

# Distribution Research Consortium

Pricing Optimization Consortium



Supply Chain Systems Laboratory

Industrial Distribution Program, Texas A&M University

# Distribution Research Consortium

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The Supply Chain Systems Laboratory (SCSL) will establish a Research Consortium to conduct research and develop research driven educational programs in **Pricing Optimization (PO)**. The consortium will conduct research in Distribution Pricing and develop practical methodology and tools that can be used by the consortium members to improve their operations. A 2 day educational session will be developed based on the resulting knowledge, methodology and tools.

## What is a Research Consortium?

A Research Consortium is a collaboration of two or more companies, associations, universities or government agencies to conduct research with the objective of developing solutions to a problem or a challenge common to everyone by pooling their resources for achieving a common goal.

## Why join a Research Consortium?

Many times companies cannot afford to invest in some research and development due to high cost and/or lack of knowledge resources required to conduct the research. Research Consortia are an economical path to low cost, high quality research and development that is essential to the growth of the company.

## Who should join this Research Consortium?

This Research Consortium will be beneficial to:

- Distributors and Manufacturers who supply through Distribution.
- Technology Providers who serve Wholesale Distributors and Manufacturers.

## What are the Benefits?

The benefit to the consortium member includes the opportunity to actively participate in this ground-breaking research into one of the most crucial and timely challenges facing the industry. Each member of this consortium will also be able to direct the scope of this research so that the results are actionable and sustainable. Additionally, **members of the consortium will have the opportunity to send up to 20 people from their organization to the educational programs at no cost** other than the travel expenses during the 2006 sessions. The educational programs will be scheduled three times every year following the conclusion of this research.

## Deliverables

In addition to the body of knowledge resulting from this research, the following tangible outcomes will include:

- Tools and methodology developed from the research and a book written by the research team.
- A 2 day educational seminar aimed at providing firms with knowledge into how they can apply the concepts, tools and techniques identified in the research.

## Consortium Structure and Fees

Membership in the consortium is limited to a **group of 10 companies** to be an effective research group. Membership will be on a first come first serve basis. The membership fee is **\$25,000** per company.

## Schedule

The Research programs will begin January 1<sup>st</sup> 2006 and conclude Aug 31<sup>st</sup>, 2006. The first three educational sessions for each consortium will be scheduled starting September 2006.

## Why Texas A&M?

With almost 50 years of Education and Research experience, Industrial Distribution Program at Texas A&M is the largest and one of best programs in the U.S. Leaders in Distribution Research: Texas A&M Supply Chain Systems Laboratory is the premier Distribution research, education and solution laboratory. Advancing the science of Distribution is our mission.

# Pricing Optimization

## Scientific Pricing of Distribution Products and Services

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### Overview & Need

Pricing is the gross margin inverse of asset management and procurement procedures. While the latter are designed to decrease cost (the lower margin boundary) the former is designed to raise revenues (the upper boundary). Pricing is typically market-based but pricing decisions are very complex and, when made in an information vacuum, will sub-optimize gross margins for the firm. While most enterprise systems collect significant information on customers, only a small portion is delivered to the sales force and then only in the format collected. The sales force, therefore, is forced to make discounting and market pricing decisions on an aggregate basis. While aggregate pricing should be understood, customer by customer discount decisions require a deeper understanding of the relationship, customer past history, credit status, and numerous other activities routinely tracked by the system. These decisions are carried out at every operation (branch), on a daily basis, by multiple individuals often with little system support.

The pricing/discounting decision is an information exercise and determines at least half of the firm's profitability equation. Distribution profitability depends on increasing revenues and reducing operational cost. More often distributors tend to spend their effort on reducing cost by optimizing their resources such as implementing effective inventory management and efficient transportation systems than to explore opportunities to increase revenue and thereby increase profitability. Pricing decisions on products and services is the key to increasing revenue, profitability and market share.

### Solution Approach

Distribution pricing has traditionally been practiced as an art and not considered a science. Scientific pricing decision making is one potential focus area for profitable revenue management. Many distributors operate on a *cost-plus* pricing mentality, making pricing decisions (discounts) based on only product, volume and customer information. Often the laws of demand, supply, degree of competition and buyer behavior is ignored. It is important to understand and develop scientific pricing models and strategy using multiple decision criteria/variables such as product, volume, customer, geography, market structure, competitive environment, customer behavioral constraints, and the economics of information management. These scientific pricing models should then be enabled by the very systems that provide the data.

### Methodology

Even though most distributors understand to some extent other external drivers of pricing such as competition and market structure, understanding and implementing a holistic approach to pricing has always been difficult. This Consortium will research pricing strategy and variables designed to include break even analysis, price elasticity, price thresholds, product life cycle pricing and price sensitivity. Scientific pricing decision making is one potential focus area for profitable revenue management. Profitability depends equally as much on pricing as it does cost control.

The key project steps are:

- Texas A&M Research team will conduct a survey of current distribution pricing strategy, practices and enterprise system capability/functionality with the Consortium members.

- Conduct quantitative research to develop new and practical methods to maximize profits.
- Research in to pricing methods of products, services and bundled products and services.
- Quantify the external price drivers such as demand, competition, value to customer, etc and develop methods to incorporate it to pricing methods.
- Research in to price discounting by customer, product line and volume.
- Develop practical pricing methods that consider price elasticity, price thresholds, product life cycle pricing and price sensitivity.
- Develop IT based tools that demonstrate the methods developed.
- Develop profitability analysis methodology and key pricing metrics for monitoring and managing profitability.
- Develop Best Practices in pricing process administration, and developing metrics to monitor and improve the performance of pricing methods.

Goals	Current Issues	Solution	Benefits
Increase Profits by Effective Pricing Management	Poorly developed discounting practices, lack of pricing training	Research based methods and tools for pricing and pricing training for sales force	Maximize total profits and provide value to key customers.
Pricing over Product Life Cycle	Poor understanding of price elasticity, discounts and lack of tools	Develop strategies and methods to maximize total profits	Increase profits during new product growth, prevent obsolescence by discounting at decline.
Effective pricing of services and price bundling	Lack of methods to price services & understanding of service profitability	Methods and tools to price services and bundles	Maximize profits on services, kits, bundles, and projects.
Automated pricing mgmt, Profitability Analysis and Pricing Information mgmt.	No Best Practice methods and Information System support	Develop Best Practices, Profitability Analysis and Key Performance Metrics (KPIs)	Automation of pricing processes, management by exception, manage & monitor profitability.

### Value to Members

The consortium members will receive results, methodology and tools developed during this pioneering research in to Distribution Pricing. The key advantage for Distributors and Manufactures would to gain a competitive advantage by implementing the scientific pricing methods or using the tools developed to maximize profits. The key advantage to Technology and Enterprise software companies will be gain the knowledge base, methods and tools that can be implemented in their systems.

Apart from shaping the research focus and gaining valuable knowledge base, methodology and tools, each consortium member will be able to send up to a total of 20 people to three educational sessions that will be developed from this research. The educational sessions alone represent a \$40,000 value.

### Schedule

June 1<sup>st</sup> – Dec 15<sup>th</sup>, 2005 : Membership Enrollment & Consortium Formation  
 Jan 1<sup>st</sup> – July 30<sup>th</sup>, 2006 : Conduct Research and Develop Tools  
 Mar 30<sup>th</sup>, May 30<sup>th</sup>, July 30<sup>th</sup> : Project Update Webinars to Members  
 July 1<sup>st</sup> – Aug 31<sup>st</sup>, 2006 : Develop Educational Program  
 Sep 1<sup>st</sup> – May 31<sup>st</sup>, 2007 : Deliver Three Educational Programs

## About the Supply Chain Systems Laboratory

The Supply Chain Systems Laboratory (SCSL) is a Texas A&M Industrial Distribution Program laboratory to educate our students, create cutting edge solutions for wholesale and industrial distribution channels, and provide answers to Distribution and Supply Chain Management (SCM) challenges.

**Leaders in Distribution Research:** Texas A&M Supply Chain Systems Laboratory is the nation's premier distribution research lab. We bring cutting edge distribution and supply chain research solutions to the industry. The Lab provides total solutions for companies by providing research expertise, project execution support, IT implementation assistance, education and training for end users.

### Research Solutions

The lab conducts research to solve distribution industry problems by developing processes, technology and connectivity to define, build, analyze, measure, improve and control the supply chain and its performance. Research topics include inventory management, distribution network optimization (asset management), logistics planning, distribution channel analysis etc. The lab performs strategy development, process improvement and technology implementation projects for industrial wholesalers, distributors and manufacturers. Projects areas include Inventory classification (ABC stratification), Forecasting, Purchasing planning, Network optimization, Applications of performance metrics, Enterprise Resource Management (ERP) process and functionality improvements etc. The lab also assists distributors and manufacturers with technology implementation, process automation and training to better manage their assets and increase profitability. The lab acts as a technology test bed for simulating and solving complex supply chain problems.

### Educational Programs

The Supply Chain systems Laboratory offers education and training to industrial distributors and manufacturers. The lab provides:

- Custom on-site training programs for executives and managers
- Online self paced learning courses for non-managerial employees
- Workshops - Interactive discussion sessions on challenges and opportunities
- Presentations & webinars on emerging topics at trade association events, distributors and manufacturer conferences.

The educational programs are research based, innovative, proven and cutting edge methods developed at Texas A&M Industrial Distribution Program.

**For more information or to  
Join the Research Consortium please contact:**

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