Pricing Practices in Manufacturing

China Case Study

July 2009
Table of Contents

- Setting the Context
- Understanding the Manufacturing Pricing in APAC
- The Need for Change in China
- Transitioning to a Value-Based Pricing Model
- Overcoming Challenges in China
The study will focus on current pricing practices in China

Objectives of the Study

- Describe current pricing strategies of manufacturers in China
- Compare and contrast with other countries in Asia-Pacific
- Introduce pricing best practices
- Show challenges facing Chinese manufacturers in achieving these best practices and how these barriers can be overcome

The Context

- The manufacturing industry in China has quickly evolved over the past two decades and the development of sophisticated pricing strategies has lagged behind
- Chinese manufacturers’ current pricing models tend to be simplistic and are not incorporated into overall business strategy
- The country’s economic and political characteristics have impacted its business strategies
- International competitive landscape is changing and other countries are showing a cost advantage over China
- Chinese manufacturers will need to find a new way to stay competitive aside from focusing on price
We will compare pricing in manufacturing industries in China with practices of those in Japan and India

<table>
<thead>
<tr>
<th>Focus on China</th>
<th>Japan and India: the basis for comparison</th>
</tr>
</thead>
<tbody>
<tr>
<td>▪ Manufacturing industry is one of the largest industrial sectors in China (over 33% of GDP)</td>
<td>The manufacturing industry in Japan is notably different from that of China:</td>
</tr>
<tr>
<td>▪ The industry is competitive, not only domestically but also internationally, and there are opportunities for Chinese manufacturers to compete more effectively</td>
<td>▪ Industry in Japan is more mature, especially in the electronics and automotive sectors</td>
</tr>
<tr>
<td>▪ Chinese manufacturers are not yet using pricing strategy to maximize profitability</td>
<td>▪ Japan's focus is on high quality, more sophisticated technology and specialized products</td>
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<tr>
<td></td>
<td>▪ Japanese companies compete on a number of elements, not just on price</td>
</tr>
<tr>
<td></td>
<td>▪ Manufacturing industry in India is smaller, but growing</td>
</tr>
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<td></td>
<td>▪ India is also viewed as a low cost country, it is a popular contract manufacturing and sourcing location, and much of its manufacturing is for export</td>
</tr>
<tr>
<td></td>
<td>▪ Both countries manufacture less sophisticated electronics and components compared to Japan</td>
</tr>
</tbody>
</table>

Source: Accenture analysis, China Statistical Yearbook 2007
Table of Contents

- Setting the Context
  - Understanding the Manufacturing Pricing in APAC
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China’s manufacturing industry differs from that of India and Japan based on capability and maturity.

Manufacturing Industry Overview by Country

**China**
- **Percentage of GDP:** 33%
- **Main categories:** electronics, metals, transport equipment, chemicals
- **Competitive advantages:** comparatively low cost of labour, established infrastructure, strong manufacturing experience
- **Drawbacks:** rising costs of labour, reputation for questionable product quality, poor intellectual property protection

**Japan**
- **Percentage of GDP:** over 20%
- **Main categories:** transport equipment, automotive, machinery, chemicals, electronic parts & devices, electrical machinery
- **Competitive advantages:** strict quality assurances, advanced engineering capabilities, use of robot technology to lower cost
- **Drawbacks:** expensive due to high cost of labour and cost of quality control

**India**
- **Percentage of GDP:** 15%
- **Main categories:** automotive and automotive components, textiles, steel, pharmaceuticals
- **Competitive advantages:** low cost of labour, engineering capabilities, English-speaking workforce
- **Drawbacks:** poor infrastructure, high cost of power

Source: Accenture analysis, India Central Statistical Organisation, China Statistical Yearbook 2007, Economist Intelligence Unit
Our study will be based on five main hypotheses

1. The manufacturing industry in China is generally commoditized
   Many products manufactured in China are low-end, low-cost products with few differentiating features

2. The pricing in the manufacturing industry in China has been impacted by China’s unique economic and political history
   China’s legacy of a planned economy, political history and cultural mentality have impacted pricing in manufacturing

3. “Cost +” is a common method of determining price in manufacturing in China
   Managers choose the “cost +” model due to lack of pricing knowledge and ease of implementation

4. Competitor pricing is also a major influence on price setting in China
   Manufacturers index prices to competitors due to commoditization of products

5. Other countries in Asia-Pacific employ different pricing models
   Pricing in Japanese and Indian manufacturers employ different pricing models
Hypothesis 1: The manufacturing industry in China is generally commoditized

Chinese manufacturers are maturing and struggling their way out of a market still filled with extensive low-end, low-cost commodities.

- Chinese manufacturing industry is at the gate of the later stage of industrialization with the rapid development of heavy equipment.
- Still dominated by labor intensive industry focusing on low cost.
- Some Chinese light industry is quite developed (e.g. the household appliance industry) though, most industries, especially heavy industries, are still at the development stage (e.g. automobile industry).

The Status Quo

1. Lack of innovation and core competency, dependent on importing techniques.
2. Extensive low-end products with limited differentiation.
3. Lowest price the main determinant of supplier selection.
4. Lack of management skills and advanced marketing skills.
5. Lack of top multinational companies or specialized middle size companies.
Hypothesis 2: Pricing has been impacted by China’s unique economic and political history

China’s legacy as a planned economy has had a lasting impact on business mentality and processes.

1. Lack of innovation, dependent on importing techniques
2. Extensive low-end products with limited differentiation
3. Lowest price the main determinant of supplier selection
4. Lack of management skills and advanced marketing skills
5. Lack of top multinational companies or specialized middle size companies

- China’s economy was planned economy, manufacturers are used to running factories as dictated
- Managers had no say over strategic decisions
- Marketing, sales and pricing management was overlooked, causing a lack of talent and management skills in these fields

- Chinese traditionally base business decisions on “Guanxi’ (relationships), so quantitative analysis aspect usually ignored
- “Cost +” method an easy solution since limited data available

- China’s government issued policies to protect certain industries from free marketization (i.e. tobacco and utility industries)
- Still an element of state control

Elements interconnected and influenced by legacy of planned economy
Hypothesis 3: “Cost +” is a common method of determining price

As a result, “cost +” is a common and “convenient” method of determining price in manufacturing in China

- As a result, “cost +” is widely since it is the easiest method to understand and the simplest method to implement
- For example, many Chinese car manufacturers use the “cost +” method for spare parts pricing, charging 100% mark-up for all spare parts across the board, regardless of customer or product
- SiemensVDO also used the “cost +” method. However, because of the pressure on price reduction, SiemensVDO launched “Design to Cost” project to reduce the car parts costs, so that their price could still be competitive after adding on a fixed amount of margin

- Selling price determined by taking the direct variable costs of producing the product and adding a mark-up
- Mark-up equals desired gross margin of the product

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Hypothesis 4: Competitor pricing is also a major influence on price setting in China

On the other side, competitor indexing is also being used to determine pricing

- In commoditized manufacturing, basing indexing against competitors is a quick and easy way to determine pricing
- For example, SGM has taken the competitor price into its pricing strategy. By analyzing customers’ price sensitivity of each service and competitors price against SGM’s price, SGM founds its price against its competitor to maximize its sales and improve profitability
- Though this methodology incorporates customer sensitivity analysis, SGM still relied on indexing high and low pricing against competitors

<table>
<thead>
<tr>
<th>Service price/competitor price</th>
<th>Number of customers</th>
<th>Sales index</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.1</td>
<td>85</td>
<td>Sales increase 94</td>
</tr>
<tr>
<td>1.2</td>
<td>70</td>
<td>84</td>
</tr>
<tr>
<td>1.3</td>
<td>56</td>
<td>73</td>
</tr>
<tr>
<td>1.5</td>
<td>46</td>
<td>68</td>
</tr>
<tr>
<td>1.54</td>
<td>45.8</td>
<td>Sales increase 70</td>
</tr>
<tr>
<td>2</td>
<td>39</td>
<td>Sales increase 77</td>
</tr>
<tr>
<td>3</td>
<td>35</td>
<td>104</td>
</tr>
<tr>
<td>4</td>
<td>33</td>
<td>131</td>
</tr>
<tr>
<td>5</td>
<td>31</td>
<td>157</td>
</tr>
</tbody>
</table>

Source: Accenture analysis
Hypothesis 5: Other countries in Asia-Pacific employ different pricing models (1/5)

With a mature industry, manufacturers in Japan are focusing on quality and service to differentiate products

Manufacturing in Japan

Industry Maturity

- Electronics manufacturing industry is mature, with a greater focus quality and innovation as opposed to low cost manufacturing
- Many electronics conglomerates, such as Toshiba and Fujitsu, have vertically integrated into semiconductor and telecommunications businesses, though smaller contract manufacturing companies still exist
- Automotive manufacturers, such as Toyota, have also vertically integrated through the value chain, though still outsource some parts manufacturing to lower cost areas

Level of commoditization

- Some commoditization in component manufacturing and semiconductor production, though technological advancement and high quality result in more product specialization
  - E.g. semiconductors manufactured in Japan and Taiwan command a higher price than ones produced in other areas due to strict product testing and quality assurances

Source: Accenture analysis, Electronic Engineering Times

Industry Attributes

- Focus on improving technology and innovation
- Engineering superiority
- High-end, differentiated products
- Quality over cost
- Global industry leaders and standard setters
Hypothesis 5: Other countries in Asia-Pacific employ different pricing models (2/5)

Example: Pricing in the Japanese Semiconductor Industry

Pricing in semiconductor manufacturing

- Industry has moved away from purely cost-based model and considering not only price setting but pricing management as well.
- Based on an Accenture survey of managers in semiconductor manufacturers it was found that:
  - There are clear organizational roles for setting and approving prices.
  - They price to customer value (due to specialization, need to treat each deal uniquely).
  - Market appears to be demand and competition lead, with the primary pricing strategy of over half of the organizations being market/competitor based (see chart below):

Survey results: Pricing strategies employed by semiconductor manufacturers

<table>
<thead>
<tr>
<th>Strategy</th>
<th>Global</th>
<th>Japan</th>
</tr>
</thead>
<tbody>
<tr>
<td>Market/competitor based</td>
<td>71%</td>
<td>54%</td>
</tr>
<tr>
<td>Value-based pricing</td>
<td>57%</td>
<td>40%</td>
</tr>
<tr>
<td>Cost-plus</td>
<td>43%</td>
<td>40%</td>
</tr>
<tr>
<td>Percent off list</td>
<td>14%</td>
<td>9%</td>
</tr>
</tbody>
</table>

Semiconductor manufacturers differentiate their products by not only ensuring high quality but also offering value-added services:

Full Service Solution:

- Product superiority (e.g. low electricity consumption, high transaction speed)
- High quality assurance through strict quality control and IP assets
- Solution oriented sales and engineering support
- Value engineering (VE) proposal to lower product cost to the customer
- Fast turnaround to ensure product is on the market before competition
- Timely sharing of product development schedule, progress, key issues with customers
- Stable supply
- Delivery support

Source: Accenture analysis
Hypothesis 5: Other countries in Asia-Pacific employ different pricing models (3/5)

Manufacturing in India is also in its development stages

Manufacturing in India

Industry Maturity
- Though India is known for outsourcing, software capabilities and chip design, the high tech and electronics manufacturing industry is not yet mature
- Popular location for contract manufacturing due to lower cost skilled labour and opportunity for global companies to hedge against country risk of manufacturing in China only
- Most high tech manufacturers are serving domestic demand for chips and components
- Foreign companies still hesitant to invest in India due to lack of infrastructure and unreliable power grid

Level of Commoditization
- High level of commoditization for generic electronic and automotive components
- Produce for more complex manufacturing situations compared to China since has R&D and engineering expertise and focuses more on value added and engineering skill based products (e.g. precision shell cast products vs. die cast products where China is the leader)

Regulatory Environment
- Ministry of Information Technology created the Special Incentive Package Scheme to encourage foreign investors to set up semiconductor fabrication and other micro and nano technology manufacturing facilities
- Government is also encouraging manufacturing by developing infrastructure, rationalizing duties and creating export-promotion zones
- Heavily bureaucratic, experienced centralized planning until the 1980’s, but has since operated as a free market

Industry Attributes
- R&D expertise and engineering skills
- High quantity of products manufactured for domestic consumption
- Low cost

Source: Accenture analysis, India Semiconductor Association, Semiconductor India, Electronic Engineering Times, Manufacturing Business Technology
Hypothesis 5: Other countries in Asia-Pacific employ different pricing models (4/5)

Example: Pricing in Indian Manufacturing

Pricing in Automotive Manufacturing
- Pricing is generally set by competitor-based or “cost +” methods, taking into consideration strategic intent around market positioning as well as inventory management.
- Since they are moving toward value added, specialty engineered parts, Indian companies are able to differentiate from, rather than compete with, companies in China manufacturing low-cost, low-quality parts and therefore can justify a higher price.

Surface Mount Technology (SMT) Equipment Industry
- Growing demand of manufactured electronics, telecom and automotive products has lead to the growth of the SMT industry in India.
- Cost-effective, skilled labour is contributing to increased operations of original equipment manufacturers (OEM) and electronic manufacturing services (EMS) companies in India, the main customers of SMT equipment suppliers.

SMT Equipment Pricing
- Continuing technological innovation forces SMT suppliers to keep abreast of the latest developments and offer the most advanced equipment at the lowest prices.
- The result is that price becomes the major differentiating factor for manufacturers.
- To combat this, some SMT equipment manufacturers have decided to price at a marginal premium by offering value-added services to customers.

Source: Electronic Engineering Times, Accenture analysis
Hypothesis 5: Other countries in Asia-Pacific employ different pricing models (5/5)

Chinese manufacturers can learn from manufacturers in other countries to improve pricing

Lessons learned from manufacturers in Japan and India

- Not all generic products are commodities
  - Focus on differentiators other than price
  - Ensure the benefits are communicated to the customer

- Recognize value-added services
  - Value-added services should be factored into the price paid for the overall solution
  - Clearly articulate differentiators that demonstrate superiority over competitors

- Incorporate pricing into the organization
  - Define clear organization roles
  - Implement organization-wide, automated systems for pricing
<table>
<thead>
<tr>
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<tbody>
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</tr>
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<tr>
<td>Transitioning to a Value-Based Pricing Model</td>
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<tr>
<td>Overcoming Challenges in China</td>
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</table>
China is no longer the lowest cost country for manufacturing

According to a global study, while China was once the lowest cost country for manufacturing, as of 2008, Mexico and India have surpassed China. China’s cost advantage has been eroding slightly as competition for skilled labour has increased wages, and transportation costs have risen as space constraints have resulted in manufacturing facilities being built farther away from main ports. Labour costs in India are on average 10-12% lower than in China. Southeast Asia (Malaysia, Vietnam, Thailand) is becoming more popular for manufacturing due to low cost, stricter intellectual property laws and lower political risk.

Source: Accenture analysis, AlixPartners 2009 Manufacturing-Outsourcing Cost Index, Semiconductor India
Chinese manufacturers are starting to recognize that they need to make a change in the way they view pricing.

<table>
<thead>
<tr>
<th>Manufacturing in China has evolved</th>
</tr>
</thead>
<tbody>
<tr>
<td>Chinese economy is becoming more open – less centralized planning means manufacturers need to make their own strategic decisions</td>
</tr>
<tr>
<td>The manufacturing industry is maturing - Chinese manufacturers are moving toward heavy industry and later stages of industrialization</td>
</tr>
<tr>
<td>Quality and technology are advancing – more manufacturers are moving from low-end, low cost goods to specialized products</td>
</tr>
<tr>
<td>Labour is becoming more skilled - engineering capabilities are improving but wages are rising</td>
</tr>
<tr>
<td>Costs are rising – Chinese manufacturers can no longer produce at the lowest cost</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Current pricing models are no longer sufficient</th>
</tr>
</thead>
<tbody>
<tr>
<td>Chinese manufacturers can no longer rely on their reputation for lowest cost, so “cost +” pricing or competitor-based models will lead to inaccurate prices</td>
</tr>
<tr>
<td>Globalization and increased export lessens the importance of “guanxi” since many clients are overseas and do not make decisions based on relationships</td>
</tr>
<tr>
<td>“Cost +” pricing is not robust enough to capture value creating services, such as engineering services and delivery support</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Pricing models will need to change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Chinese manufacturers not only have to be competitive against domestic competitors but also foreign players</td>
</tr>
<tr>
<td>Companies can no longer rely on the “easiest” or “quickest” way for pricing and must move toward the most effective way to stay competitive and maximize profitability</td>
</tr>
<tr>
<td>Chinese manufacturers must find another way to compete, aside from just lowest price</td>
</tr>
</tbody>
</table>
Table of Contents

- Setting the Context
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Chinese manufacturers can leverage different models to improve pricing capabilities

Move from…

- Primitive pricing models
  - Reactive
  - No differentiation between customer segments
  - Volume driven

- “Cost +” or competitor-based pricing
  - Based on cost + margin or indexed against competitor
  - No understanding of value to customer

- Product-level pricing
  - Pricing based on individual product only
  - May have volume discounts but added services not considered

To…

- Sophisticated pricing models
  - Proactive
  - Pricing for customer segments
  - Profit driven

- Value-based pricing
  - Recognize elements that create value for the customer and price to capture that value

- Pricing for bundles and solutions
  - Recognize value to customer of additional services
  - Price based on full solution
Chinese manufacturers will need to move from Primitive or Ad Hoc pricing models to Opportunistic and Sophisticated ones

<table>
<thead>
<tr>
<th>Descriptor</th>
<th>Primitive</th>
<th>Ad Hoc</th>
<th>Opportunistic</th>
<th>Sophisticated</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Vision / Strategy</strong></td>
<td>“Just don’t know”</td>
<td>“Just Do it”</td>
<td>“Believer”</td>
<td>“Practitioner”</td>
</tr>
<tr>
<td></td>
<td>• React if possible</td>
<td>• Follower</td>
<td>• Alignment</td>
<td>• Strategic pricing</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>• Price Optimization</td>
</tr>
<tr>
<td><strong>Price Drivers</strong></td>
<td>• Cost-plus</td>
<td>• Better Cost-plus</td>
<td>• Rules-based</td>
<td>• Buying behaviors</td>
</tr>
<tr>
<td></td>
<td>• No differentiation</td>
<td>• “Gut feel”</td>
<td>• Value Segments in place</td>
<td>• Demand, supply, expected yield</td>
</tr>
<tr>
<td></td>
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<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Financial Focus</strong></td>
<td>• Volume</td>
<td>• Revenue</td>
<td>• Shifting to profit</td>
<td>• Profit</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>• Strategic goals</td>
</tr>
<tr>
<td></td>
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<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Process</strong></td>
<td>• Person-to-person</td>
<td>• Manual</td>
<td>• Little automation</td>
<td>• Formal, rigorous</td>
</tr>
<tr>
<td></td>
<td>• Single decisions</td>
<td></td>
<td>• Decentralized</td>
<td>• Re-calibration</td>
</tr>
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<td></td>
<td></td>
<td></td>
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<td></td>
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<tr>
<td><strong>Organizational</strong></td>
<td>• Lack of clear RACI</td>
<td>• Role clarity</td>
<td>• Role clarity and supporting metrics</td>
<td>• CRO and supporting metrics</td>
</tr>
<tr>
<td></td>
<td>• Conflicting metrics</td>
<td></td>
<td></td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Systems</strong></td>
<td>• None</td>
<td>• Phones &amp; Spreadsheets</td>
<td>• Many tools, but separate</td>
<td>• Integrated</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>• Web, wireless</td>
</tr>
</tbody>
</table>

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Relying on “cost +” or competitor-based pricing can have negative implications

### Implications of “cost +” pricing:
- Product price is determined by the engineering department, not management, and may not fit into the overall company strategy.
- Cost is not always clearly defined, resulting in inaccurate prices.
- The pricing model ignores customer value and competitor prices, which means the product is usually under-priced.
- Cost drives price instead of price driving cost:
  - There is little incentive to promote cost reduction since it is easy to assume cost and margins are predetermined.
  - However, if the firm determines a price first, then there is an incentive to seek cost reductions since they would lead to an increase in margins.

### Implications of competitor-based pricing:
- Risk of price wars – competitive pricing drives down prices and margins for everyone in the industry as companies try to undercut each other to gain volume.
- Ignores customer’s willingness to pay for any potentially differentiating elements of the product or service.
- It is a reactive rather than proactive approach to pricing.
A move to value-based pricing would set prices based on the customers’ value perception rather than product cost.

### Value-based pricing:
- Price set using the customer’s perceived value of the product
- Identifies the maximum customers will pay for the benefits received from products, and portion of the value customers will cede to suppliers
- Determined through customer communication and data analysis
- Requires more effort and data accuracy than “cost +”, which is simple to implement

### Results:
- Pricing focused on customer demand
- More accurate margins
- Recognition of product elements that create value to the customer and differentiation from competitors
Bundling products and services can create differentiated offers to various customer segments, creating differentiation for seemingly commoditized products.

Product-service bundles can create unique offerings to different customer segments at different prices.

Illustrative example:

**Services:**
- Product allocation
- Order lead time
- Assembly services
- After sales support
- Technical support

**Segment 1 Offer:**
- Product A
- 2-month lead time
- Free after sales support
- Free technical support

**Segment 2 Offer:**
- Product A
- 1-month lead time
- Full assembly service
- Paid technical support

**Segment 3 Offer:**
- Product B and C
- 1-month lead time
- Free after sales support
- Paid technical support

Product bundling can also result in increased revenue and decreased cost.

Illustrative example:

1. Identify good product bundles
2. Increase revenue and profit
3. Realize cost reduction, e.g. reduced inventory

Sales before bundling

Sales after bundling

Inventory before bundling

Inventory after bundling
Companies in other industries have broken out of the commoditization trap by finding value in, or bundling services with, seemingly undifferentiated products

### Global Telecom Companies Example

**Challenge:**
- Telecom companies were selling commoditized products, such as leased lines, with no technologically differentiating factors
- Companies could only compete on price and bandwidth

**Solution:**
- Analyzed elements of customers’ value-chains and identified aspects where they could offer full solutions incorporating product, software and service
- E.g. for financial services firms required additional data protection, telcos offered solutions with added security

### US-based Global Lubricants Company Example

**Challenge:**
- Rapidly increasing raw material costs, large direct customers and competitive activities placed continued pressure on margins
- Heritage of sales-led pricing process with a focus on volume selling

**Solution:**
- Moved away from sales-led, volume based pricing principles to more value based strategy
- Adopted a segmented approach to pricing, establishing pricing by offer/channel combination

### US-based Global Silicone Supplier Example

**Challenge:**
- Products attributes undifferentiated from competitors and products could be viewed as pure commodities (bulk silicone products)

**Solution:**
- Adjusted pricing to reflect customer value-in-use and price sensitivity
- Reduced service levels to customers and segments that did not perceive value
- Charged for services not included in basic offering (e.g. rush shipments, order changes)

### Large US-based Semiconductor Company Example

**Challenge:**
- Broad product line consisting of mostly commodity; but increasingly specialized and differentiated products
- Low customer satisfaction, high inventory write offs, poor profitability

**Solution:**
- Assessment of customer attractiveness and profitability to create logical customer groupings
- Design and implementation of deal management processes including price setting by customer group
- Implemented price management software
Chinese manufacturers can learn from other commoditized industries

- Price to maximize profit, not volume
- Although the product may be the same for all customers, do not assume that all customers are the same – determine customer groups and price according to each segment’s value perceptions
- Identify value creating services to differentiate products from competition
- Create full solutions and bundles rather than selling individual products
Chinese manufacturers can apply value-based pricing and bundling to their products and services.

**Illustrative Example**

**Recall: “Cost +” pricing for car parts manufacturers**

Automotive component manufacturers pricing spare parts at a 100% markup across the board.

**Identify customer segments**
- Budget car makers
- Luxury car makers

**Identify value-creating services**
- Value engineering
- Customization
- Assembly
- Modular design
- After-sales support
- R&D services
- Delivery support
- ...

**Create full solutions for segments**
- Budget car makers
  - Value engineering
  - Modular design
  - ...
- Luxury car makers
  - Extra quality control
  - R&D services
  - ...

**Price to customer value rather than cost**

**Determine what each segment values**
- Customer surveys
- Analysis of historical sales data

**Move to more advanced pricing models**
Table of Contents

- Setting the Context
- Understanding the Manufacturing Pricing in APAC
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There are challenges facing Chinese manufacturers in making a change to their pricing strategies

**Barriers to Change**

- **Lack of information and historical data**
  - Little or no marketing data captured with customer information (only financial information kept for regulatory / taxation purposes)
  - Difficult to determine customer segmentation, price elasticity, etc. since no records kept

- **Poor abilities due to legacy of planned economy**
  - Historically, pricing, volume, etc. was determined by the state since all enterprises state owned
  - Little need for advanced marketing, sales and pricing capabilities so managers are not focused on nor skilled in these areas
  - Little history of innovation, so managers were only focused on managing costs rather than improving overall service

- **Mindset of managers**
  - Concept of “guanxi” is most important, so managers make business decisions based on relationships instead of analytics
  - “Cost +” pricing is quick and easy – they do not believe there is value in spending time evaluating pricing strategy
  - State planning meant no need for taking personal responsibility for decisions - many managers are now risk averse and will not implement ideas unless certain of success
Chinese manufacturers can take steps to improve overall pricing capabilities

**Encourage a mindset shift**
- Convince managers that change is necessary
- Demonstrate successful implementation from other geographies and industries
- Emphasize that pricing is strategic, not tactical

**Develop capabilities**
- Educate managers on marketing and sales management
- Develop capabilities in pricing models throughout the organization
- Define roles within the organization dedicated to pricing

**Implement more robust data management systems**
- Capture marketing and sales data, not just financial data
- Better understand customers to determine segmentation and value perceptions
- Use analytics in pricing decisions

**Focus on Innovation and services**
- Look beyond commoditization to see how technology and innovation can differentiate their products
- Incorporate services to create full solutions and price accordingly
Manufacturers in China can move to the next level of pricing strategy to become more competitive in an evolving industry

- Move away from viewing products as commodities
- Determine various customer segments and discover what generates value for each
- Identify value creating services
- Customize offerings and full solutions
- Determine pricing through robust models that include customer value perceptions