



EXECUTIVE SUMMARY

The task of achieving optimal pricing in the automotive and equipment parts industry can be quite challenging.

Market-based pricing techniques---even with perfect information about competitor prices---are an attempt to meet the challenge. However, recent research conducted by PROS for an auto parts manufacturer indicates that

new tools and techniques are required to overcome what can be described as a “market-based pricing credibility gap.”

This gap occurs because current methods of using only competitive data to determine a “market-based” parts price are incomplete and inadequate to the task. As a result, many parts manufacturers and distributors are experiencing far more uncertainty in market-based pricing analysis than they might initially realize.

This also increases the likelihood that they are not optimizing prices for profitability, and it poses a greater risk that they are wasting money on competitive pricing research.

To close the “market-based pricing credibility gap,” professionals today must explore new methods for pricing parts that incorporate more comprehensive scientific methods and automation through advances in software technology.

MARKET-BASED PRICING METHODS USING AVERAGE COMPETITIVE PRICE DATA

Over the past several decades, automotive and heavy equipment parts manufacturers and distributors have come to categorize their parts as either highly competitive, competitive, or captive.

A commonly recognized rule of thumb is that the highly competitive parts and competitive parts (typically 20%-30% of total inventory, combined) generate

approximately 80 percent of revenue and are therefore very important to overall sales and profitability.

For the sake of efficiency, many pricing professionals have focused on that percent of parts that generate the vast majority of revenue, often using a market-based pricing approach. One common way to conduct market-based pricing is by using competitive pricing data (either purchased from a third party or compiled internally) of actual price points of competitors’ parts in the market.

The logic behind this market-based pricing approach says, “if you want to price to the market, you should price to the average competitive price” for each part. In other words, if the part you manufacture has three different competitors manufacturing the same part, your task should be to determine the price of each of the three, take the average, and then set average as the base metric for pricing your part. If you believe the part should be priced at a premium, set the price above the market-based average. Likewise if you think the part should be sold at a