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Global Pricing Study 2011: "Weak pricing cuts profits by 25%" Management Summary

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Executive summary: Weak pricing cuts profits by 25%

1

Pricing power untapped

65% of the companies are not able to charge the prices they deserve

- Only 35% of the companies have sufficient pricing power* to achieve the "right" price for their products/services.
- Low pricing power is costly. It cuts profits by 25%.
- Chemicals (14%) and transport & logistics (19%) have the lowest pricing power.
- Brand and product value are the primary drivers of high pricing power.

2

Price wars continue

46% of companies still think they're in a price war (they didn't start)

- The crisis is over, but many companies are still fighting price wars.
- The extent of price wars differs greatly by country and industry; the Japanese market has by far the highest level (84%), followed by Italy (69%) and Spain (65%).
- High level of misperception: 83% of companies in a price war blame competitors for starting it.
- *"If you ask your people to strive for volume only, you should not be too surprised to end up in a price war"* (comment from surveyed manager)

3

Inflation threat underestimated

Companies only get half of what they expect when they try to raise prices

- Only about one-third of the companies is able to achieve at least 75% of the originally planned price increase.
- Telecommunications (25%) and life sciences (29%) have the lowest price implementation performance.
- 68% of the companies plan to increase prices below or in line with inflation; given the poor price implementation performance, this will not be enough.
- Construction, industrial goods and transport/logistics plan to increase prices above inflation rate to cover higher costs.

4

Four key measures

The better the pricing know-how, the higher the pricing power, the higher the profits

1. Re-direct your price strategy to achieve higher profits, rather than volume or market share. Introduce pricing power as a new KPI.
2. Pay particular attention to the pricing of new products and services.
3. Improve pricing expertise in sales, marketing and management.
4. Make your company inflation-safe by improving the price implementation and setting high price increase targets.

* Pricing power is the ability of a company to get the money it deserves for the value it delivers

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Set-up and methodology

The Global Pricing Study 2011 is the first of a series that will be repeated every year.



Methodology

- Online survey
- 15 questions in four parts:
Profit orientation, pricing power, inflation, profit outlook



Duration

- May 7 to June 28, 2011



Participants

- Mainly from Europe, the US and Asia
- From all major service and manufacturing industries
- Simon-Kucher & Partners clients, members of the Professional Pricing Society, alumni of IE Business School

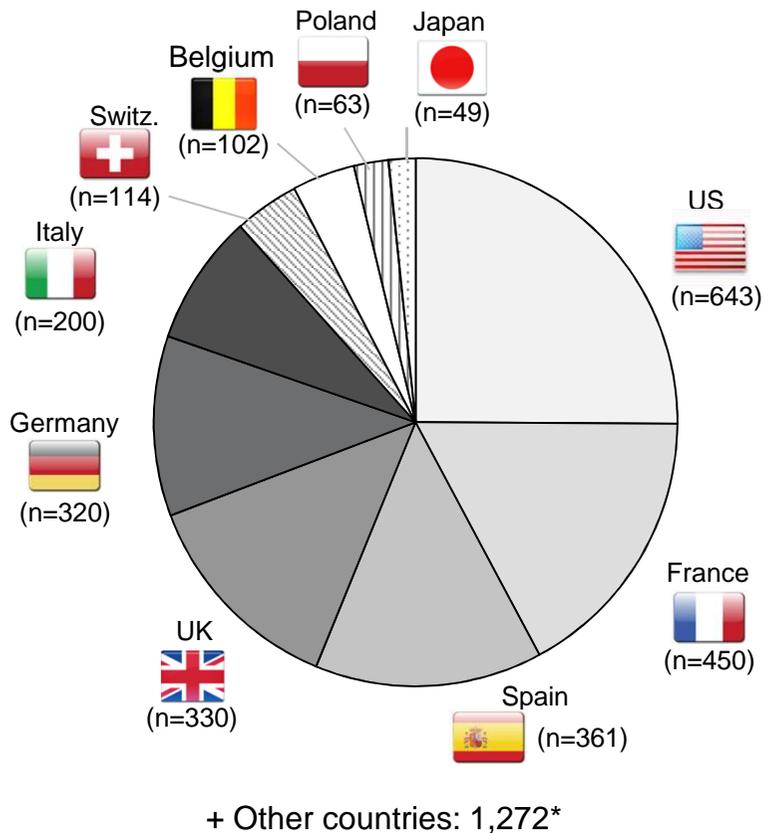


Sample size

- 3,904 valid responses

Geographic and industry distribution

Geographic distribution*
Total: 3,904 respondents



Industry distribution

Financial services (banking, insurance, private equity)	19%
Pharma, biotech/medtech	15%
Travel/hospitality	7%
Transport/logistics	6%
Automotive (manufacturers/suppliers)	6%
Media/entertainment	5%
Retail	4%
Industrial goods/machinery	4%
Construction	4%
Chemicals	4%
Telecommunications	3%
Consumer goods	3%
Energy/utilities	2%
Other (services)	10%
Other (manufacturing)	8%

* Countries with fewer than 49 respondents are not included in the graph. Among these countries are the Netherlands, Sweden, Austria, Denmark, Norway, Finland, China, Ireland, Russia, Canada, Mexico, Puerto Rico, Australia, New Zealand and Morocco. They account for a total of 1,272 respondents.

Profile of respondents

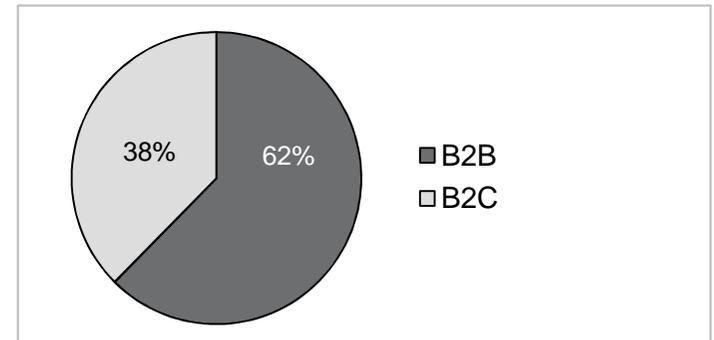
C-level executives account for almost one-third of the respondents; 41% are from €1bn+ companies.



Distribution by position in the company

Position	Percentage
C-level executives	31%
Marketing	20%
Sales	15%
Product management	8%
Finance/controlling	6%
Other (purchasing, reg. Op Co...)	20%

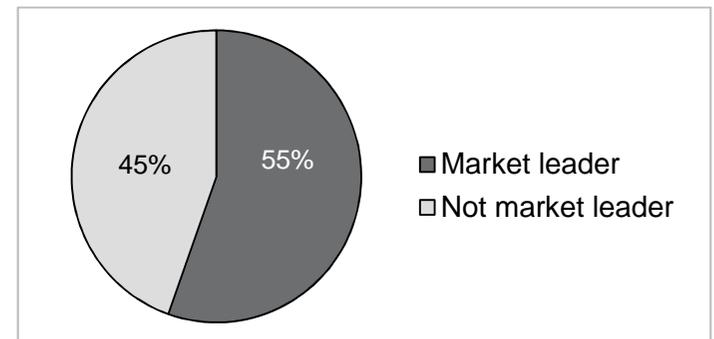
Distribution by type of activity



Distribution by company size

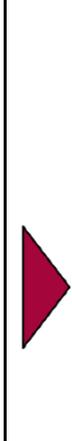
Company size (sales p.a. in €m)	Percentage
≥ 1,000	41%
500 to <1,000	11%
200 to <500	13%
50 to <200	17%
<50	18%

Distribution by market position*

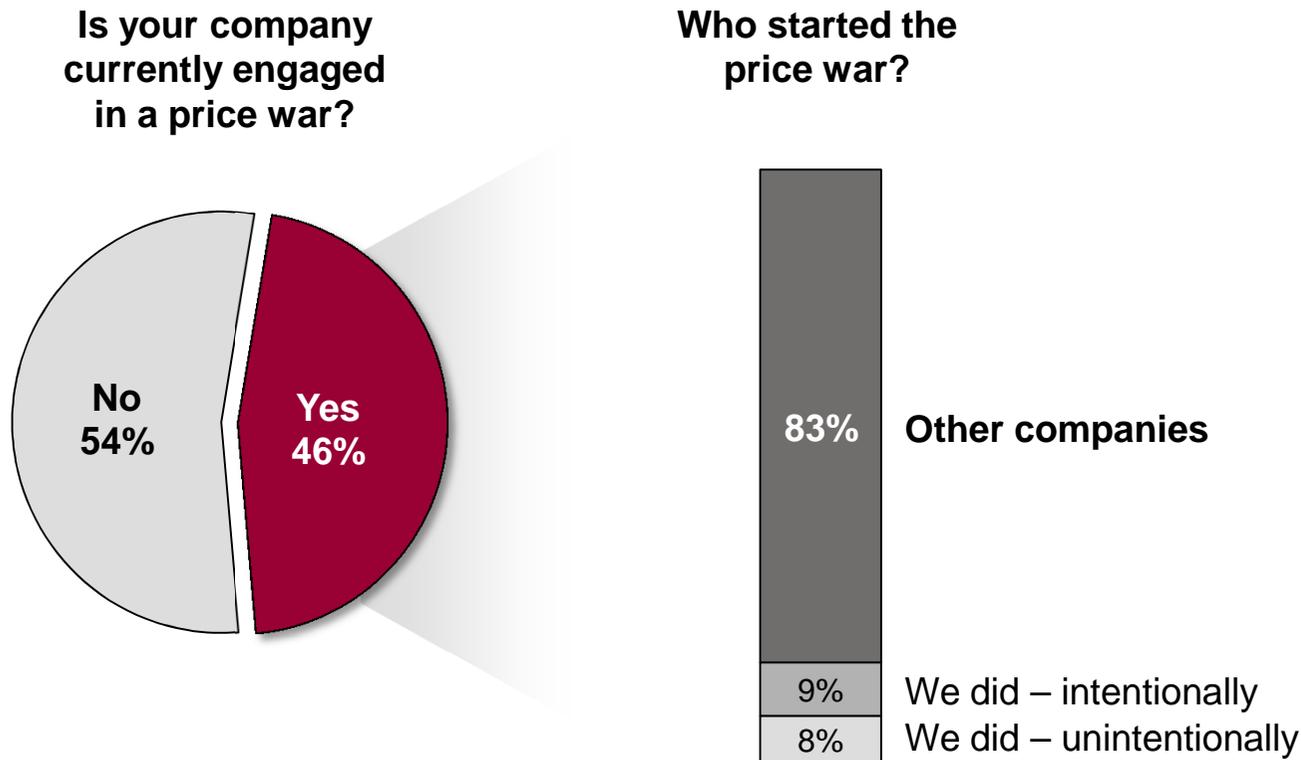


* As assessed by respondents

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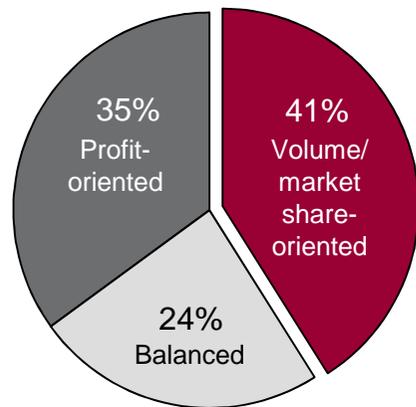
46% consider their company to be in a price war, and 83% of those blame competitors for starting it



- Industries with a disproportionately **large share of price wars**: construction, energy/utilities, chemicals, industrial goods, automotive
- Japan is the country with the most ongoing price wars (84%)

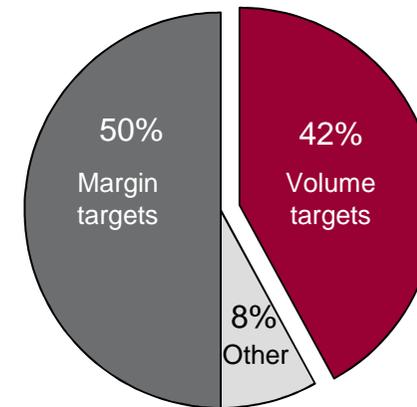
The majority of respondents describes their industry as volume-oriented

How do you describe your industry?



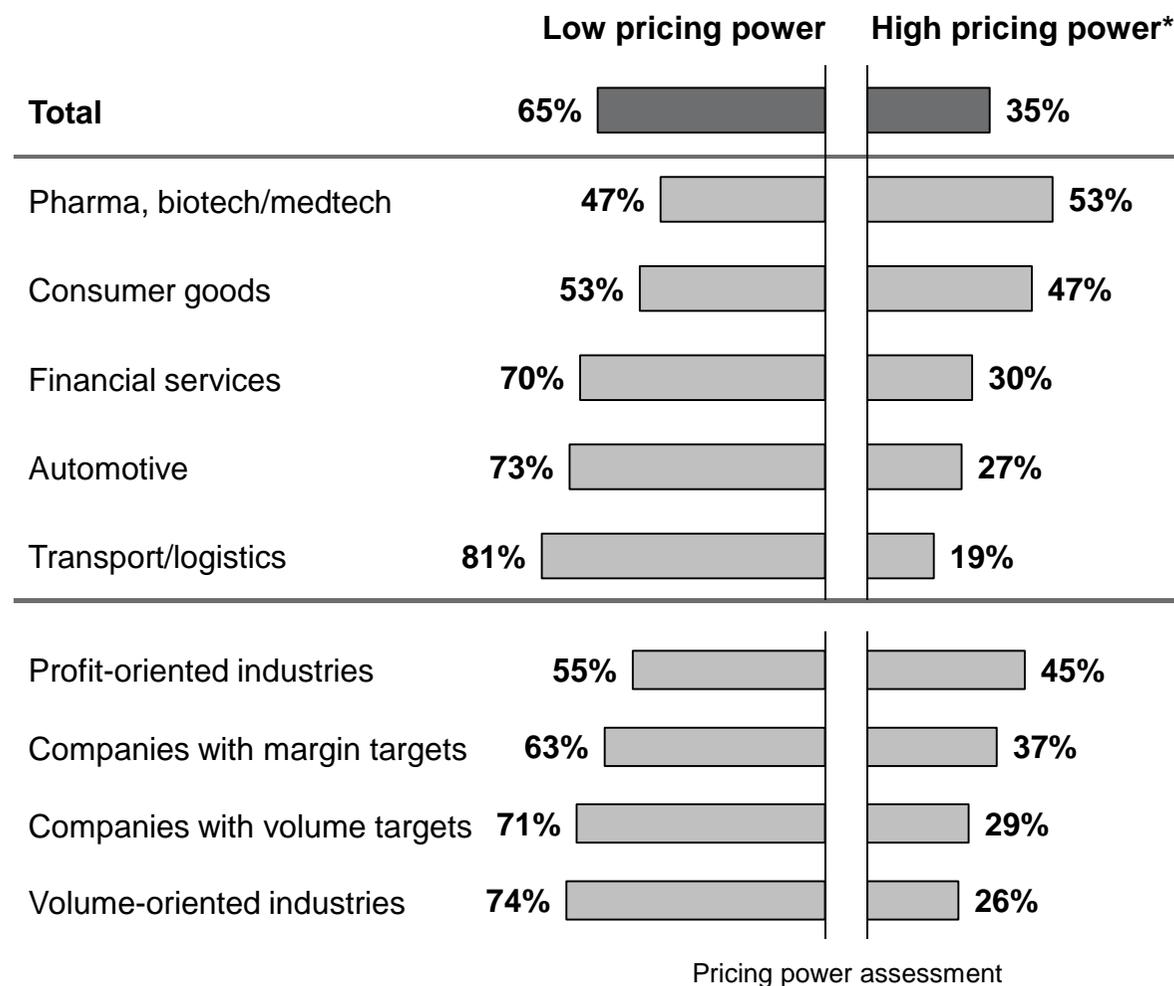
- Volume orientation especially strong in automotive, travel/hospitality, transport/logistics
- Not surprisingly, industry character influences the main targets of the price strategy

Predominant target of pricing strategy?



- 41% of industries are volume-oriented, 42% of companies have volume targets
- In Poland margin targets are most common, in Japan less so
- In energy/utilities, price strategy is dominated by margin targets

Low pricing power: Only 35% are able to get the "price they deserve"



- Two-thirds do not have sufficient pricing power to achieve the "prices they deserve"
- Large differences across industries

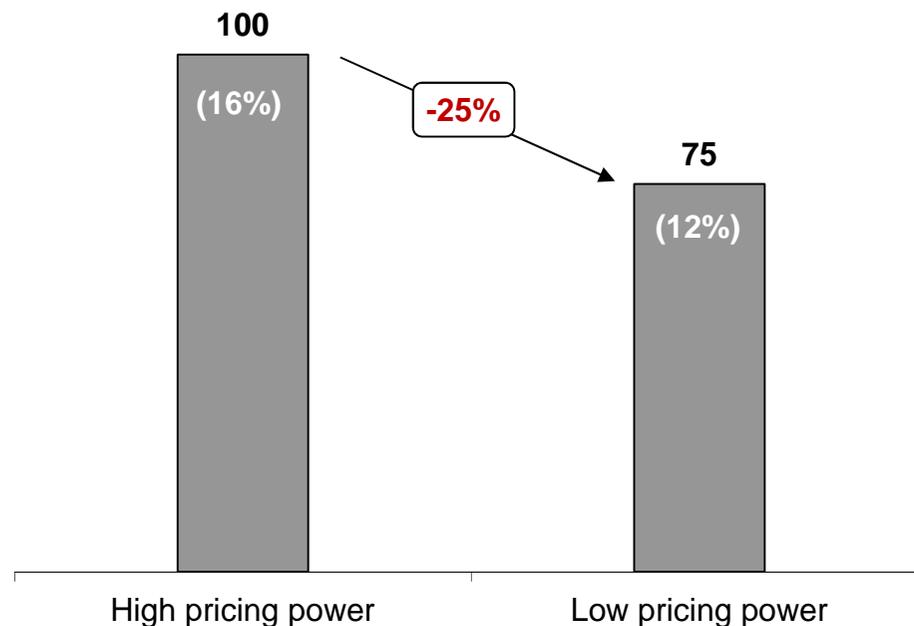
"If volume is your target, you should not be surprised if you end up with too low prices and low profits."

* High pricing power is the ability of a company to fully/almost get the money it deserves for the value it delivers

Source: Simon-Kucher & Partners Global Pricing Study 2011

Low pricing power reduces profits by 25%

EBITDA margin* over the last three years
(index, percent)

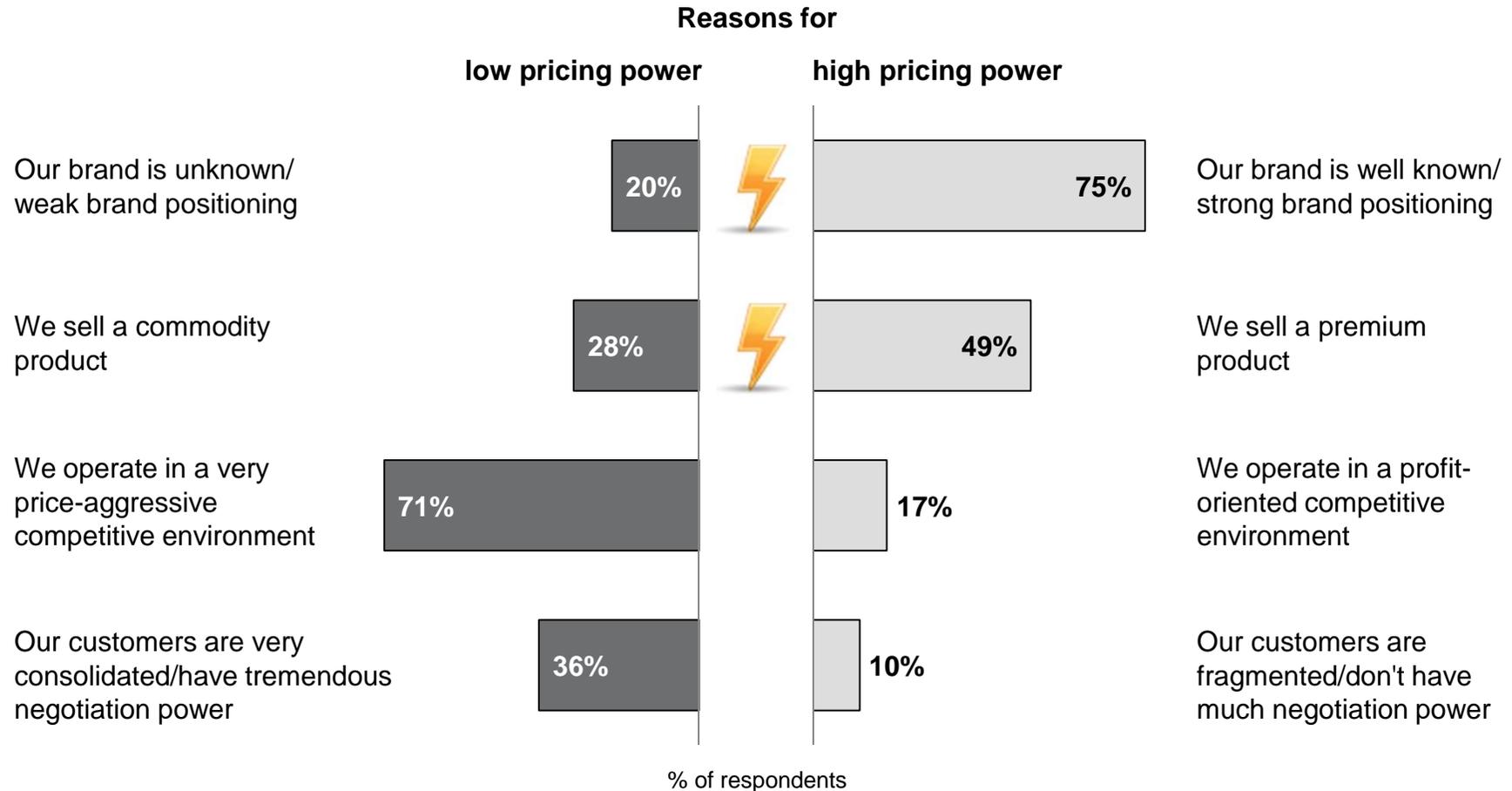


- Companies with low pricing power give away 25% of their profits
- "If all companies were aware of the negative consequences of poor pricing they would put more effort into the pricing function."
- Pricing power should become an important KPI for all companies

*EBITDA margin: earnings before interest, taxes, depreciation and amortization
Source: Simon-Kucher & Partners Global Pricing Study 2011

Brand and product value are the primary drivers of high pricing power

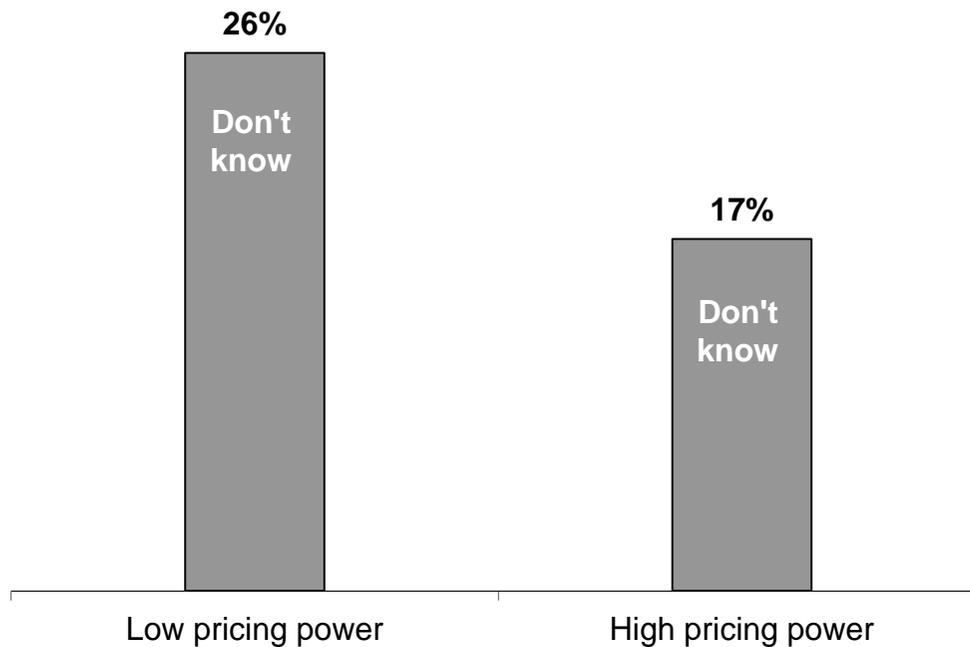
Companies with low pricing power primarily blame others (aggressive competitors, customers), even though value and brand lies in their own hands.



Source: Simon-Kucher & Partners Global Pricing Study 2011

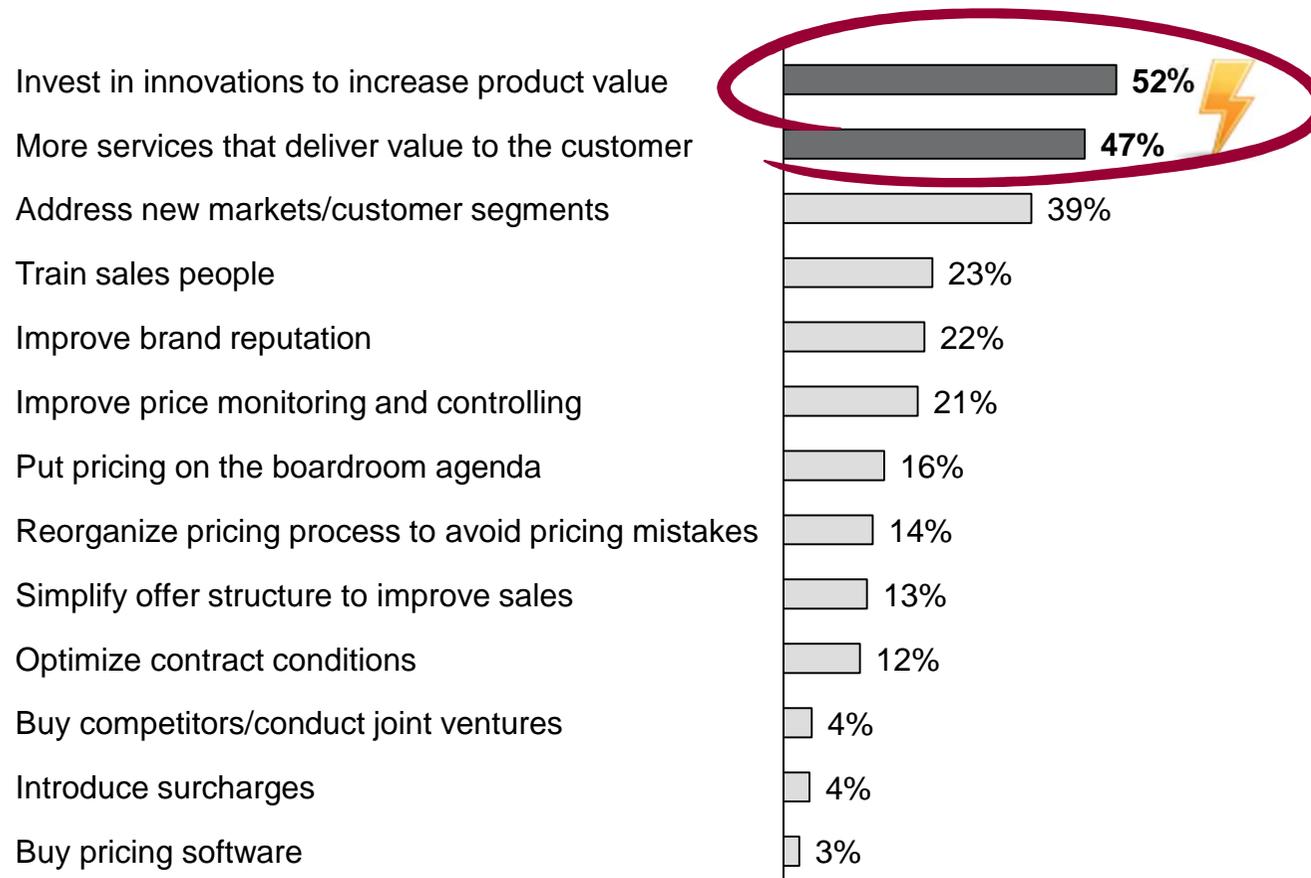
Companies with high pricing power have better pricing knowledge

What typically happens/would happen to your sales volume if your company raises/lowers prices by 5%?



- Pricing power does not emerge by accident
- A better understanding of price-volume relationships and more realistic price elasticity estimates lead to better pricing decisions

“Higher value” is the most important means of increasing pricing power



To dos:

- More focus on innovation
- Product **and** service innovation
- Right (value) pricing for these innovations
- Do the basic homework (price monitoring, train sales people etc.)

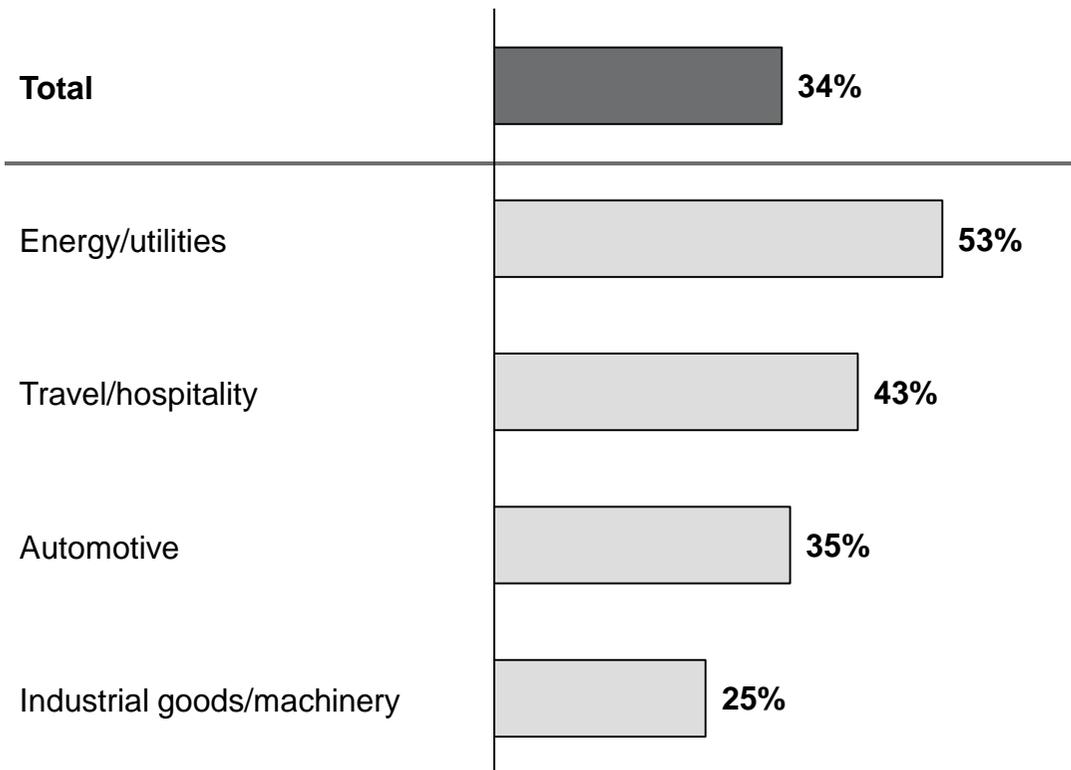
% of respondents indicating that this measure would best increase pricing power*

* Respondents could choose up to three reasons

Source: Simon-Kucher & Partners Global Pricing Study 2011

34% of respondents see a (major) profit risk caused by inflation

(Major) profit risk caused by inflation



- Large differences between industries
- Some industries like industrial goods/machinery, chemicals see higher inflation as a profit opportunity

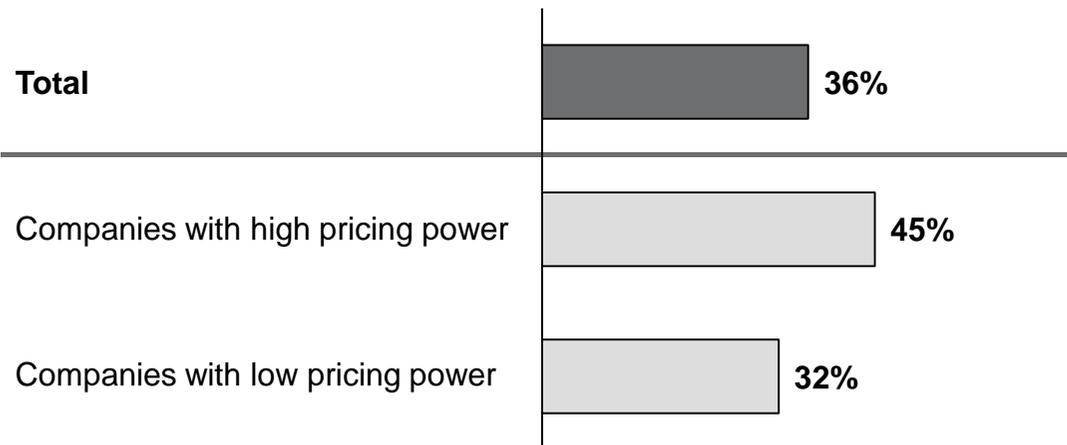
Source: Simon-Kucher & Partners Global Pricing Study 2011

On average companies realize only 53% of their planned price increase

Actual achieved price increase compared to target



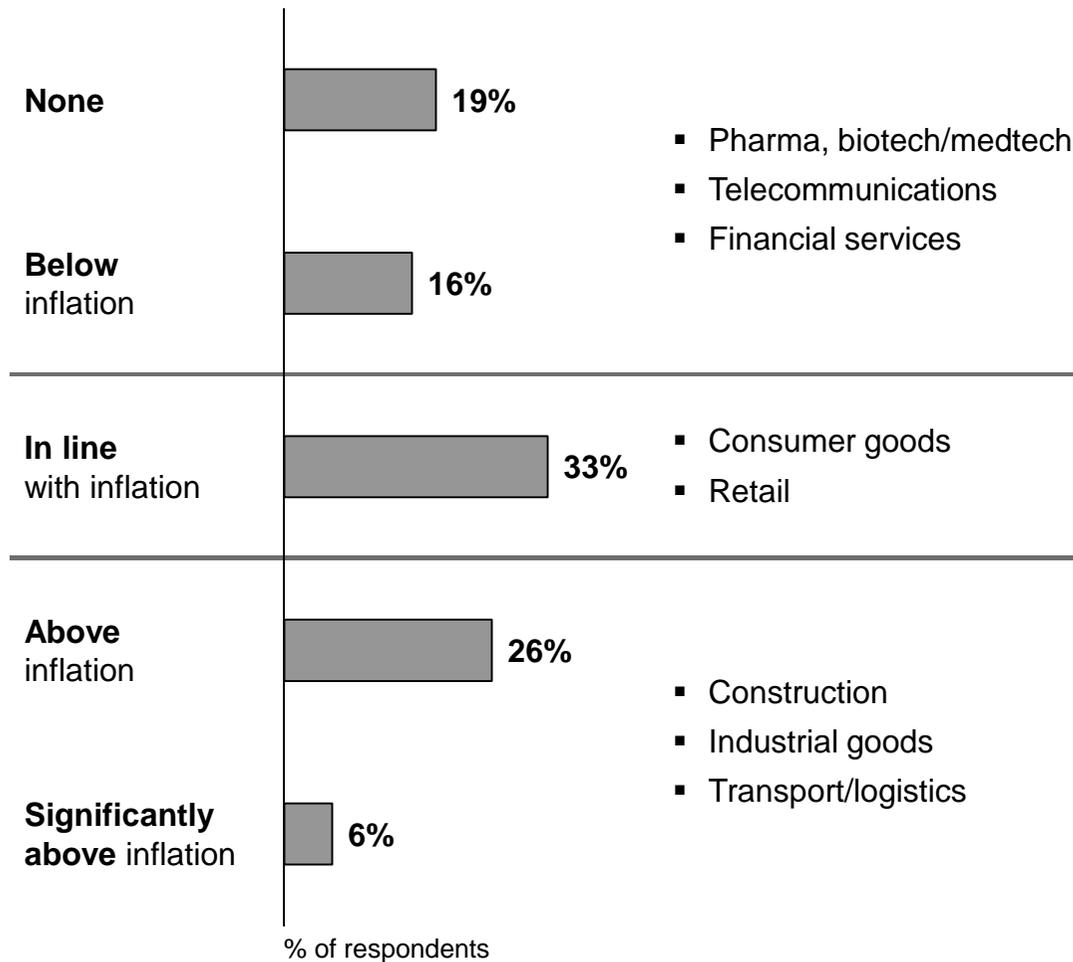
Percentage of companies achieving at least 75% of their target



- In general, ability to implement price increases is poor
- Significant improvement necessary, otherwise big risk in inflation periods
- Companies with high pricing power are doing much better than the rest

The majority of companies will raise prices at or below inflation rates

Target price changes relative to inflation rates



Top reasons

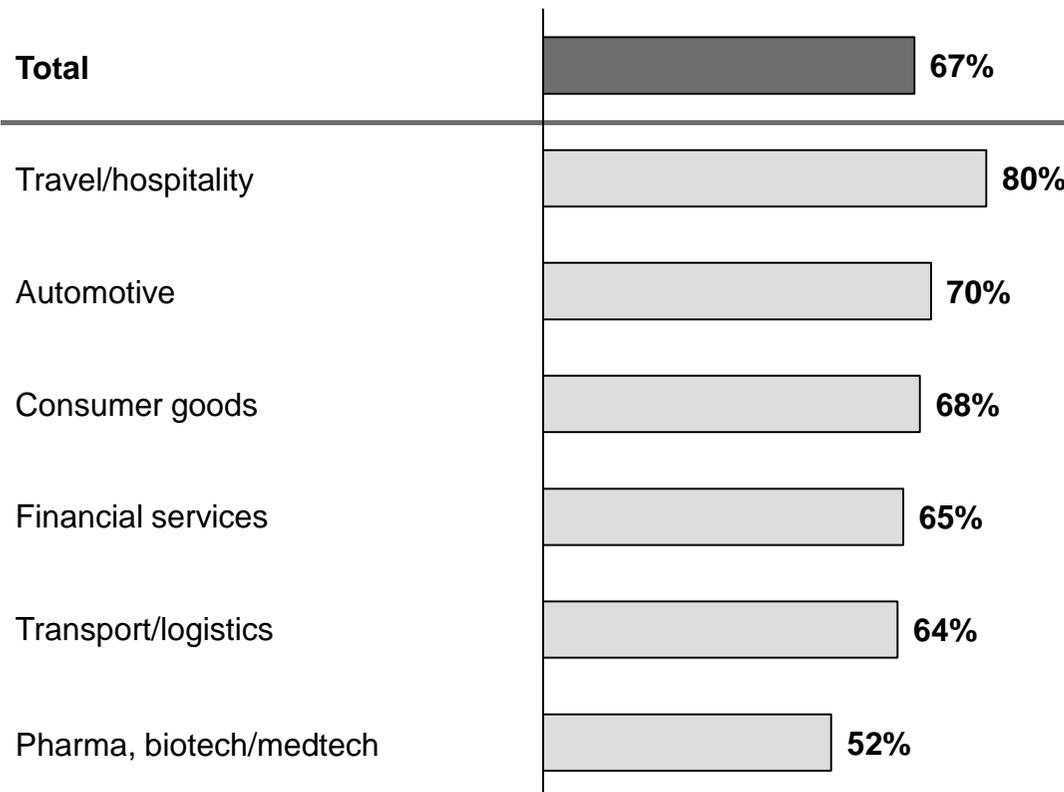
- *"Competitors won't raise their prices. So we have to stay below the inflation rate."*
- *"Our customers won't accept higher prices."*
- *"Contracts and commitment to price stability block any price increase."*
- *"We can explain a price increase in line with inflation to customers, but not more."*
- *"We have to pass on the cost of inflation to customers to maintain our profits."*
- *"Cost increases exceed inflation and need to be covered."*

Given the poor price implementation performance, this will not be enough.

Source: Simon-Kucher & Partners Global Pricing Study 2011

Profit outlook is positive overall

Share of companies expecting a (strong) profit increase over the next three years

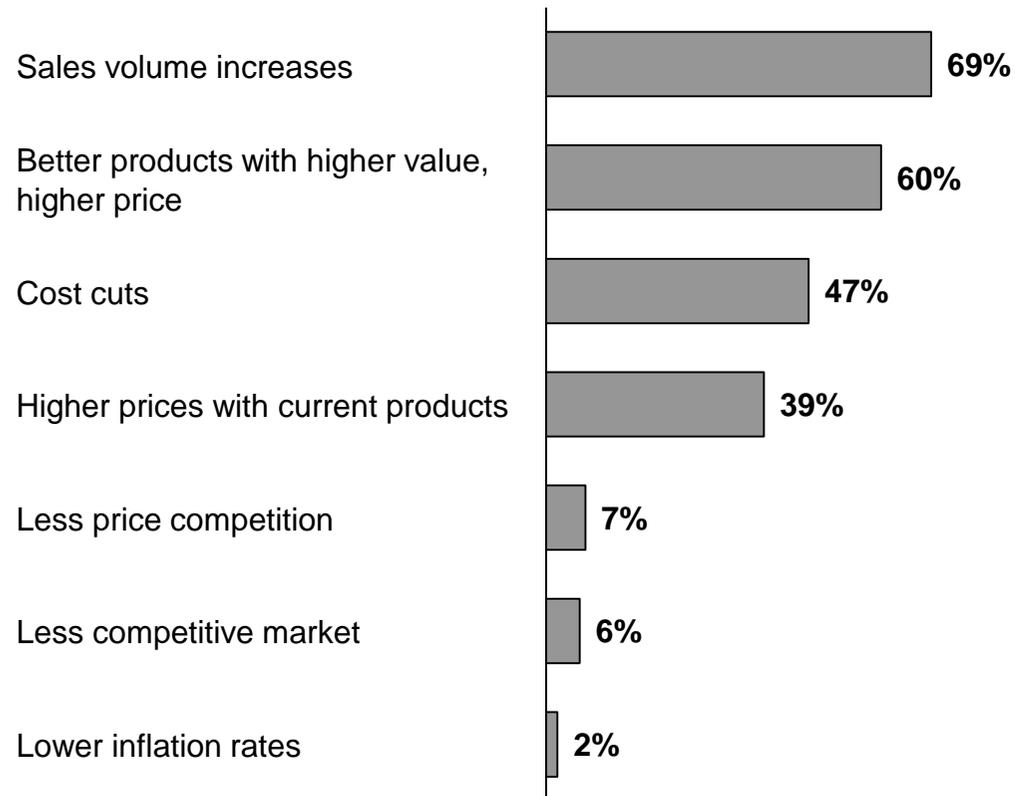


- Respondents in most industries have high expectations of profit growth
- Confidence is higher in cyclical industries such as travel and automotive
- Profit growth is expected to come mainly from volume growth and better products with higher prices

Source: Simon-Kucher & Partners Global Pricing Study 2011

Main profit drivers: More volume and higher prices for innovations

Most important reasons for the expected higher profits



% of respondents indicating this lever is a reason for a positive profit outlook

- Pricing contributes to profit growth by means of **higher prices for new products** (rather than price increases for current products)
- Volume increases are seen as the most important profit driver
- Cost cuts are less important than pricing and volume

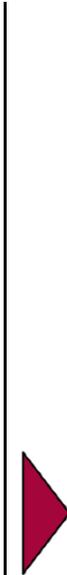
* Respondents could choose up to three reasons

Source: Simon-Kucher & Partners Global Pricing Study 2011

What you should do: Lessons learned from pricing champions

1. Poor pricing performance is not a question of fate. So do not simply blame competitors and customers for your low pricing power. To a large extent it is up to you whether you become a pricing champion and achieve higher profits than your peers or whether you end up in price wars with ruined price levels.
2. Prevent price wars at all costs. Start with your strategic goals. Assess your price strategy and make sure that it clearly focuses on profit instead of volume or market share.
3. Companies with high pricing power achieve higher profits and perform better in many aspects. Redirect your whole organization towards pricing power and make it one of your top KPIs.
4. Strategic measures to improve pricing power: Invest in value and brand. Pay particular attention to the pricing of new products and services; mistakes in this field cannot be corrected.
5. Short-term measures to improve pricing power: Do your basic homework. Improve pricing expertise in sales, marketing and management. The better your pricing know-how, the higher your pricing power and the higher your profits.
6. Make your company inflation-safe. Improve your price implementation performance and set high price increase targets which take that performance into account.

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Simon-Kucher & Partners: Scope and reputation

World market leader in pricing

BusinessWeek

"World leader in giving advice to companies on how to price their products"

The Economist

"The world's leading pricing consultancy"

THE WALL STREET JOURNAL

"Pricing strategy specialists"

Peter Drucker

"In pricing you offer something nobody else does."

No. 1 in marketing and sales in Germany*

Rank	Consultancy	Score	manager magazin
1	Simon-Kucher & Partners	389	
2	Boston Consulting Group	387	
3	McKinsey & Company	372	
4	Bain & Company	349	
5	Roland Berger	346	

Global presence

23 offices worldwide

Employees: 500



Revenue, 2010: €105.4m

* Maximum 500

Source: *manager magazin* August 2007/IMB (Institute for Management & Consulting); survey of 264 top managers; *manager magazin* August 2011/IMB (Institute for Management & Consulting); survey of 452 top managers

> 2,000 projects in the last three years



- Growth and competitive strategies
- Product portfolio (re-)design
- Pricing excellence
- Customer relationship and customer value management
- Sales strategies and sales channel optimization