Negotiation Case Study >>

Using Economic Leverage to Successfully Negotiate a Price Increase

Summary:

After twice failing to negotiate a critical price increase with customers, a Fortune 50 healthcare company turned to Inside Edge, Inc., an Alliance Performance Systems strategic partner, to identify the issues derailing the negotiations and to develop a successful solution to the problem. A thorough analysis revealed the company's sales professionals were routinely giving in on price or terms because they were not effectively trained to:

- Identify an economic leverage position (ELP),
- Manage critical moments, or
- Pinpoint and consider customer interest.

With these issues identified, the Fortune 50 company asked Inside Edge to develop and implement a customized version of its proprietary negotiation training program. Inside Edge Negotiation is specifically designed to give sales professionals the skills they need to avoid making mistakes that frequently derail negotiations and reduce profit margin. The program combines instruction in the foundations of negotiation with real-world, strategic practice that emphasizes using economic leverage positions to achieve win-win negotiations.

Inside Edge Negotiation helped make the third time the charm for this Fortune 50 healthcare company. The company's sales force used its newly-acquired skills and knowledge, and the confidence those skills and knowledge bred, to successfully negotiate the price increase with 97% of the customer base.

The Issue: Company Makes Two Unsuccessful Attempts to Negotiate Customer Buy-in for a Price Increase

Faced with rising costs and falling margins, a Fortune 50 company operating in the healthcare marketplace determined it was time to pass some of its increased cost on to customers. Cognizant of the financial pressures customers faced in a slow economy as well as the low costs to switch to competing firms in the sector, the company developed a three-step plan to introduce its new pricing to customers. First, the company sent a letter to customers detailing the business reason for the coming price increase. Second, the company met with its sales force to review the letter and the business decision. Third, the company deployed its sales professionals into the field to further explain the price increase to the customer base.

The push back from customers was nearly universal. Though the company's sales professionals empathized with their customers and explained the price increase was linked to pricing moves made by suppliers, customers vocalized their displeasure. Worse yet, a number of major clients threatened to switch to the competition if the company implemented the new pricing model. The backlash from the marketplace forced the company to abandon its plan—not once, but twice.

The Analysis: Sales Force Commits Three Critical Negotiation Errors

Frustrated by its inability to push the price increase to market, the Fortune 50 company turned to the Inside Edge team of negotiation experts for help. The team conducted an in-depth analysis of the company's strategy and the current marketplace to find out what was derailing the price increase negotiations. Three critical mistakes rose to the top. Sales professionals, the team reported, had not identified a position of economic leverage, had not managed critical moments, and had not pinpointed and considered customer interest.

Mistake #1:
Not identifying and developing an economic leverage position (ELP)

The Fortune 50 company's sales professionals approached the price increase negotiations with their clients as apologies instead of business discussions. The apology is a classic fallback tactic for novice negotiators worried that "bad news" will sour their relationships with clients. Unfortunately, apologies rarely move customers because customers are focused on how change impacts their situation, not the seller's situation. In this case, most customers responded to the price increase explanation with variations of these four words: "That's not my problem."

Sales professionals who approach negotiations as business discussions strive to calculate the true value of the products, services, and other intangibles their company provides to each client. Inside Edge calls this true value the economic leverage position, or ELP. The ELP is calculated by reviewing customer data and metrics, and it is much more than a number. Because the ELP turns intangible benefits (like the claim that the product or service reduces medical errors) into economic drivers that matter to the specific customer (like the fact that reduced medical errors will save the customer $500 million every six months), it gives the seller a point of leverage in the negotiation. The ELP can turn a conversation that begins like this:

> *"Bob, I'm really sorry. You are a great customer. You do a lot of business with us. That's what makes this so difficult, but I've got to pass a price increase on to you. I really have no choice; our suppliers are raising our costs. I hope you understand."*

Into a conversation that begins like this:

> *"Look, Bob, in the next cycle, we are going to increase the prices on certain products. If you let me review your product mix data, I think I can put together a proposal that will save you money or, at the very least, be cost neutral for you."*

The second conversation, which is ELP driven, increases the odds of achieving a win-win. In the case of this Fortune 50 company, sales professionals would have been more likely to achieve a win-win if they had used customer data to illustrate how specific clients could lower overall cost and negate the impact of the price increase simply by purchasing in greater volume from an expanded list of the company's product lines. Of course, in some instances, a win-win remains difficult to achieve because the client objects even after being presented with the ELP. If this occurs, the seller can still use the calculation as a benchmark to identify just how much room he or she has to give on price or terms. This type of guidepost is critical to protecting profit margin, since, as reported in a McKinsey study of Fortune 1000 companies, a 1% reduction in price translates into an 8% reduction in operating earnings.

Negotiation Case-in-Brief: Aviation Services Company Embraces ELP

A leading aviation services company faced a major challenge negotiating sales of its core product, aircraft engines. The company believed its engines outperformed competing engines in three major categories: duration of life, maintenance needs, and fuel efficiency. The company priced its engines to reflect these benefits. Unfortunately, account mangers found it difficult to get potential customers to look past the expensive price tags. Though account managers told customers the engines lasted longer, had better maintenance records, and burned less fuel than competing engines, customers remained focused on price.

Driven to boost the sales force's negotiation success rate, the aviation services company contracted with the Inside Edge Negotiation team. The team showed the company's sales professionals how to calculate economic leverage position (ELP) and use it to shape conversations with potential customers. Using ELP, account managers were able to put numerical values on the cost savings associated with what the customers had considered intangible benefits of the company's aircraft engines. Since the engines saved customers money associated with repair and fuel, they were, for many customers, less expensive investments than competing engines with smaller price tags. This aviation services company recently used the Inside Edge Negotiation framework to close the largest aircraft engine deal in its history.

Mistake #2:
Not managing critical moments

The Fortune 50 company's sales professionals did not prepare effective strategies for the crucial junctures in the conversation that are most likely to influence the outcome of the negotiation. Inside Edge calls these junctures "critical moments." Sellers can encounter a variety of critical moments in any single negotiation. One of the most common occurs when the customer presents a competing offer as leverage during the conversation. For example, the customer may tell the seller, "Company X met with me last week and made the same offer you just made me, but the price is 4% less."

When a critical moment like this occurs, the next words out of the seller's mouth generally determine the outcome of the negotiation (i.e., whether the seller will make any margin on the sale). If the seller has not prepared an effective strategy, he or she will likely say something like, "Let me see what I can do," or "Let me run that by my boss." Novice negotiators, like the sales professionals at the Fortune 50 company, think these noncommittal responses hold ground and give them time to develop reasonable solutions to customer issues—solutions that will protect their firm's position. But, in reality, these responses tell customers that the seller has room to give on price or terms. Customers who witness this tapdance will be inclined to ask for more rather than less.

On the other hand, the seller who has effectively prepared for critical moments can protect margin in these situations. This type of professional negotiator might respond, "Well, of course our competition would offer those terms when they can't offer the same value proposition we can." Then the seller can launch into a discussion of the true value of his or her product, services, and other intangibles—elements already uncovered during calculation of the ELP.

Negotiation Illustration: Jaguars, Fords, and Critical Moments

A customer walks into a Jaguar dealership and test-drives a new luxury sedan. The customer enjoys the drive and is interested in purchasing the car. He sits down to negotiate with the Jaguar sales professional, who begins the conversation by saying the car costs $85,000. The customer objects to the price and introduces a point of leverage. He says, "I was just at the Ford dealership down the street. The Ford sales rep is prepared to give me a heck of a deal on a Taurus. You need to rework the numbers if you want to make this sale happen."

This absurd scenario underscores the importance of how sellers handle critical moments in a negotiation. The Jaguar sales professional is never going to respond, "That's some deal on the Taurus! Let me see what I can do." She knows the true value of her product, and the Taurus isn't in the same value class. To make the sale, she will focus on explaining the Jaguar's economic leverage position (ELP) to this naïve, hypothetical customer. She will not give in on price or terms. And she is an example for all sales professionals who have figured the ELP for their solutions. They should never indicate they could give in on price or terms, even if their ELP is less obvious than the ELP in this scenario.

Mistake #3:
Not pinpointing and considering customer interest

The Fortune 50 company's sales professionals had limited understanding of the foundations of successful negotiation, particularly the Harvard Negotiation Project's principle of getting beyond position to interest. As a result, they made no attempt to identify and address the core needs driving each customer's objection to the price increase. Instead of exploring how their company could help meet customer needs overall, the sellers only discussed whether the price increase was justifiable—a debate they could not win.

Knowledge of core customer interest, which customers themselves may not be able to clearly identify or articulate, is a vital ingredient in any seller's recipe for a successful negotiation. Once this interest is identified, sellers can use it to shape a position that is more likely to generate customer acceptance. The Fortune 50 company's sales professionals had not received the training necessary to pinpoint customer interest and use it to position the price increase as a win from each customer's point of view.

Even if these sellers had taken a course in negotiation, they probably would have been just as unprepared to accomplish this complex task. Why? Because few negotiation training programs actually show sales professionals how to identify and effectively utilize customer interest. These programs may provide questioning tips and tools to uncover it, but they fail to provide an easy-to-understand, replicable formula for asking questions. Such a formula will lead customers to communicate bits of information that reveal their true motivations. Inside Edge calls these bits of information "flares." When sales professionals can identify flares to pinpoint customer interest and use that knowledge to shape their position, they become smart negotiators.

Negotiation Case-in-Brief: Leading Biotech Uncovers Customer Motivations

Sales professionals at a leading biotechnology firm found that customers were unhappy with the price of one of its core products. The drug, customers said, was too expensive. If the company did not reduce the price, they would discontinue its use. The biotech was determined not to reduce price and margins, and its sales professionals did not panic. They had successfully completed Inside Edge Negotiation training. As a result, the sellers focused on uncovering the customers' true motivations. They used the Inside Edge formula to ask questions designed to surface flares. And, when they did this, they learned customers were not truly concerned about price or costs. Instead customers revealed, "We are spending too much on drugs overall."

Armed with the knowledge that a reduction in overall drug spend would be seen as a win by customers, the biotech's sales professionals worked with individual customers to review the way their organizations were using the drug. The goal of this analysis was to identify flaws and inefficiencies in drug utilization. Once these issues were spotted and corrected, the customer was able to reduce overall drug spend without demanding the biotechnology company lower its price. The company's sales professionals, trained using the Inside Edge Negotiation model, had successfully achieved a win-win.

The Solution: **Sales Force Embraces "Inside Edge Negotiation"**

After reviewing the in-depth analysis, the Fortune 50 company asked Inside Edge to implement a solution. This solution was Inside Edge Negotiation, a proprietary training program designed to introduce participants to the foundations of negotiation and also provide guided, strategic practice—practice that includes learning how to calculate economic leverage positions (ELPs) for customers. Inside Edge Negotiation is always customized to the client's needs and marketplace. In this case, the Fortune 50 company had two overriding goals for the program:

1. Prevent sales professionals from making the three mistakes that derailed earlier negotiations, and
2. Prepare sales professionals to go out a third time to successfully negotiate customer buy-in for the price increase.

The customized program developed for this Fortune 50 company began, as most versions of Inside Edge Negotiation do, with an introduction to negotiation concepts and skills. One integral element emphasized during this phase of the training program was the formula participants could use to uncover their clients' true motivations. Sales professionals can use this easy-to-understand formula to surface flares by asking customers questions from three different angles.

The second and most intensive phase of Inside Edge Negotiation customized for this company focused on preparing its sales professionals for the real-world negotiation they were about to tackle. Inside Edge experts assembled the sales team for an "All Hands on Deck" workshop. During this workshop, participants learned how to calculate the ELP for their clients and use that information to articulate a win from the customer's point of view. Next, sales professionals practiced for the real-world negotiation—the actual price-increase conversations they would have with customers, not simply conversations built around generic case studies. The real-word practice was videotaped and evaluated on site, with both peers and Inside Edge experts offering immediate feedback designed to help participants hone their negotiation strategies. The process also allowed the company to develop a very consistent, Marketing-approved message all members of the sales force could use to shape their negotiations with individual clients.

The Outcome: **97% of Customers Accept Price Increase**

After completing both phases of Inside Edge Negotiation, the Fortune 50 company's sales professionals approached their third effort to negotiate a price increase with extreme confidence. Their mission was to articulate a win from the customer's point of view, and they had acquired the skills and completed the practice to do just that. These sellers now understood the economic leverage position (ELP) for each of their clients, which meant they no longer had to resort to apology tactics. They had prepared strategies to manage critical moments in the negotiations. As a result, when customers raised important issues, the sellers did not make the mistake of immediately giving in on price or terms. Instead, they examined the true value the client derived from the company's products, services, and intangibles. In addition, the sellers were able to pinpoint customer interest and shape positions that generated customer acceptance because they could rely on a formula for asking effective questions.

The preparation and the confidence it bred served the sales professionals and the Fortune 50 company well during the third mission to negotiate. 97% of the once vocally displeased customer base accepted the price increase. The company did lose a handful of customers, but calculations had already proven these customers were some of its most unprofitable. Today, this Fortune 50 company has embraced the Inside Edge Negotiation framework. The sales force routinely calculates ELP before any negotiation, and sales leadership always schedules an intensive strategic practice workshop (i.e., an "All Hands on Deck" meeting) prior to any major negotiation.

To find out more about Inside Edge Negotiation, contact Peter Pisarri, Senior Vice President of Client Development for Alliance Performance Systems, at: ppisarri@alliceperformance.net or call (941) 766-0058.