automated and continuous readouts of the location of a person, a vehicle, or a ship with extraordinary accuracy. Sailors from only a few decades ago would be amazed at our navigation capabilities with error margins measured in feet.

Research suggests that a company spends an average of \$4.3M on pricing initiatives¹. However, the return on the investment may not meet expectations because many corporations are managing pricing programs like the ocean navigators of yesteryear. They are proceeding half blind, focusing on the wrong axis for "positioning" a pricing program, and the result is a house of cards that can collapse easily from all kinds of outside forces.

Like a ship plotting its position and course, a company must think in terms of two axes when crafting a pricing improvement effort:

- The strategy axis, the overall direction of all pricing efforts in a company.
- The transaction axis, where pricing actually takes place.

The transaction axis is a company's "longitude." That is, it is the missing axis that can put a pricing program on the rocks, unable to reach the destination (return on investment, time to value, increased profits) that management seeks.

Transaction axis pricing is the key to success. It is the foundation that greatly influences the strategic strength of a program. Charting the "voyage" of a new pricing initiative must start at the transaction level in order to see the right ROI and time to value, and to get to the desired business destination.

¹ N. Tohamy, H. Keltz, Building a Bulletproof Business Case for Pricing Improvement Initiatives. Supply Chain Planning and Execution Report 2008. AMR Research, Inc, 2008.

The Siren Song of Strategy Consultants

When considering pricing initiatives, many companies succumb to the belief that time must be spent creating a complete strategy before any other activities take place. “Strategy First” is not the most effective approach to pricing changes in most companies, even though this is the most common approach. Starting with strategy works only in certain situations:

- The company must be ready for the strategy that has been designed.
- The stakeholders (e.g. the sales force) must be willing to incorporate the new processes and policies that the strategy calls for.
- Management must be able to measure the effectiveness of pricing initiatives and make adjustments as needed.

The fewer of these requirements that are in place, the more difficult strategy implementation will be and the less likely the pricing initiative will produce the desired results.

Another part of the siren song of strategy is the belief that outside assistance (and the associated expense) is needed. Consultants are engaged to collect and analyse data and then to develop a pricing strategy. They design a strategy navigation chart, wish the client best of luck with implementation, and submit their invoice for services rendered. Company management must take the wheel and steer the initiative as close as possible to the route provided by the consultants. Too often, they end up on the rocks with little or no return on the sizable investment made in strategy.

The “Transaction First” approach eliminates the need to call on costly strategic consultants and sets a pricing initiative up to achieve expected goals and ROI.

Transaction Level Pricing as the Missing Axis

Introduction of a new strategy into an unreceptive environment is at best a waste of company resources and at worst a serious setback to business growth.

A solid foundation must be in place before strategy execution can go forward. This foundation lies along the transaction axis. Taking time to create and validate a solid transactional foundation will save time and resources during implementation of strategic initiatives.

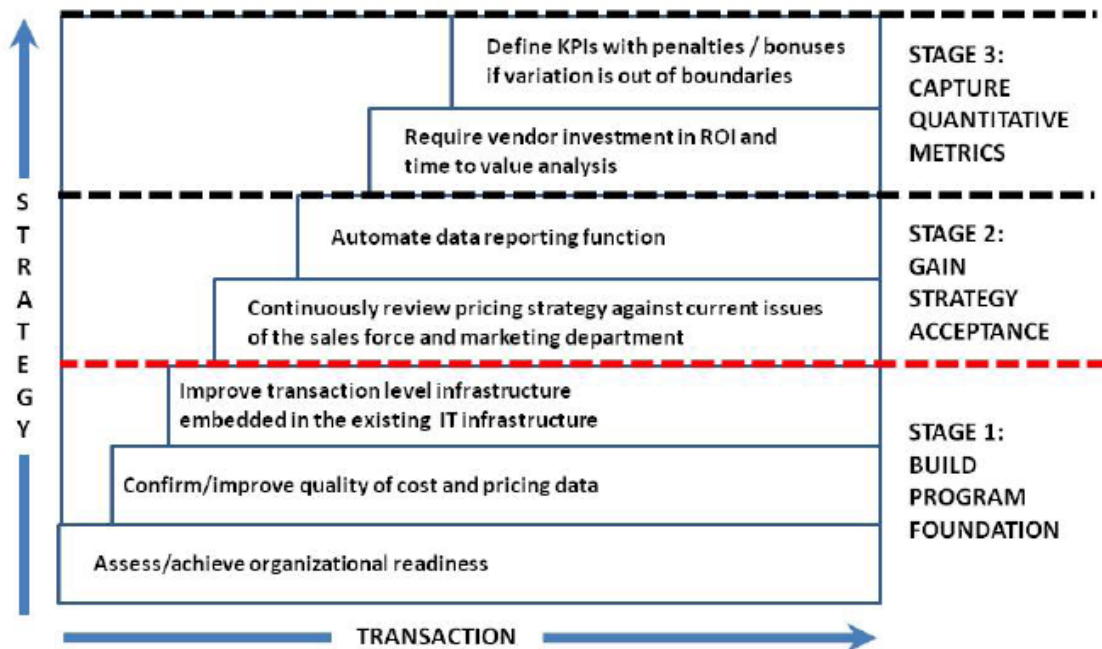
Focusing on the transaction axis prior to full strategy development allows in-house resources to capture and confirm the insight and capabilities needed to develop an effective strategy.

In our engagements with clients from a range of industries, we have found that three issues consistently impair the ability to put new pricing strategies into effect:

- The pricing organisation is not ready for the planned improvements. This lack of readiness could be cultural, technological, or both.
- The key stakeholders (usually the sales force) refuse to accept the changes made to pricing policies and processes.
- Quantitative measurements of pricing activities do not exist, which creates an “opaque” view of the effectiveness of policies and processes.

We work with clients to ensure that none of these issues impedes the progress of a pricing improvement initiative, which has allowed us to pinpoint critical path tactics—that is, leading practices.

Figure 1. Leading Practices for Transaction-Based Pricing



Leading Practices along the Transaction Axis

Stage 1: BUILD PROGRAM FOUNDATION

Either on the advice of an outside consultant or because of a transactional “blind spot” among decision makers, many enterprises skip all or part of the foundation building stage, favouring investment in the other two, more strategic stages. And like a ship navigating only with accurate latitude measurements, they do not reach their destination. The leading practices in this stage must all be implemented before any further stages are activated.

Leading Practice 1.1: Assess organisational readiness. The current state of the pricing organisation and processes must be characterized and evaluated in order to assess readiness for improvement initiatives. Evaluation of current state needs to include at least the following items:

- Cost data quality
- Pricing method (cost-based vs. value-based)

- Pricing processes
- Pricing organisation (i.e., who is responsible for pricing?)

If management finds that the current pricing organisation is not prepared for the planned improvements, this evaluation will help identify what changes are needed. These changes must be implemented before a pricing strategy can be executed.

Leading Practice 1.2: Confirm/improve pricing data quality. In order to move pricing improvements up the strategy axis, data quality must be high. Without accurate data, report automation and quantitative metric capture will be a “garbage in-garbage out” exercise of no use to decision makers. Said another way, data quality is a critical path factor for pricing program improvement.

Verification of data quality requires consideration of dimensions such as those listed in Figure 2².

² Leo L. Pipino, Yang W. Lee, and Richard Y. Wang, Data Quality Assessment, Communications of the ACM, April 2002, Vol. 45, No. 4.

Figure 2. Dimensions of Pricing Data

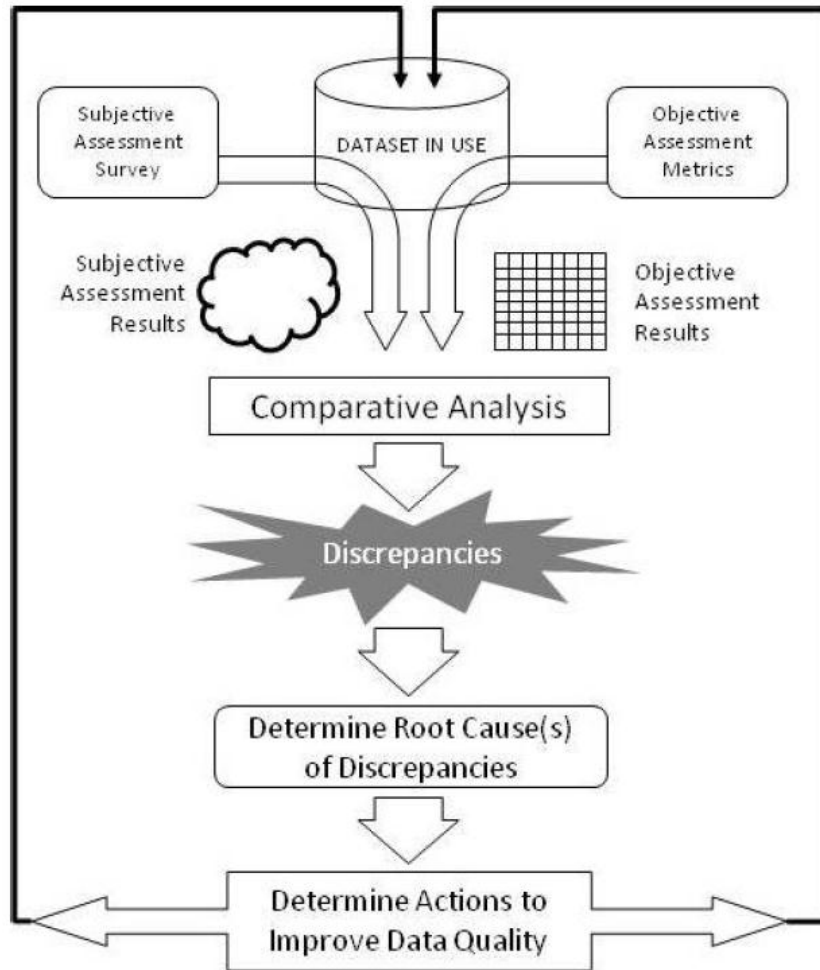
Dimensions	Definitions
Accessibility	The extent to which data is available, or easily and quickly retrievable.
Appropriate Amount of Data	The extent to which the volume of data is appropriate for the task at hand.
Believability	The extent to which data is regarded as true and credible.
Completeness	The extent to which data is not missing and is of sufficient breadth and depth for the task at hand.
Concise Representation	The extent to which data is compactly represented.
Ease of Manipulation	The extent to which data is easy to manipulate and apply to different tasks.
Free-of-Error	The extent to which data is correct and reliable.
Interpretability	The extent to which data is in appropriate languages, symbols, and units, and the definitions are clear.
Objectivity	The extent to which data is unbiased, unprejudiced, and impartial.
Relevance	The extent to which data is applicable and helpful for the task at hand.
Reputation	The extent to which data is highly regarded in terms of its source or content.
Security	The extent to which access to data is restricted appropriately to maintain its security.
Timeliness	The extent to which the data is sufficiently up-to-date for the task at hand.
Understandability	The extent to which data is easily comprehended.
Value-Added	The extent to which data is beneficial and provides advantages from its use.

From Leo L. Pipino, Yang W. Lee, and Richard Y. Wang, Data Quality Assessment, Communications of the ACM, April 2002. Vol. 45, No. 4.

Both subjective and objective assessments of data are required to determine quality. Subjective data assessment gauges the perceptions of data users, and reflects the needs, expectations, and experiences of collectors, custodians, and consumers of data. If one or more stakeholder groups consider data quality poor, their decisions, actions, and behavior will be influenced by this perception. Objective data assessment can be context-dependent, context-independent, or both.

The simplified workflow in Figure 3 outlines the steps in an analysis of data quality. This is an iterative process that should continue until both subjective and objective assessments are within acceptable quality parameters.

Figure 3. Data Quality Analysis –Simplified Workflow



Based on Leo L. Pipino, Yang W. Lee, and Richard Y. Wang, Data Quality Assessment, Communications of the ACM, April 2002. Vol. 45, No. 4.

Leading Practice I.3: Improve transaction level infrastructure embedded in the existing IT infrastructure. A successful pricing improvement strategy starts with excellent data. Our experience shows that investment in transaction level infrastructure results in continuous data availability, which allows continuous and up-to-date transaction data analysis. Cost data, for example, is essential and needs to be analysed before a strategic pricing discussion can be initiated. Analytical data views like the pricing waterfall are provided by a good transaction level infrastructure (see Figure 4).

With the right transaction level infrastructure, current data is automatically combined with historical transactions, resulting in accurate trend analysis that is essential for developing a pricing strategy. In

addition, underperforming and top performing business activities can be identified and can be addressed as part of strategy design.

Stage #2: GAIN STRATEGY ACCEPTANCE

While pricing strategy must be accepted across the whole organisation to be successful, the critical stakeholders are members of the sales team. Involving the team in strategy formulation is the best way to achieve acceptance and implementation. Including the sales organisation in the pricing strategy discussion has not just the advantage of compliance. It also provides the pricing manager with a more comprehensive picture of potential sales and the rate and magnitude of business growth.

Leading Practice #2.1: Continuously review current pricing strategy in partnership with the sales and marketing department. With a solid transaction level infrastructure your organisation will have good quality,

up-to-date transaction data at hand. Using a pricing process developed at Wipro (see Figure 5), this transaction data can be combined with the sales organisation's input and then analysed.

For example, Figure 4 charts data in the form of average pocket margin calculated over past transactions with multiple clients for each of eight products on the x-axis. The sales organisation provides the input for the y axis by grouping products according to their potential in the market based on sales reps experience. Three groups are available: 1) high growth; 2) slow/no growth; and 3) declining sales. Combining the sales view on the y-axis with the pricing view on the x-axis enables design for a growthfocused pricing strategy.

Figure 4. Simplified Pricing Waterfall

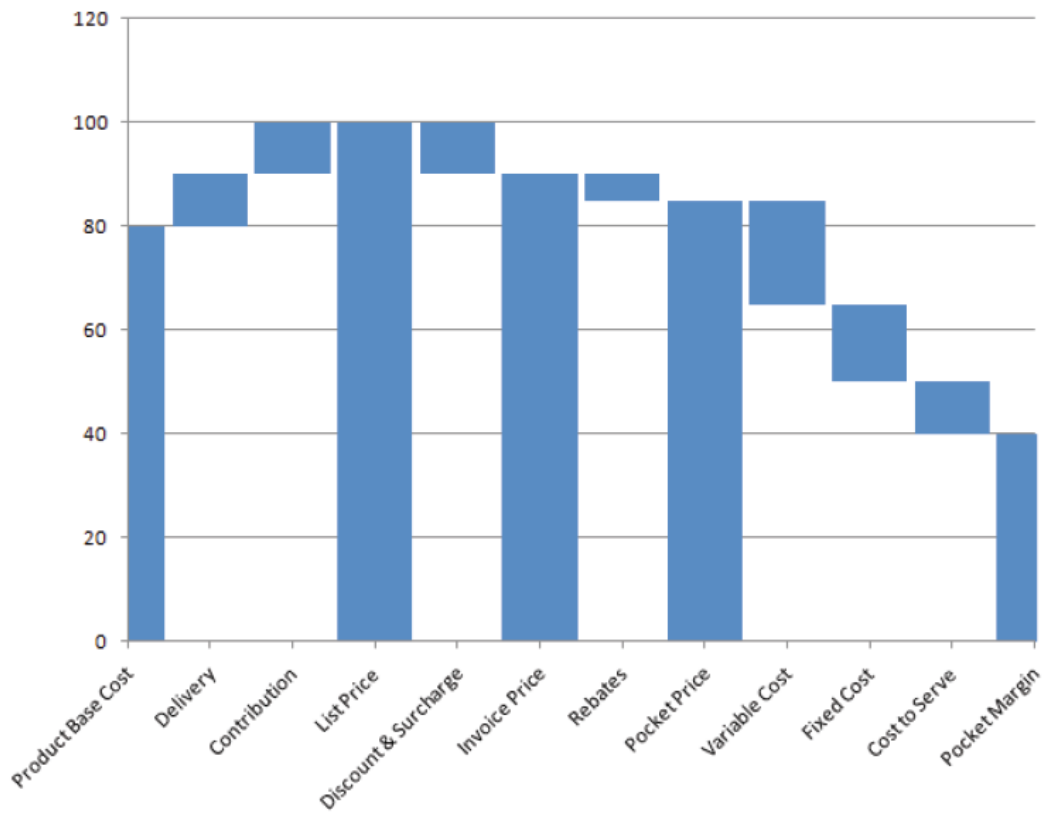
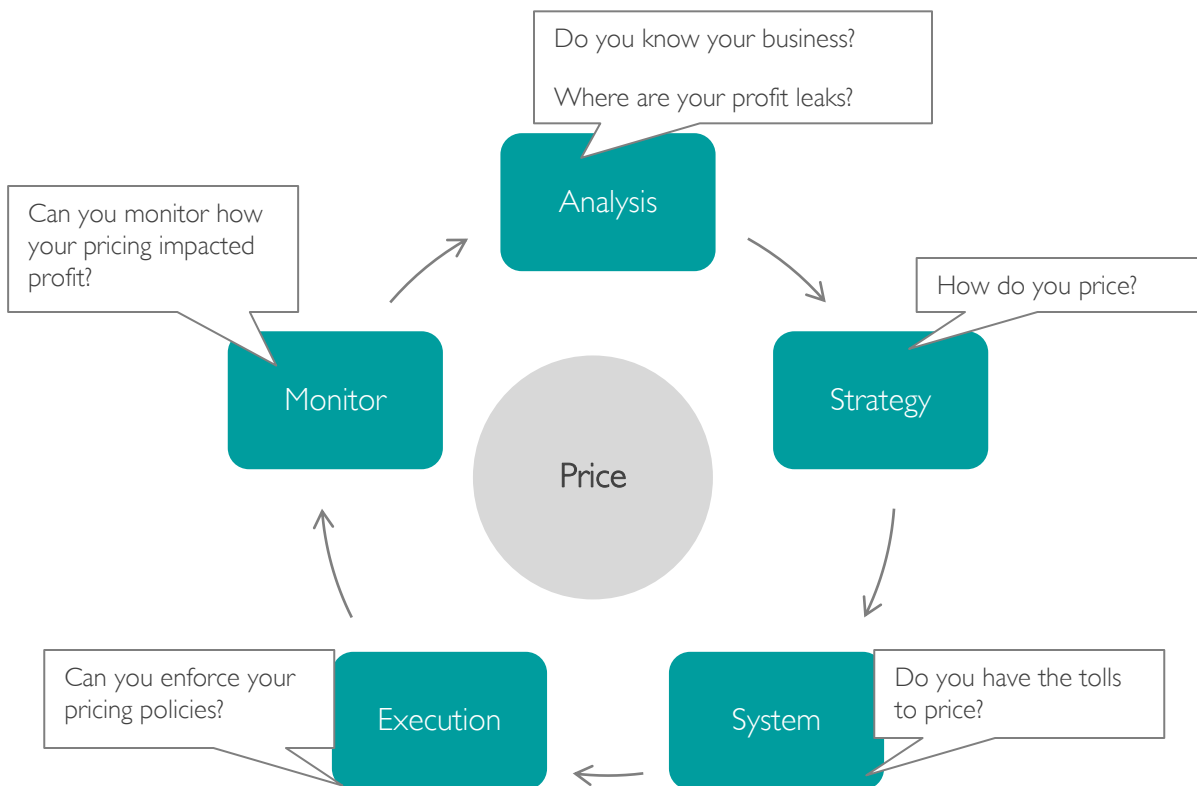
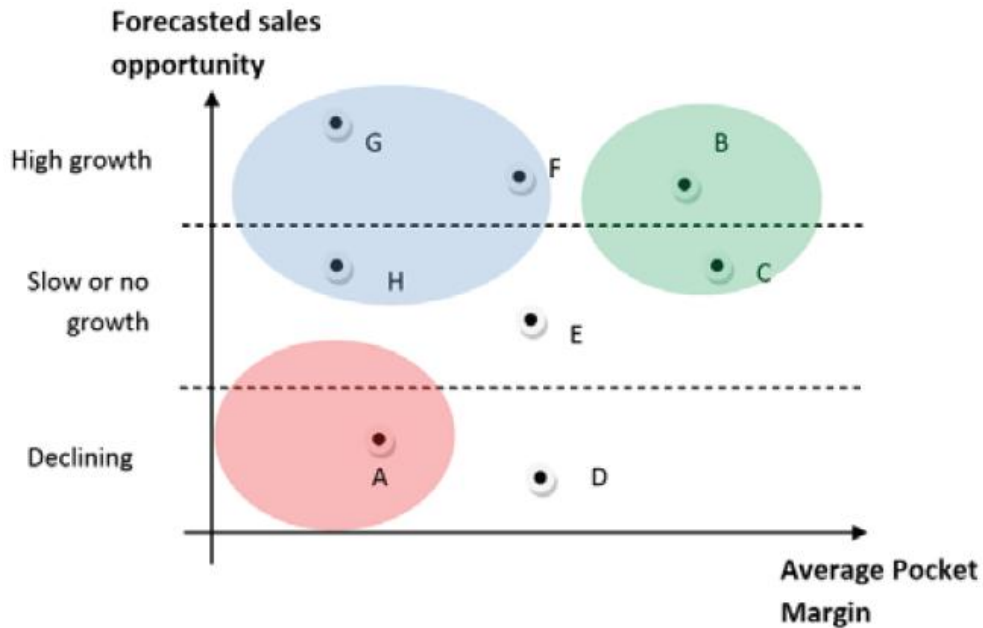


Figure 5. Wipro Pricing Process



Focus on the transaction axis allows capture and confirmation of insights and capabilities needed to develop an effective strategy in house...

Figure 6. Example Analysis of Product Performance Based on Pricing Data and Sales Input



In the example shown in Figure 6, products B and C (top right area of the graph) are pricing winners with high growth potential. Product A (bottom left) is a candidate for discontinuation, especially if the average pocket margin is close or below zero. Products F, G and H are in a high growth area but do not perform well from a pricing perspective. This should be an “early warning” for the pricing manager, and steps should be taken immediately to put these products in a more favourable pricing position to create a higher average pocket margin.

Involving the sales organisation in the pricing strategy discussion gives the pricing manager a more accurate picture of potential sales and forecast for the direction of the business.

Leading Practice #2.2: Implement automated data reporting. Combining current transaction data with historical transactions provides accurate trends that are essential for developing a pricing strategy. Automating a large portion of the data analysis offers a number of key advantages:

- Reports are provided in a consistent and timely manner.
- Data accuracy is assured.
- Employees are able to concentrate on business-critical tasks that cannot be automated.

Report automation increases the strategic effectiveness of decision making. Management can easily and quickly identify underperforming and top performing business activities; the business can become more agile and adaptive as a result.

Issue #3: CAPTURE QUANTITATIVE METRICS

Definition and continuous capture of key quantitative metrics allows in-flight improvements to pricing initiatives. This saves time and money compared to end-of-initiative results analysis and change implementation and also puts the business in a much more advantageous position in the competitive landscape.

Initial definition of these metrics will have occurred during preparation of the business case upon which the program investment is based. Once the foundation is established and strategy acceptance has been achieved, the metrics must be confirmed.

Transaction axis price optimisation should be based on detailed ROI, time to value and risk planning. Technology and automation solutions facilitate collection of quantitative data that can be used to design and track key metrics for the pricing improvement initiative.

Leading Practice 3.1: Require vendor investment in ROI and time to value analysis. In today's market, software vendors that offer pricing solutions often cover the cost of forecasting ROI and time to value as part of the engagement. A third party system integrator with experience in transaction level infrastructure projects should be involved in reviewing and verifying the vendor's predictions.

Leading Practice 3.2: Define KPIs with penalties / bonuses if variation is out of boundaries. When a pricing software vendor is selected, key performance indicators (KPIs) should be defined as part of final negotiations in order to hold the vendor accountable for results. Allowed variances from the actual KPI values and ROI estimates should also be defined and included in contract documents, along with monetary bonuses and penalties that will be incurred by the vendor if metrics are outside the variance limits. This contractual framework incentivizes the vendor to make correct ROI and time to value estimates while forming a true partnership with one common goal; improving your transaction level infrastructure within the given time and budget constraints. Use the agreed upon KPIs as milestones throughout the project time line to ensure that the vendor's ROI forecast are correct. If actual measurements are outside the variance limits, the vendor will pay a penalty or receive a bonus, depending on the nature of the overage.

Conclusion

Like a ship focused on reaching its destination, achieving optimum results from a pricing improvement initiative requires focus on both longitude (transaction axis) and latitude (strategy axis). Failure to base a pricing initiative on the transaction axis leads companies to follow the siren song of strategy consultants. They end up paying for a service that could be accomplished in-house if the proper (transactional axis) foundation is established. Depending on expensive strategy consultants to establish a new pricing strategy could put the organisation on the rocks because the current culture or technology cannot support the change.

Effective pricing strategy depends on a good transaction level foundation. Achieve strategy acceptance by ensuring organisational readiness, confirming data accuracy, and embedding the right transaction infrastructure into the current IT function. This will enable in-house pricing strategy development rather than strategy design by outside consultants.

By investing in the transaction axis first, your organisation will gain the competitive advantage of continuous strategy reviews, agility in responding to market events and strategy acceptance across the sales force. Most importantly, you will be able to drive pricing strategy in-house, which will reduce the costs of your price optimisation efforts and empower your management team to run an ROI-driven pricing programme.

About the Authors

Mirko Brinker is a consultant with the Wipro Pricing and Profitability Practice. He graduated from Imperial College Business School with an MSc in Management and from Copenhagen University College of Engineering with a BEng in Electronics and Computing. Mirko is a Prince2 certified project manager and has several years of experience as a consultant. Prior to joining Wipro, he founded and managed his own consultancy with two employees and worked as a consultant / project manager for two leading ICT providers in Europe, the US, and Brazil.

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Mark Allen is a Partner in Wipro's Global Energy Consulting Practice. He has over 20 years of experience in the oil and gas industry, first as part of a super major and then with two global management consulting firms. Mark has a proven track record helping clients with process improvements, cost management, system implementations and strategy execution. Prior to joining Wipro, Mark was the upstream industry lead for SAIC's oil and gas practice, with a focus on upstream oil and gas, and midstream natural gas and liquids energy segments.

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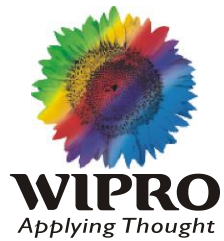
About the Wipro Pricing and Profitability Practice

With strong strategic alliances with the world's top pricing system vendors, Wipro's Pricing and Profitability Solutions Practice offers a beginning-to-end approach for all aspects of pricing improvement and management for profit growth. Our services include organizational readiness, process strategy, scientific analysis and optimization, technology selection, system integration/implementation, and change management. Our consultants and analysts help customers realize quick value, increase competitive advantage, and lower total cost of ownership through improvements in pricing strategies, processes, and technologies.

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