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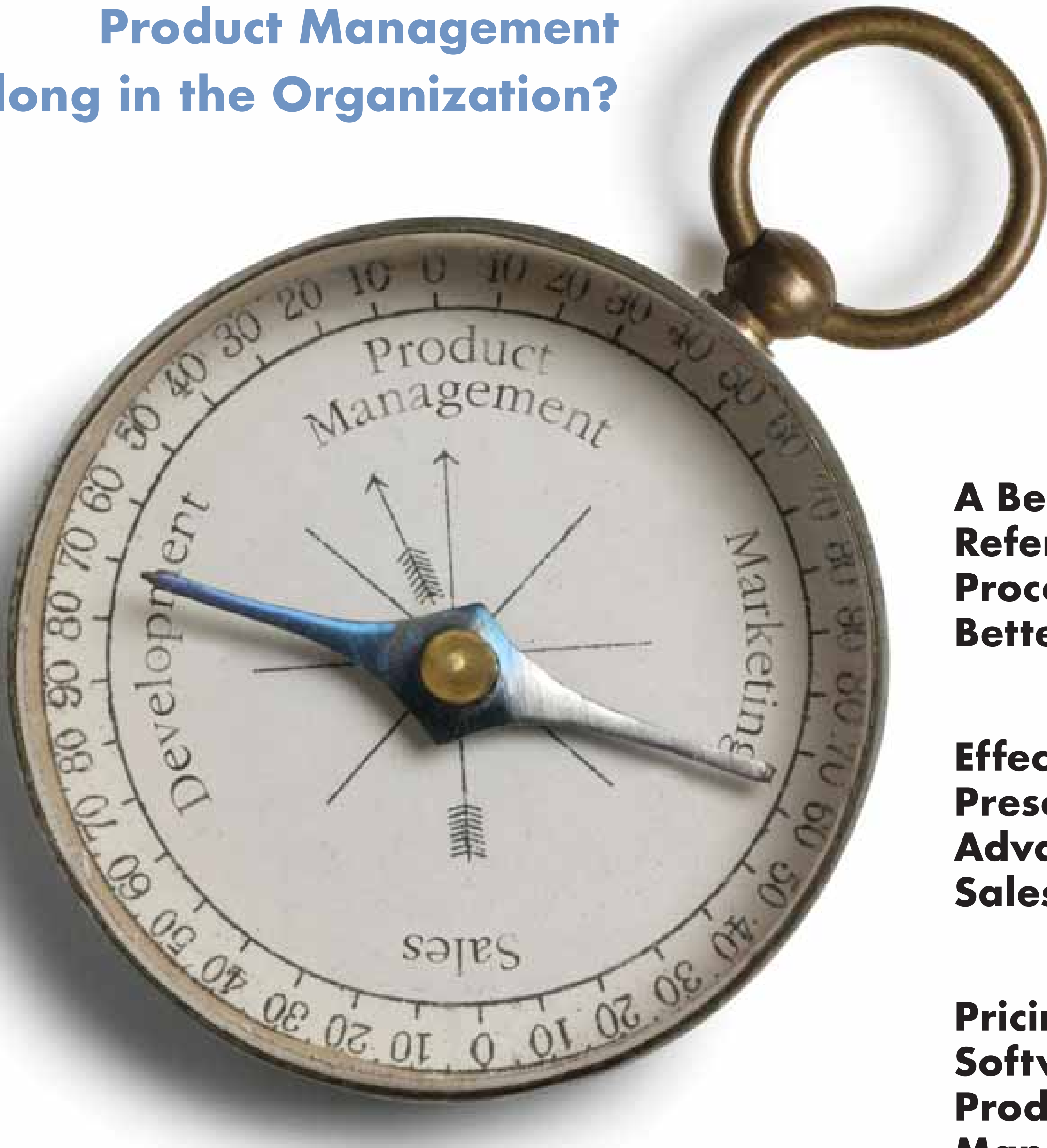
## Where Does Product Management Belong in the Organization?

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Pragmatic Marketing, Inc. was formed in 1993 to provide product marketing training and consulting to technology firms by focusing on strategic, market-driven techniques. Pragmatic's training courses emphasize business-oriented definition of market problems, resulting in reduced risk and faster product delivery and adoption. Since its inception, Pragmatic Marketing has successfully graduated over 30,000 product managers and marketing professionals. For more information, visit www.PragmaticMarketing.com or call (480) 515-1411.

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# Where Does Product Management Belong in the Organization?

*By Steve Johnson*


Product Management is "messenger of the market," delivering market and product information to the departments that need facts to make decisions. That is why it is not surprising that 23% of product managers report directly to the CEO, acting as his or her representative at the product level. Yet many organizations subordinate the job under one of the other VPs:

• 13% are in Development or Engineering

• 25% are in the marketing department

• 8% are in a sales department

In effect, subordinating Product Management relegates it to a support role for the primary goal of the department. Vice presidents and department heads have a natural inclination to support their primary department. The VP of Development has a primary responsibility of delivering products, so he tends to use product managers as project managers and Development gofers. Product Management soon evolves into a group of Gantt chart experts—project managers. The VP of Marketing owns collateral, sales tools, lead generation, and awareness programs. So this VP uses product managers as content providers to Marketing Communications. And the VP of Sales, focused on new sales revenue, uses product managers to achieve that goal: product managers become "demo boys and demo girls" who support sales people one deal at a time.

As our companies grow larger and become more mature, the company president needs someone thinking about the product we *ought* to be offering, new markets we could serve. The company president needs someone thinking about the future of the product. We already have people focused on product, promotion and place. Who—if anyone—is identifying *market problems* for the next round of products? Who is the VP of market problems? And what results does the president want from Product Management? ➔

Increasingly we see companies creating a VP of Product Management, a department at the same level in the company as the other major departments. This VP focuses the product management group on the business of the product. The product management group interviews existing and potential customers, articulates and quantifies market problems in the business case and market requirements documents, defines standard procedures for product delivery and launch, supports the creation of collateral and sales tools by Marketing Communications and trains the sales teams on the market and product. Product Management looks at the needs of the entire business and the entire market. Product managers should never be involved with one customer or one salesperson.

Recognizing that existing and future products need different levels of attention, some companies split the product management job into smaller bits: one group is responsible for next year's products while another group provides sales and marketing support for existing products. These companies often add a product marketing component to the marketing communications effort, supporting them with market information and product content. As we grow ever larger, the product marketing role expands further: we still need a group defining our go-to-market strategy and providing content to Marketing Communications, but now we also need more marketing assistance in the field. So field marketing is born: product marketing people in the sales regions create specific programs for all of the sales people in a given geographic area.

As companies grow, the product management role entails three or four functions: product strategy, technical product management, product marketing and field marketing. It is a big job. In a small company, all of these functions are performed by one person. In large companies, they are performed by four departments. But they are all part of product management.

Yet when we hire a new product manager, one of two things happen quickly: the product manager imposes some well-needed discipline, helps the company run like a business and becomes a respected member of the product team. Or the product manager becomes the source of the best demo and is rarely effective in any other role.

Product Management's reporting structure corresponds to the results the company can expect from Product Management. In Development, product managers shepherd the development projects; in Marketing, they provide technical content; in Sales, they become demo boys and girls.

If you want better products in the future, if you want a messenger for the market, Product Management should have a seat at the senior executive table; you need a VP of Product Management.

# Why we need to evolve from ST:TOS to ST:TNG

I have found that the key to success in technology companies is an understanding of Star Trek. Most engineers, developers, and technical people are familiar with these characters. Perhaps the Star Trek characters are most familiar because we work with them every day. The characters of Star Trek give us the typical personas in a technology company.

If you were not a fan of Star Trek and need to get acquainted quickly, go rent the movies numbered II, IV, and VI. If you never watched ST:TNG, you'll also need to get Star Trek: First Contact or Star Trek: Insurrection. Now you're reasonably up-to-speed on both series. With Star Trek fresh in your head, consider your company.

## Is your company The Original Series or The Next Generation?

Of course, everyone can equate Spock with the typical developer: quite logical without emotion, using facts and reason to draw conclusions. Spock is willing to spend hours on a problem despite pressure to make a quick decision. As we saw in Star Trek IV (the one with the whales), Bones implored Spock to make a guess. Spock: "Guessing is not in my nature." Yet in many cases, a development "guess" is adequate to make decisions.

Unfortunately, sales people are often like Captain Kirk: action without thought, asking for the impossible and frequently violating the prime directive. Meanwhile, Dr. Leonard "Bones" McCoy is like many marketing people: emotion without logic, frequently complaining about what they aren't: "Damn it, Jim. I'm a doctor, not a bricklayer." Thankfully, we have Scotty as a stand-in for our sales engineers or field consultants. Scotty initially tells Kirk that whatever he wants is impossible and fifteen minutes later, says, "Okay, you've got warp drive."

Where is the president in all of this? Back at Starfleet, without a clue of what is really happening in the field. Alas, in many companies, the sales people are running the show; the VP of Sales is really the COO.

As our company grows, we need to evolve to be more like Star Trek: The Next Generation. Here we have Captain Picard, acting as our president; Commander Riker is our sales people. Data, in the development role, continues to use logic, as Spock did, but attempts to understand the human elements of man, as Spock rarely did. Beverly Crusher, in the marketing role, is a good doctor, as was McCoy, but she also understands the business of the starship, can and does serve as an executive officer with understanding of all roles, and uses scientific metrics to evaluate the health of the crew.

In "Relics" (Episode #130, Season 6) Scotty has survived for three quarters of a century by keeping himself suspended in molecular limbo in the ship's transporter system. When he and Geordi La Forge attempt to work together, Scotty listens in horror as Geordi delivers an accurate assessment of the situation to Captain Picard and Commander Riker.

SCOTT: (Shocked) "Ye didna tell him how long it was really going to take you?"

GEORDI: (irritated) "Of course I did."

SCOTT: "Oh... Laddie. You've got a lot to learn if you want them to think of you as a miracle worker." *

Here is the difference: Picard can be trusted with accurate information while Kirk cannot. Picard never makes promises that his crew cannot keep while Kirk frequently does. And the crew knows it… in both cases. The "old school" acts more on instinct and hope while the next generation acts on procedure and knowledge.

Is your company like the Next Generation or stuck in the Original Series?

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*source: http://www.twiztv.com/scripts/nextgeneration/season6/tng-604.txt

# A Better Reference Process

The Director of Public Relations (PR) has just finished informing the executive management team that there is no way this launch will be a success without customer references. He has fewer than six reporters who want to speak with customers about the new features. The Director of Industry Analyst Relations (IAR), attending the meeting as well, chimes in that there are four industry analysts who want to speak with customers. Even the normally-sedate Director of Investor Relations (IR) is expressing frustration that there are no customers available to speak with stock analysts about the merits of the new features touted on the past three earnings announcement calls.

These people, whose job it is to influence the company's key influencers—the press, industry analysts, and stock analysts—do not have what they need to be successful. They need customers to speak with these key influencers to validate the product's claims so that the company will 1.) get "ink" on the new product in target publications, 2.) have industry analysts recommend the products to the target market, and 3.) have sell-side stock analysts recommend the company's stock, and for the buy-side stock analysts to buy it.

Who is to blame for the shortfall in customers willing to participate? "Not me," according to the beta manager. He sent the product marketing manger a spreadsheet of customers who said they would be a reference. The product marketing manager sent it to the customer reference manager. "No one followed up with the customers," the product marketing manager continues. The product marketing manager claims he did his job: "I told the customer reference manager to follow up with numerous customers who are really excited about the new feature set."

And then there is the customer reference manager who told the beta team manager that all of the customers in the beta program have policies against public reference activities. "Why didn't you follow up with the customers I recommended—the ones we know will provide a quote and speak with the media?"

This is a not-so-uncommon scenario, with fingers pointing in every direction except inward. It is painful for everyone.

Long before the launch, the launch team must determine:

- How many customers are needed to support a launch
- A starting point
- What it takes to secure customer participation in order to pull off an effective, customer-focused launch

## Define customer requirements

It is important to know precisely how you want customers to assist you with your launch so that you can clearly communicate the request to customers. Your customer likely needs approval from his manager and his corporate communications group. Your communication should take into consideration the customer's ultimate approvers. Launch activities are straightforward and include:

- Quotes in a press release
- Quotes for general marketing purposes such as web, collateral, presentations
- Interviews with media, industry analysts, and stock analysts

# Means Better Launches

*By Amy Perkel*

## How many participants do you need?

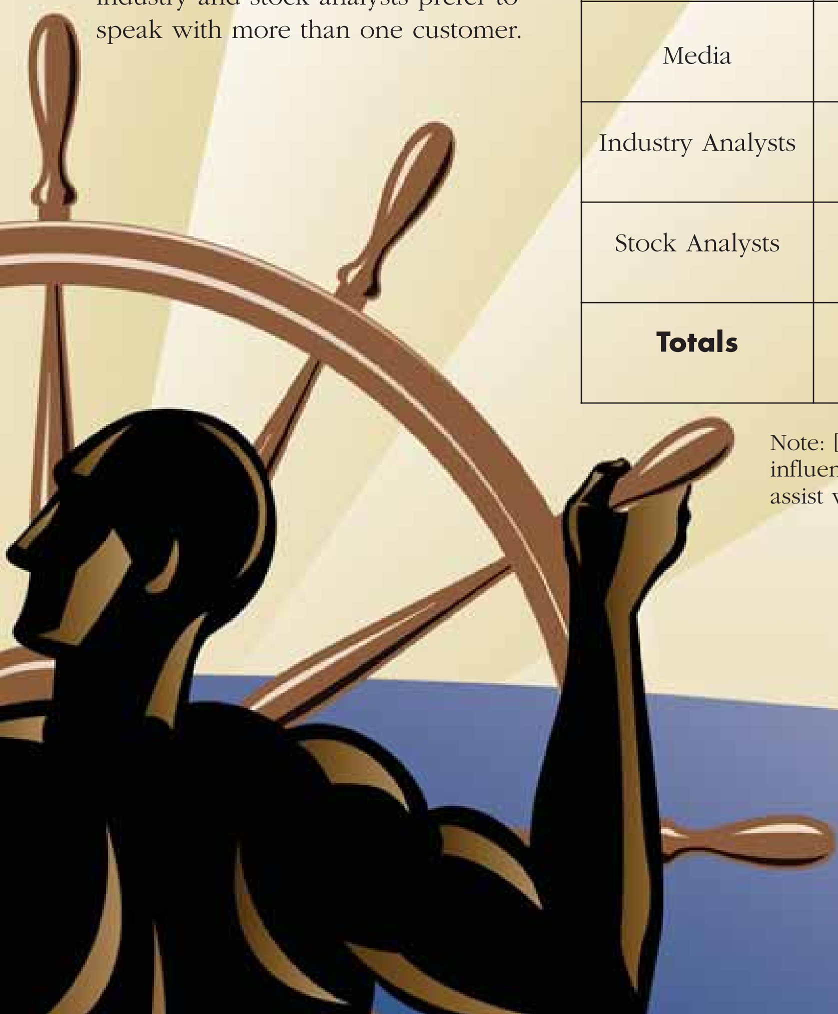
Do you have two references? Or 18? How many do you need? The first step in determining how many customers you need for launch support is to ask the PR, IAR, and IR managers how many people they will be briefing. The assumption is that all who will be briefed will want to speak with one customer, if not two or more. The PR manager might brief five reporters, the IAR manager might have three analysts who will want to speak with customers, and the IR manager two stock analysts who will want to speak with customers. Generally, one customer interview is sufficient for a reporter; however, industry and stock analysts prefer to speak with more than one customer. Let's assume two. Given these circumstances, the key influencers will want to speak with 15 customers.

It is unrealistic to expect a customer to do more than two interviews with any combination of reporters or analysts, owing to people's busy schedules. And it is not uncommon for a customer to participate in only one interview. Based on the scenario above, a company would need seven customers willing to speak to the merits of the new product's features—assuming the customer is willing to speak with two interviewers of any sort. It is important for the PR, IA, and IR managers to recognize that there is a limited pool of available participants, so they need to prioritize their analysts and provide fewer references than they requested. ➔

### Launch-related customer interviews needed to satisfy key influencers

| Reference requests | No. of key influencers per launch | No. of references needed per influencer | No. of customer interviews needed |
|---|---|---|---|
| Media | 3 - 6 | 1 | 3 - 6 |
| Industry Analysts | 2 - 4 | 1 - 2 | 2 - 8 |
| Stock Analysts | 2 - 3 | 1 - 2 | 2 - 6 |
| **Totals** | **7 - 13** | **3 - 5** | **7 - 20** |

Note: [1] This chart is a guide and may vary depending on number of influencers your company engages; [2] assumes customers likely to assist with one and no more than two interviews of any combination.



## Allow ample time

Recognize that getting customers to publicly endorse your products is a multi-touch process that takes weeks, if not months. It is critical to factor in enough time for the customer reference manager to secure customers participating in the launch. Customers are as busy as you and often their objectives are not the same as yours.

Remember that your customer's manager, who needs to sign off, has a busy schedule as well. And your customer's PR manager has her own objectives that are not your customer's and certainly not yours. For all of these reasons, allow ample time for getting approvals. A two-week approval period is very aggressive. Most customers cannot come back with approval so quickly. Allow at least one month or a full quarter.

## The reference program

The customer reference business is a numbers game. For many companies, corporate policies simply do not allow customers to publicly endorse products, for a myriad of reasons.

One great source of references is the product beta program. While the primary role of the program is to test the product in customer environments, it can also generate references from your early adopter clients.

With that said, you should assume that at least 30% of your customer base, which includes Beta program participants, is not allowed to engage in public-facing reference activities—including a quote in a release and speaking to media. The financial services and insurance industry have very strict policies and may not even allow a name mention. A number of major retailers—with very strong brands—protect their brand very closely. It may still be possible for customers at these companies to speak with industry or stock analysts since interview notes are not published, so it is worthwhile to ask. But in terms of a public endorsement, look elsewhere.

There are a number of companies able to assist with public-facing reference activities, but have policies against speaking about a product that is not production; i.e., they do not want to risk endorsing a product that has not been fully implemented, or has not been in production for a certain period of time. Even if such a corporate policy is not in place, some individuals are reticent to endorse a product until it is implemented. Conservatively, that cuts another 10% from your beta program, leaving 60% of the pool of beta participants who can possibly participate.

The funnel continues to narrow. A certain percentage of people will not be pleased with the features in your new release. Let's say that equates to 15%. A certain percentage will drop out of the beta program because they did not have the time to participate. Let's say that equates to 15% as well. You are now left with 30% of your beta participants who may be able to assist.

Even those in the 30% pool who do participate may be too busy to assist, as noted above. I would put this number at 15%, leaving approximately 15% of your beta participant pool who may be able to assist. If there are 100 people in your beta program, you are in good shape. However, if you have a smaller beta program of 50 people, only 7.5 people are likely to assist!

Customer reference people know these ratios and have experienced them first hand but it is hard for many people involved in the launch process such as PR, Product Marketing, the Beta team, and certainly executives, to recognize this.

Determining the number of customers you want in the beta program who will support you in the launch is a straightforward mathematical equation. If you need seven customers to speak with your key influencers, and you know approximately 15% of the people in your beta program will be willing and able to assist, then you need nearly 50 people in your beta program.

## Seed your program

Getting to this point—knowing which of the 7.5 customers can publicly endorse your product—is time consuming. Keep in mind that a "yes" given to the beta manager

### Estimate of beta customers willing to assist public reference activities

| Reasons for not assisting | Eliminated | Remaining pool |
|---|---|---|
| Policies prohibit | 30% | 70% |
| Policy requires completed implementation | 10% | 60% |
| Dissatisfied with features | 15% | 45% |
| Dropped out of beta program | 15% | 30% |
| Willing, but too busy | 15% | 15% |

does not necessarily mean yes. It is certainly a good base to start from, but not all willing customers know if their corporate policy prohibits PR and media participation of a vendor's launch effort. Further-qualify your potential "yeses."

You can count on the customer reference manager spending an average of one hour per customer in

- initiating customer contact by phone and email
- subsequent follow up if you do not reach them in person
- recording communication notes

A product beta program with 50 participants equates to a week and a half's worth of work. The 50 hours occurs over several weeks, as it takes that long for your customers to respond.

You can now see the value in truncating this process. And the best way is to seed the program with people you know can help, based on their knowledge of corporate policies. The customer reference manager is the person to recommend these people. It is very important for the beta manager to closely monitor the progress of these customers.

If some of your best references are too busy to participate in the beta program, you want to provide a mechanism for them to learn about new features. Arrange a webcast where the product marketing manager covers the product's new features, and the customer reference manager explains and invites customers to this event.

## Don't skip approvals

Your customer likely will need to get approval from management, and if you are asking for a quote in a press release or customer willingness to speak with the press, permission from their PR manager is necessary. Do not overlook this step. It is important to let your customers know in advance that public-facing activities like a press release and media interview require their company's corporate communications approval. This adds a lot of time to the approval process. One well-known vendor requires 13 weeks for a quote to be approved by all the involved departments. But don't take shortcuts. Here is why.

Shortcuts generally result in a few unsavory outcomes:

- your customer will get admonished by upper management
- your PR team will get a call from your customer's irate PR team and/or an irate customer executive
- your customer will tell you at the last minute that they cannot assist because their corporate policies do not permit such participation

In any of these scenarios, you have likely lost this customer as a reference for good.

This brings us to the scenario of when executives are dissatisfied that there are not enough "big name" companies supporting the launch. Your CEO will want to know why, for example, there is not a quote from Big Name Company XYX in the release. You have heard directly from the account manager, the customer, and his PR manager that Big Name Company XYX will not provide a quote in the release. Corporate policies at some companies are so strict that not even a name mention on a website is allowed. Accept that some companies do not allow endorsement of vendors, and turn your attention for launch support to the customers who will assist.

## Pave the way

Proactively provide all the information your customer, his manager, and his PR manager need to make a decision as quickly as possible. This means crafting a detailed email that states exactly what you are asking for and when. Further, the PR and product marketing mangers should draft the quote that they want the customer to approve. The customer reference manager will tell the customer that this is the ideal quote as drafted by PR and product marketing, but the customer should feel free to tailor it to reflect his environment.

Also, remind the PR and product marketing managers not to get too wrapped up in their messaging. Most people, and in particular your customers, do not talk in messaging. If customers make tweaks to your quote, or even radical edits, so long as they are generally on point, accept the edits. Why? Because that likely is the only way you will get a quote approved by that customer.

Work directly with your customer's PR whenever possible, although it is OK to work through your customer if that is what the customer prefers. Find out how the customer's PR team likes to be engaged. Are they OK with their employees speaking directly with the press? Or do they require a PR person to join the call? Some PR groups require in advance the questions the reporter is likely to ask. Or, the customer's PR manager may require any copy to be reviewed. Many reporters will not allow this, so that requirement generally rules out that customer for media opportunities.

Finally, find out how the customer should be alerted to the media opportunity once it arises. Should you call and/or email? Should you send it to the customer and PR manager? ➔

## Ensure no trouble with the media

The worst case scenario would be your customer speaking negatively about your product to the media. We all assume customers who are a part of the beta program are pleased. The customer reference manager should double-check this. And be direct! The customer reference manager should tell the customer we assume they are a happy customer, as confirmed by the beta manager, account manager, or other such party.

If you are not familiar with this customer, you should directly state in a polite fashion that bringing up any product issues with the media is not ideal. You can even express embarrassment at having to say that, but to avoid mishaps, be direct. The customer reference manager needs to directly state and hear that this customer will be suitable to speak with the media.

While some customers are perceived as better references than others in that they are particularly well-spoken and excellent communicators, do not rule out those who are more understated. Assuming they have a good story to tell that meets the writer's requirements, they should make a fine reference. In general, the only customers to rule out are those that are "hot and cold" or unreliable.

## Schedule time slots for media interviews

In order to ensure getting "ink" on what your customers have to say about your new product, secure two to three time slots of 30-minute increments on your customers' calendars multiple weeks in advance of the expected time that reporters will want to speak with your customers. This may seem overzealous, but if you want to ensure your customer's schedule is free, this is the recommended approach. Reporters are usually on deadline with a small window of free time.

To make this work, the PR manager needs to tell the customer reference manager when they will be briefing reporters, and when they expect the reporters will want to speak with customers. They all have publishing deadlines, and your PR team should know them. While the PR and product marketing teams are briefing reporters during the media tour, you can be sure reporters will want to speak with your customers. By arranging time slots with customers in advance, the PR manager can ask the reporter what times work best, then share that information with the customer reference manager, who will confirm the pre-agreed time slot with the customer.

## Thank your customers

You need your customers' help to make the launch a success. Let them know the importance of the activity: "In order to be successful, we need to have our customers let our key influencers know that what we are saying is validated by you, our customers." And when customers agree to assist you, genuinely thank them. Thank the customers who are unable to assist as well.

Is it common for customers to ask for something back in recognition of their participation? In general, the best references do not expect anything in return. They are willing to assist for a variety of reasons:

- a general willingness to be helpful
- a love of the product because it is integral to their success
- pride in what they have accomplished using the product
- the desire to showcase their success

A few customers recognize the symbiotic relationship between customer and vendor. In order for a vendor to sell more products, it needs existing customers to publicly state the merits of the product. A successful, revenue-generating company is then

able to pour additional funds into development, so that customers continue to get excellent products. When a customer vocalizes this relationship, you know you are working with a very helpful reference.

Numerous problems may arise if you compensate customers for reference activities. First, you may run into a tit-for-tat scenario. A customer may require you to compensate them for every activity. This means that your marketing people need to have good negotiating skills, which is not likely an area of expertise. Do you have a budget to accommodate frequent compensation? Second, should a customer renege on an agreement, are you prepared to insist that the customer uphold their end of the bargain? Third, would you—the marketing organization—be prepared to be one of the first phone calls a customer makes when they are unhappy with the product?

Some companies do put into place a "points" system and have good success with this. However, this depends on the makeup of your customer base. If your customer base is high-level executives, they are not motivated by redeemable points. If your customer base is motivated by a points system, do not underestimate the infrastructure required to launch, execute, and manage such a program.

For all of these reasons, it is best to provide a genuine thank you to your customers during your reference request process and to conclude the launch process with a thank you gift. It could be immediately after the launch or part of a quarterly thank you program. A logoed item, such as a high-end pen set, makes a nice gift, as does a box of chocolates. Depending on how much the customer assists, a coupon or free pass to your annual user group conference or some level of free training, should your company be able to support such gifts, is much appreciated.

## Better references mean better launches

Following these suggestions, the beta, product marketing, customer reference, and PR managers, working together, ensure target media write glowing articles about your new release; industry analysts tell your prospects to purchase your products; and investors buy your stock. Good references are critical to a successful launch. It is almost impossible to find these references afterwards. So be sure to identify references early in your launch-planning cycle.

*Amy Perkel is principal of Red-Spark Customer Marketing, a consulting practice focused on customer reference programs. Working with hundreds of executives from Fortune 1000 companies, she has created unique systems to track customer interactions, extract business stories, and leverage customer reference activities. Amy has ten years of high tech marketing experience, working for Oracle, Hyperion, and Documentum. She can be reached at amy.perkel@red-spark.com*

## Key responsibilities by launch team member

| Role | Key responsibilities |
|---|---|
| Customer reference manager | • Recommends customer references<br>• Secures customers participating in the launch<br>• Provides realistic number of customers able to assist to PR, IAR, and IR managers |
| Beta team manager | • Shares list of beta participants with CR manager<br>• Invites customers recommended by CR manager into beta<br>• Closely monitors progress of CR manager's recommended customers |
| Product marketing manager | • Delivers webcast on product features to reference customers not participating in beta program<br>• Works with PR to draft ideal quotes for customer approval |
| Public relations manager | • Works with Product Marketing to craft ideal quotes for customer approval<br>• Alerts CR manager to timeframe of release and media interviews<br>• Schedules interviews between reporters and customers |

*Jim Davis, Senior Vice President & Chief Marketing Officer, SAS Institute, Inc.*

"Our overall goal is to deliver products and solutions that provide customers with differentiated value. Pragmatic Marketing® has given us a framework for managing the entire supply chain—from initial development to customer acceptance."

*–Jim Davis*
*Senior Vice President*
*& Chief Marketing Officer*
*SAS Institute, Inc.*

If you are trying to leverage your investment in product management and marketing, the first place to start is with a proven methodology. Pragmatic Marketing has always focused on the unique challenges of managing and marketing high-tech products.

The Pragmatic Framework has been fine-tuned by 30,000 attendees over 12 years and has been proven to create high-tech products that customers want to buy. Pragmatic delivers on the promise in its name—presenting a practical course of action that really works.

Pragmatic Marketing®

*The Industry Standard in Technology Product Management and Marketing Education*

Visit www.PragmaticMarketing.com to learn more.

# Effective Sales Presentations: **Advancing the Sales Cycle**

*By Stephanie Tilton*


Effective sales presentations are at the core of a successful sales cycle, yet many presentations miss the mark in terms of appropriate content and flow. While presentation skills contribute to the success (or failure) of a sales presentation, presentation effectiveness also hinges on the value of the message and the quality of the content. Your sales team members rely on you to deliver a solid presentation that they can successfully use in their selling efforts. Here are proven methods for ensuring that your sales team is armed with the content it needs to win deals.

## Taking inventory

Before you begin creating a presentation, take inventory of the information you will need to get started. This will serve as a checklist to ensure that you and your team are staying on course and creating a presentation that will hit the mark. Engage your sales representatives in creating this list—they typically know which messages resonate best with different prospects. They can also provide input as to how they intend to use the presentation and what tactics and content have (and have not) worked in the past.

- Identify the target audience and its business issues
- Determine the goal of the presentation and its role in the sales process (e.g., to generate interest in learning more about your product or service, or to gain introduction to the decision maker?)
- Determine the level of detail appropriate for the audience
- List key messages for the solution (e.g., value proposition and key differentiators)
- Enlist appropriate reviewers (e.g., Sales, Marketing, and pre-sales technical engineering personnel) to ensure full content accuracy as well as help establish interdepartmental "buy-in"

## Think outside the PowerPoint slide

Many presentation writers try to brainstorm the story they want to tell while using Microsoft® PowerPoint®. But crafting a story when you are limited to bulleted concepts can be difficult. Instead, try writing out the story you would like to tell. (You can leverage this to create speaker notes—more on this later.) By formally capturing your thoughts in a written document, you can craft your story more quickly and easily. Key reviewers may find it easier to provide critical feedback on your "story" as well.

For example, the following is a sample guide for an IT-industry presentation that can help you outline an overall concept and define what content needs to be included. An outline also helps the presentation team members consider "branch slides" that can help address a specific industry or audience member (e.g., a CFO).

| # | Slide Title | Key Elements and Messages | Possible Branch Slide Sets |
|---|---|---|---|
| 0 | *Title Slide* | (Self explanatory) | |
| 1 | *Agenda* | Summary of content to be covered | |
| 2 | *Key Trends* | If applicable, describe key industry or business trends in order to provide a context for the business problems/customer pain points described in the next slide. | **Vertical audiences:** branches that drill down on industry-specific trends |
| 3 | *Business Challenges/ Pain Points* | List the pains/challenges facing businesses/employees that do not have the particular solution being offered. The goal is to help the audience identify personally and feel the "pains" as their own. | **Vertical audiences:** branches that drill down on industry-specific pain points |
| 4 | *Understanding the Problem* | Elaborate on the complexity of the problem and how existing processes, workflows, customer demands, etc. require a new approach to the particular business area. | **Line-of-Business (L.O.B) audiences:** branches that drill down on business problems to be solved, for example, for a VP of Sales or CEO |
| 5 | *The Answer: Your Solution* | Introduce your solution by providing a high-level introduction that answers the questions, "What is it? Why should we spend our limited budget on it? What is the real value?" If possible, graphically illustrate the solution and how it provides business value (show rather than tell). | **IT audience:** a branch that discusses the larger IT environment that this particular solution requires |
| 6 | *Key Capabilities and Business Value* | Prove the business value by explaining how the solution provides a capability or benefit that solves one or more of the business challenges listed previously. | **Industry audiences:** include branches with industry-specific benefits that demonstrate a deep understanding of the industry-specific pain points and how the solution addresses them |
| 7 | *ROI/Business Case* | Summarize the business case for the solution by providing benefits backed up with ROI data (dollar amounts or percentages regarding cost savings, increased productivity, reduced downtime, etc.). | Expand the business case with branches that may include:<br>**CXO audience:** Slides that elaborate on how the solution impacts both the top and bottom line through "hard" and "soft" returns (reduce costs, increase revenues)<br>**Industry-specific audiences:** industry-specific ROI data, if available |
| 8 | *Customer Success Story* | Describe a powerful customer success story with ROI data, if available. | **Industry audiences:** branches of industry-specific success stories<br>**L.O.B audiences:** branches with L.O.B.-specific success stories |
| 9 | *Next Steps* | What is the call to action? | Depending on the audience, the next step may be to seek an introduction to the decision maker or to show a demo of your solution to the technical group. |

## Keep it focused… on the customer

In today's business world, your audience probably already has researched your company and its products on your website. So if prospects invite your sales representative to their offices, they really want to know how your solution will solve their business issues and pain points. The prospects must be convinced that you understand the business obstacles they are trying to overcome. This fact alone may mean you need to create more than one presentation for a specific product or solution, perhaps focused by industry or by audience type (e.g., the budget owner wants to hear different points than the implementer of the solution).

The following table of typical stakeholders across a company can help you consider the presentations that you may need to create for different audiences. (This list is oriented toward IT presentations, but stakeholder profiles are typically similar from company to company.)

## Plan for customization

Experienced marketers know that their sales representatives will customize presentations to fit their prospects' needs. This behavior should be encouraged, not discouraged. After all, your sales representatives will be most successful if they have done their homework to understand the unique business pains facing their prospects and how your company's solution can address those issues. The salesperson may not be presenting to an individual or group for the first time, and therefore, may have to tailor the content to cover only the most relevant information. After all, nothing loses an audience more quickly than covering stale material.

While you must be willing to relinquish some control over how and precisely what your sales team presents, your role is to provide the foundation for a logically flowing, compelling presentation that adheres to corporate standards for messaging, language and design. One way to maintain some content control is to include an appendix with branch slides suitable for various industries and company sizes, etc. For instance, survey the sales force during presentation development to learn which success stories would be most useful and include those as extra slides for use as needed. By providing easy-to-use, ready-made slides, you know your sales people can customize the presentation to meet their needs without compromising the standards of the material.

## Balance brevity with useful detail and illustrations

For better or for worse, bulleted lists tend to be the dominant form factor in PowerPoint. The advantage of bullet points is that they prevent overzealous authors from trying to convey every bit of information about your company. Bulleted lists present a concise summary of your message and can be easily read by those listening to the presenter. The presenter expands on points where necessary, which can often only be determined by "reading" the audience. To ensure that the bullet points are read, make sure they convey valuable information and are not reduced to industry jargon and sound bites.

| Stakeholder Profile | Characteristics |
|---|---|
| *Initiator* | Has identified the problem areas to address and has asked staff to identify possible solutions. |
| *User* | Will be the one to actually implement/use the solution. Concerned about ease of use and support. |
| *Influencer* | Will likely define technical specifications and provide information for evaluating options. Wants to understand the technical underpinnings of the solution and how it fits into the overall enterprise architecture. |
| *Decision maker* | The one to make the final recommendation to the approver. Ultimately responsible for ownership of the solution, including implementation, integration, internal support, and tracking ROI. |
| *Buyer* | Controls finances. May question price, ROI, TCO. |
| *Approver* | Top management with final budget authority. Needs to be convinced the solution is the best option for the money. |

Similarly, do not try to fit every piece of information about a point onto the slide. Leaving something for the speaker's notes ensures that the audience will listen to the presenter and keeps the amount of screen-cluttering text to a minimum. At the same time, your content should be memorable and meaningful to the prospect. Remember that people grasp pictures more quickly than words. Visually illustrate your points whenever possible with a graph or image and choose visuals that help to further the audience's comprehension of your points.

## Mastering organization

Although a story is not compelling if it does not flow properly, determining the optimal flow of a story is difficult until all the parts have been recorded. Even best-selling authors rarely establish the flow without many rounds of reorganizing. So, after you have created your first draft and walked through a practice run, shift the content around until the flow feels natural and the presentation tells a compelling story. If you have backed up your key points with persuasive supporting content, such as industry statistics, analyst quotes or customer testimonials, you are likely to see a positive response to your presentation.

Your sales representative may choose to present only portions of the presentation. For that reason, "modularize" the presentation into discrete sections that make sense on their own. Ensure the presentation flow is strong regardless of which or how many modules are skipped.

## What goes into speaker notes?

As the marketing guru, you need to provide scripted speaker notes so the presenter has detailed information about each of the points on the screen. And since you started the creation process by capturing your presentation in story form, you can now lift from that document to build your speaker's notes.

While some presenters may add a personal twist to the story, the story should essentially remain the same—by providing speaker notes, you can ensure a basic level of messaging consistency. Have faith in your sales people—in many cases, they do not require a narrative script as much as clear, concise talking points presented in a logical order.

## Test and revise

Finally, make sure you test the presentation with a few sales people (both senior and junior). As part of this testing, you should see how well the presentation works when skipping certain sections. Obtain feedback and revise the presentation appropriately. Nothing ruffles the feathers of the sales team more than being handed a sales tool that doesn't meet their needs—especially when they are sitting down the hall from you and are often eager to provide input into the development of these tools.

No sales presentation will be successful without aligning your sales and marketing organizations. With such goal-oriented cooperation in place, you can help your sales representatives succeed by providing them with a customer-centric message that clearly explains how your solution solves the prospect's business issues. Ultimately, by managing the messages in your company's sales presentations, you can increase the effectiveness of your sales team's communications and help shorten the sales cycle.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# Problems. Solved.

Do you understand the relationship between product management and product marketing?

Does it seem that product managers are overloaded with tactical activities?

Are you getting the most out of your investment in Product Management and Product Marketing?

Does your Product Management function need more structure and process?

Are product managers spending too much time supporting Sales? Development? Marketing Communications?

Do your product managers and product marketing managers understand their roles?

Are your product managers trailing the other departments instead of leading them by six or more months?

Are requirements a moving target?

Do your product managers rely on the sales channel for product requirements, positioning, name, or pricing?

Are your Market Requirements Documents not providing enough detail to Development so they know what to build?

Do your product managers wander into design in the Market Requirements Document rather than provide the market facts that Development needs?

Are you struggling to keep control during the product planning process?

Is there agreement between Product Management and Development on what to do?

Does your Product Marketing function need more structure and process?

Is your marketing plan just a revised list of last year's tactics?

Do you want better workflow between Product Management, Product Marketing, Industry Marketing and Marketing Communications?

Is Marketing disconnected from the sales process, generating leads and sales tools that go nowhere?

Is your message and program strategy based on a clear understanding of buyer problems and the reasons they should prefer your solution?

Do you know how to effectively measure all of your programs?

Have you been asked to create a marketing plan, without any guidance on what should be in a marketing plan?


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# Complete Curriculum for Technology Product Managers

| Product Strategy | Product Planning | Program Strategy | Sales Readiness | Channel Support |
|---|---|---|---|---|
| Business Case | Positioning | Marketing Plan | | |
| Pricing | Sales Process | Awareness Plan | | |
| Buy, Build or Partner | Market Requirements | Customer Acquisition | | |
| Thought Leaders | Product Roadmap | Customer Retention | | |
| Innovation | User Personas | Buyer Personas | Collateral & Sales Tools | Channel Training |
| | Product Contract | Market Messages | Presentations & Demos | "Special" Calls |
| | Release Milestones | Launch Plan | White Papers | Event Support |
| | **Requirements That Work™** | Lead Generation | Competitive Write-Up | Answer Desk |

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Practical Product Management is for product managers and those who manage or contribute to aspects of product marketing and management. This two-day seminar fully explores the role of technical product management, providing tools and a framework to help get products to market more efficiently.

### I. Strategic Role of Product Management
- What is marketing?
- Definition of the role of product management
- Contrasting product management and product marketing
- Assigning ownership of responsibilities
- Identifying the "first steps" with gap analysis

### II. Market Analysis
- Distinctive competence
- Market research
- Market problems
- Technology assessment
- Competitive analysis

### III. Quantitative Analysis
- Market sizing
- Product performance
- Operational metrics
- Win/loss analysis

### IV. Product Strategy
- Business case
- Pricing
- Buy, build, or partner?
- Thought leaders
- Innovation

### V. Product Planning
- Positioning
- Sales process

### VI. Case Study

### VII. Delineating Responsibilities
- Communicating market facts to Development, Marcom, and Sales
- Drawing the line between Product Management and the other departments

## DAY 3 Requirements That Work™

*(For those who write requirements)*

### VIII. Building the Market Requirements Document (MRD)
- Writing requirements
- Implementing use-case scenarios
- Programming for the "persona"
- Determining product feature sets
- Creating the MRD

### IX. Analyzing Business and Technology Drivers
- Reviewing specifications
- Prioritizing the product feature set

### X. Getting (and Keeping) Commitments
- Product contract
- Getting the product team in sync
- Getting executive support
- Communicating the plan in the company and in the market

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- Define clear roles and responsibilities
- Introduce a product planning methodology

## II. Gathering Input

- Channels of input to product planning
- Organizing product ideas
- Quantifying market needs

## III. Building the Market Requirements Document

- Writing requirements
- Implementing use-case scenarios
- Programming for the "persona"
- Determining product feature sets
- Creating the Market Requirements Document (MRD)

## IV. Analyzing Business and Technology Drivers

- Reviewing specifications
- Prioritizing the product feature set

## V. Getting (and Keeping) Commitments

- Product contract
- Getting the product team in sync
- Getting executive support
- Communicating the plan in the company and in the market

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- Build useful audience profiles
- Influence the buying process
- Create high-impact market messages
- Select the right programs for your audiences

## III. The Strategic Program Plans

- Develop clear market strategies
- Create the right budget
- Relate plan elements to company and sales goals
- Build the business case for marketing investments

## IV. Align with Sales

- Respond to endless tactical requests
- Collateral and tools that impact buying decisions
- Measure and improve sales tool productivity

## V. Goal-Oriented Program Execution

- Manage lead quality and throughput
- Integrate programs by target audience
- Build and measure positioning awareness
- Influence customer retention
- Measure progress, with or without CRM

## VI. Start Immediately

- Prioritize next steps
- Apply the process to current programs
- Continuously measure and improve

# Pricing for $oftware Product Managers

*By Daniel Shefer*

Pricing has far-reaching effects beyond the cost of the product. Pricing is just as much a positioning statement as a definition of the cost to buy. Price defines the entry threshold: who your buyers are and their sensitivities, which competitors you will encounter, who you will be negotiating with and what the customers' expectations are. Good pricing will remove the price issue from being an obstacle to a sale. Pricing is also used as a weapon to fight the competition as well as gray markets. Pricing is also unique from other marketing decisions for several reasons:

- Price is the only marketing element that produces revenue; all other marketing decisions produce costs.
- Pricing is the most flexible marketing decision.
- Pricing reflects a product's strengths and weaknesses; it implies value as well as positioning.
- Pricing has the most immediate impact on the bottom line. In the high tech industry, a 1% increase in prices can lead to a 10% (or more) increase in profit. This is twice the effect that the same change in volume and fixed or variable costs have on profits.

## Pricing software products

### When it comes to pricing software, Economics 101 does not apply

When pricing software, the "Economics 101" you learned in college is irrelevant. There are many reasons for this:

- Supply and demand curves are based on the assumption that the marginal cost for manufacturing additional products is non zero and that it decreases with quantity. In the software industry, the marginal cost for an additional copy of software is zero.
- Estimating price elasticity for a specific product is practically impossible. Hence, pricing decisions cannot be based on supply and demand curves.
- Estimating the potential market for a product is possible, but estimating demand is problematic. Most customers tend to be enthusiastic when seeing a new product, but their input is not a good indicator for real demand.
- For enterprise software, sales numbers are too small for a statistically significant study. By the time a company has sold enough licenses, it has advanced to a newer version or the market has changed, or both.
- For most products, there are competing products, and their influence on the demand curve is hard to estimate.
- Product life cycles are short, making comparisons more difficult.
- Purchasing decisions are complex and are influenced by many constantly changing factors. →


# Tips for Setting Prices

## The company's perspective

- Before making pricing decisions, you must thoroughly understand your target market's decision-making and buying processes.
- Properly-priced software will not guarantee the company's profitability.
- When deciding which product competes with your own, the market's perspective is what counts.
- Internal company parameters such as distribution costs come into play only when looking at the potential profitability of the product. I.e., can the company make money selling the product at a given price point?
- The price of the software must be higher than the cost of selling it, and the margins must be higher than the cost of creating, marketing, selling and supporting it or else the product will lose money.
- When new to a market, being a small, unknown company minimizes brand value. Lower, "penetration" pricing may be required.
- If customer segments value the product significantly differently, this may justify segmenting the product for each of these markets.
- When attempting to price commodity products, it is basically the competition that sets the price of the product. Setting a higher price in a commodity market is limited to the company's ability to differentiate the product from its competition. On the flip side, offering a lower price in such a market is sustainable only if the company has a lower cost structure.
- Just like other aspects of the product, pricing needs to follow the technology adoption lifecycle of the product. Early market buyers may be interested in your product but tend not to be willing to pay its full price. It may make sense to price the product at its target price for larger markets and offer early adopters the product at a discount.

## The customer's perspective

- The price has to consider what the customers feel is reasonable. For example, market leaders are expected to charge more. Hence their higher prices can be perceived as "legitimate," up to a certain level.
- Using the pricing model as a differentiator is always worth considering as long as the model is easy to explain and it makes sense to the customer.
- The costs of training, implementing and supporting the product are perceived as additional costs by the customer.
- When setting the price within a range of competing products, it is important to understand how reference prices affect your customer's price evaluation. This is imperative when customers have limited product or price knowledge.

## Guidelines for setting the price of software in *existing* markets

When setting the price for a software product, classical economic theory comes up short. Here is an empirical, iterative method to arrive at a price.

The purpose of these guidelines is to arrive at the “right” price. This is the price that lets the company accomplish its goals for revenue, profit, market share, renewals, etc. The method detailed below will help you identify the highest price a market with existing competitor presence will bear:

- The price of the software must be less than the ROI it provides. The smaller the ratio of the ROI to the cost of the software, the easier the sale.
- Create a market segmentation chart based on feature sets. Identify all competing products and place them on this chart. Identify and group the value elements in the product that address the needs of each segment. For each segment, identify the features for which customers are willing to pay extra and that differentiate your product from the competitor’s. Attach a price tag to the value of each attribute that is not identical such as:
  - The feature and functional differences.
  - The difference in brand value that customers attribute to the products.
  - The difference in cost for implementing the respective products.
  - Any other item that customers attach value to such as localization of the application, geographic proximity (for services), etc.

If the product excels in a certain aspect, then simply add that value to the price, if it lags, simply subtract the value. This step must be iterated for each competing product. The price of the software must be similar or less than that of the main competing product in each segment minus the difference in price that is justified by the functional and other aspects previously identified.

- The price must be below the purchasing authority of the targeted decision maker signing off on the purchase.
- The price should be outside the “Dead Zone” of $5,000 to $20,000.
- The price must fit how the market perceives the product category. For example, desktop utilities can be priced up to $50, productivity tools up to $500, etc. If the product is priced too high, the price will become an issue. If it is priced too low, customers will perceive it as not worthy.

## Guidelines for setting the price of software in *new* markets

If there are no reference products, the approach is slightly different. The first step in setting a price is identifying how customers will position it in their minds. If the product is perceived by customers as a utility or productivity tool, price it in these ranges—that is, until the product can be positioned (in the buyers’ minds!) as belonging to a higher place in the food chain. See below for examples of products and typical price ranges.

If the product does not fall into the previous category, start by defining the price ceiling. This is the highest price based on a product’s benefits. A high price will work if early adopters are willing to pay a premium for a new product. However, this price level may prove to be unrealistic as there may not be a sufficient number of buyers for a new product at that price level.

Then, choose a “penetration” price. Penetration pricing is used when a product is first launched in order to gain market share. A low penetration price is used to discourage competitors from entering the market and to gain market share. Its drawbacks are lower margins, difficulty in raising prices in the future because pricing expectations are now set and the risk of customers perceiving the low price as a low quality indicator.

## Typical software price ranges

- **Utilities: $50 to $70.** Purchases of utilities are many times spur-of-the moment decisions. Customers need to feel that the potential financial risk of buying the wrong product is minimal.
- **Productivity tools: $100 to $500.** These are purchases that are within the budget of a low-level manager.
- **Professional tools: $1,000 to $5,000.** Applications that are required by professionals to do their job, such as computer-aided design tools and many others.
- **Enterprise applications: $20,000 and up.** Applications that impact many functions and departments in the customer’s organization and that require an evaluation process, and sometimes, a purchasing committee. Selling into such a customer is many times a costly and labor-intensive process.

The penetration price has to be sustainable and higher than the company's variable costs. If possible, the price should be low enough to remove the price of the product from the buying decision.

These two markers set the price range for a new product. Follow the relevant guidelines in the previous section to finalize the price point.

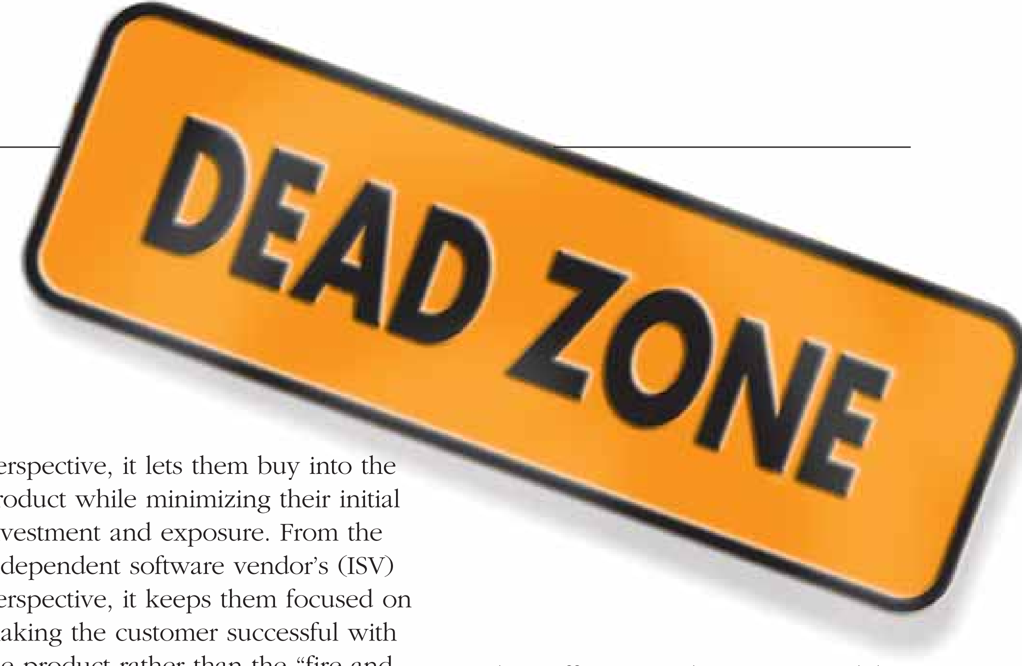
## The software price "Dead Zone"

The Pricing Dead Zone is a price range between $5,000 and $20,000. Some would even say that the range extends up to the $40,000 - $50,000 range. Software products in the Dead Zone are the exception. This is because software priced in this range is hard to sell profitably.

Products that cost less than $5,000 can be sold over the web or through channels. A purchase of this size is within the decision authority of middle managers, and there is no need for on-site visits to close a sale. More expensive products require higher-level signing authority or purchasing committees. A committee's decision can cause the sales cycle to drag on for months and get entangled in internal politics. These products require sales reps' on-site visits but have to produce enough profit to support this type of sales effort. $20,000 is at the bottom of the price range that can support a complex sales process. The exact boundaries of the Dead Zone depend on the specifics of how the product is sold.

## Perpetual vs. subscription licensing

Subscription software is an application that is "rented" on a temporary basis. Licensing is usually on an annual basis, but monthly terms also are available. Subscription licensing works when customers see an ongoing benefit from the software. From the customers' perspective, it lets them buy into the product while minimizing their initial investment and exposure. From the independent software vendor's (ISV) perspective, it keeps them focused on making the customer successful with the product rather than the "fire and forget" approach to selling software.




Moving from a perpetual license to a subscription model increases the vendor's risk as it becomes easier for customers to walk out on them. It may also have a negative effect on the short-term stock price due to Wall Street's focus on quarterly revenue vs. cash flow as the vendor is mortgaging their present for their future. This is because, over time, the income statement reflects the growth from prior years' bookings, as the deferred subscription revenue is transferred to the income statement. Over the long term, the subscription model allows for significantly better revenue visibility and consistency. This is beneficial, as Wall Street loves companies that make their numbers. For example, when signing a three-year license for $100,000, one-twelfth of it can be recognized each quarter with high certainty. In such a case, cash flow becomes the much more representative indicator of income. This works as long as the renewal rate is high.

By offering a subscription-pricing model, customers face smaller payments. From the sales reps' perspective, a lower initial price lets them aim their pitch lower in the customer's organization. Another advantage for the sales process is that calculating an ROI on a shorter time scale makes it more tangible, hence helping the sale along.

When offering a subscription model, the vendor is betting its future on its ability to keep customers. For hosted apps, setting up a hosting environment can be very costly. The vendor is basically giving customers a loan that will be paid back over the length of the contract. This creates additional risks that vendors may want to avoid.

So now, the bottom line. How much do you charge for a subscription model? There are no axioms here, but many companies charge one-third of the cost of a perpetual license for an annual term. When offering a subscription model, maintenance is usually mandatory.

## Pricing maintenance and support

For enterprise applications, 18 to 20% of the list price is the "standard" cost of support. This usually includes support over the phone for a single contact from the customer during regular business hours as well as product updates (both point and major releases). More advanced packages that include 24/7 support are priced higher, in the 20 to 25% range, and require a minimum of $30,000 to $100,000. Minimums of $200,000 to $300,000 are the norm for packages that include assigned support engineers. Onsite support should always be priced as an extra. ➔


Most companies have a no-discount policy on support. That is, even when the software is discounted, the support pricing stays at a percentage of the list price. Very large deals may justify a discount, such as if all support calls are routed from a single person at the customer. One approach is to give away a few months of support during the first year. Psychologically, it is better to give away "months" than to lower the price of the yearly contract.

For non-corporate users, there are two basic models for providing support:

- The per-incident model: The most common model for personal support is "per incident"—that is, a flat rate for resolving each support question, regardless of call length. The median per-incident price for surveyed companies that offer this option is now $100, with 50% of these companies charging per-incident prices between $35 and $185. Support for developer tools and more technically advanced issues run into the hundreds of dollars per incident. For example, a call into Microsoft's tech support for developers costs $245. These models typically include a refund if the problem is determined to be a defect in the vendor's product.
- The per-minute model: A less-popular model is a "per minute" rate. Here, there is less variation in pricing: The median per-minute price is $2.71 and the 50% range is $2 to $2.95. Note that the $3 per-minute rate is one of the few service prices where there is significant customer sensitivity and pushback.

## Discounting and non-linear pricing

Discounts come in two variations, scheduled and negotiated. Scheduled discounts are those that are pre-approved by the company, based on pre-defined criteria such as the volume of the purchase. Negotiated discounts are an ad-hoc result of the sales process that differ from or go beyond the pre-set scheduled discounts. This article will only discuss scheduled discounts.

## Volume discounts

There are multiple reasons why ISVs offer volume discounts:

- Many times, the utility to the customer of additional licenses decreases as volume increases. To guarantee that the value to the customer is more than the price of the software, the price must decrease as the volume goes up.
- In many sales situations, the cost of sale per unit decreases. This savings can then be passed on to the customer.
- A volume purchase increases the customer's investment in your product and reduces his or her chance of buying the competitor's product.
- Large customers are convinced that it is their inherent right to pay less per unit than smaller customers.
- Buying more units now rather than in the future has a discounted current value.

Once a discount is offered, buyers will assume that this discount—or a better one—will be offered for all future purchases.

Before offering discounts, you have to understand the impact on revenue. When offering a 10% discount at a contribution margin of 70%, you will have to increase sales—above baseline—by 17% to make a positive contribution to profit.

## Calculating volume discounts

The way most companies calculate their discount schedules is surprisingly off the cuff. They simply decide how much money they would like to get from a large target customer per user and then draw a curve between the price of one unit and the price of a unit at the high-volume level. They then stand back, look at the curve and play with it until "it looks good."

Another, more rigorous method for calculating volume discounts is to select a consistent discount rate for every growth in units. For example, a 10% discount on the 10 - 20 units, a 10% discount from the previous price on the next 10 units (which equals a 19% discount from the original price) and so on.

## VAR discounts

Value Added Resellers (VARs) get the software they resell at a discount. Discounts are typically between 40 and 60%, depending on the marketing and sales efforts required by the VAR to promote the software. Many companies design incentives for VARs by creating volume thresholds that increase their discount level. Tier discounts require VARS to commit to sales volume. For example, they may give a 15% discount for no commitment and 35% for very serious ones. VARs receive training and licenses for an additional cost. In comparison, reference partners whose activities are limited to referring customers to the vendor get 5 to 10% of the deal.

When setting a pricing schedule for VARs, take into consideration that the VAR has to make a profit and may be feeding its own distribution channels. This approach is relevant to original equipment manufacturer (OEM) pricing as well.

## OEM pricing

One of the difficulties of pricing OEM deals is that there are no industry standards or accepted price ranges.

When signing an OEM agreement, some companies require an up-front fee for Non Refundable Engineering (NRE), which are efforts needed to tailor the product to the OEM's specific needs. NRE fees include charges for developers, QA and project management. These fees can easily run into the six digits. Some OEM deals will tier their pricing based on the up-front fees and volume commitment. As a rule of thumb, the higher the commitment and up-front fee, the lower the royalties.

## Site licenses

Site licenses give customers unlimited use of a product across their enterprise while paying a flat fee. A buyer's request for a site license is mostly a purchasing ploy. The reasoning is that with a site license, the buyer does not have to worry about counting seats. However, it's only another way to ask: "what is your best price?" One problem with this model is that as a vendor, you lose your ability to track the number of installations at the customer site, and if your product is successful, you will be leaving money on the table. Another drawback of site licensing is that when you sell a site license, you have effectively lost that customer for any repeat sales. If you are concerned about getting the product in front of as many users as possible, just offer steeper discounts to encourage proliferation and use.

Site licenses must provide adequate safeguards so keep usage within the boundary of the site. Customers may not want to count "seats" but they need to have a means for controlling the use of the product. ➔

## Pricing discrimination

Price discrimination is a technique for maximizing profits by offering the same or similar product at different prices to different customers. The idea behind this is to set prices so that purchasers who are able and willing to pay higher prices do so. Pricing discrimination allows vendors to capture additional market share by addressing segments that attribute a lower perceived value to the product.

Price discrimination can be explicit or implicit. Explicit price discrimination is when a special price is limited to customers who meet certain criteria. For example, academic pricing is a form of explicit price discrimination because only students and faculty can buy at that price. Implicit price discrimination is when all customers are technically eligible for the special price, but the vendor inserts a condition that makes it unattractive to some. For example, rebate programs are a form of implicit price discrimination.

To make pricing discrimination work:

- Each segment needs to have a version unique to that segment
- One market segment cannot buy the product created for another segment
- The difference in pricing must be justifiable and must not create a feeling with customers that they are being treated unfairly

Another common form of pricing discrimination is introductory pricing. The idea behind this technique is to release a new product at a premium price and to lower the price in time. This is a common technique in the computer chip industry where power-hungry buyers are willing to pay extra for the latest and greatest. The reverse can also be true: introduce a product at a significant discount for a limited period to stimulate early sales and then return to the higher list price once the initial surge of excitement has passed.

## Illegal pricing discrimination

The Robinson-Patman Act made it illegal for sellers to directly or indirectly discriminate in the price of similar commodities, if the effect hurts competition. This is especially important when selling to distributors and VARs. For example, if a vendor has two distributors that compete against each other, they have to be offered the same basic terms. If one distributor is allowed to buy software from you at a lower price than another, competition is adversely effected because the second distributor, buying at the higher price, will have a greater difficulty in reselling the software.

It is important to note that there are situations where pricing discrimination is explicitly legal. These include situations where the vendor's manufacturing, delivery or financing costs are different for different customers as well as situations where a competitor dropped its prices. Meeting the lower price is not illegal even if this price is not offered to other customers.

Note that the law applies only to products and not to services.

## Bundling

Bundling is when a group of products (or services) is offered as a single package. By offering bundles, ISVs can increase their sales to segments that would buy only one product. There are two types of bundling:

- Product bundling. Product bundling is when two products are integrated into a single package. The purpose of product bundling is to create a combined product that has more value to customers than the separate parts. An example of product bundling is the Oracle ERP® package where the database and application layer are bundled into a single package.
- Price bundling. This is when an ISV provides a discount to customers who buy two or more products at the same time.

There are basic differences between price and product bundling. Whereas price bundling is a pricing and promotional tool, product bundling is more strategic in that it creates added value. Price bundling products does not create added value in itself. Therefore, a discount on their combined prices has to be offered to motivate consumers to buy the bundle.

Bundling can be "pure" or "mixed." Pure bundling is when a vendor does not offer any other option but the bundled products. Pure price bundling is basically forcing a customer to buy at least one product that they are not interested in and can be illegal. Mixed bundling is when a vendor offers both the bundle and the products separately.

## Legal issues when bundling

All mixed bundling strategies are legal. This is because the customer's ability to choose the product they want is not hindered. On the other hand, pure pricing bundling is illegal if the vendor has "market power." Market power means that the vendor can force a consumer to do something that he would not do in a competitive market or when "a substantial amount of commerce is at stake."

If a vendor possesses market power, pure product bundling is legal only if the benefits to consumers offset potential damage to competition. For example, in the Microsoft® vs. DOJ case, Microsoft's claim of consumer benefit was enough to justify the integration of Internet Explorer with Windows®. Note that merely combining products together in a single installation does not constitute integration and will be difficult to defend as providing benefit to consumers.

## Price bundling is used to:

- Increase sales to segments that have different perceived values for the vendor's products.
- Expose a new product to a large customer base.
- Provide product visibility and a low-cost opportunity for customers to test a new product.
- By offering bundles, vendors make it difficult for consumers to price-shop.

Product bundling is used to create added value for customers. By using integrated products, customers can increase productivity, performance, lower costs of ownership and reduce purchasing costs.

In both types of bundling, vendors can increase customers' switchover costs by selling them more products than they intended to buy.

## Compensating for bundling's effects on profits

An issue that must be addressed when offering products as a bundle is the potential loss of revenue. The higher the variable costs for the products in a price bundle, the larger the increase in sales needed to overcome the discount involved. For example, consider two offerings: a refrigerator and stove costing $2,000 and $1,000 with variable costs of $1,600 and $800 respectively. The second offering is a bundle of a spreadsheet and a package of financial macros costing $300 and $100 with variable costs of $20 and $10 respectively. When sold separately, the packages will provide $600 and $370 of profit. By offering a discount of 10% on the bundles, the profit will be reduced to $300 and $330 respectively. Therefore, the appliances company has to sell 100% more units to make up for the discount vs. the software company that has to increase sales only by 9% to make up for the discount.

## Unbundling

Unbundling is a process where a product offering is split into modules with some becoming optional. By taking a complex product and splitting it into modules, the product can become attractive to additional segments. Furthermore, each segment tends to become less price-sensitive regarding the modules they need. For unbundling to make business sense, sales to additional customers have to make up for the optional modules that customers passed over. Another drawback of unbundling is the added complexity to the product. After unbundling the product, there are multiple options for customer installations, managing the product and supporting it increase in complexity. One risk of unbundling is that if the product becomes too granular, vendors run the risk of giving the customer a feeling that they are "nickel and dimed."

## International pricing

The international prices of identical products vary widely compared to U.S. pricing. The "uplift" as it is called, varies anywhere from zero to a premium of 50%. This uplift is justified by increased costs due to the need for localization of the product as well as marketing and sales expenditures the vendor faces in foreign markets. The cost of localizing the software has to be considered, but in many cases is not the bulk of the investment in foreign sales. Higher support costs are due to the additional languages needed, the more expensive labor (at least in Western Europe) and of course increased business risk. On the flip side, in some geographies such as in Asia, services are less expensive than in the U.S.

Note that differential pricing in international markets runs the risk of creating a "gray" market for the product.

Another issue that makes international pricing difficult to manage is fluctuation in exchange rates. There are two approaches to adjusting prices when the exchange rates change:

- Adjust the local price to reflect the price in U.S. dollars. This approach may cause difficulties in countries where the currency's buying power decreases compared to that of the dollar.
- Adjust the local price to partially compensate for the change in the exchange rate.

Both should be done with an eye on optimizing sales, taking into consideration how revenue is affected as well as the effect the change has on gray market pressures.

# Other pricing issues

## Pricing NRE projects

Non-Recurring Engineering (NRE) is a one-time engineering effort by a vendor that is paid for by a customer. NRE is driven by a feature or capability that a product lacks for which a customer is willing to pay.

In theory, costing an NRE project is easy. Estimate the engineering hours and overhead costs, add a "fudge" factor for uncertainties and risks and multiply it by your grossed cost rate. The result should then be multiplied by a factor of 5 or so. This is assuming that your company spends 20% of its revenue on R&D.

It is critical to understand the reason for this "5" factor, especially when the NRE takes up a significant portion of engineering's resources. If engineering costs amount to approximately 20% of revenue, an NRE project costing X would have a 5x negative impact on sales. This is because the resources used for the NRE were diverted from producing sale-generating products. This indirect cost must be taken into consideration and not doing so runs the risk of embarking on revenue generating but money-losing projects.

A company that is in good financial condition can follow this procedure for costing NRE projects but a company on the brink will probably not be able to achieve these premiums.

Support and maintenance costs need to be priced as well. If the results of the NRE efforts are not incorporated into the product and are available only to the customer who paid for it, support is extra. These costs should be more than the going rate to compensate for the added difficulty of supporting code which is basically a one off. This is because each maintenance release becomes an NRE project in itself.

## Price wars

A price war occurs when two companies drop their prices regularly to close sales. Pricing wars start once the differentiation between products has eroded. Proper product planning and positioning can help prevent a price war by allowing the leading vendor to charge a premium. However, if two competing products have similar offerings, as the market matures, price becomes a bigger factor in the buying decision. Unless the vendors can extract themselves from the price war with better positioning, the vendor that is able to offer lower prices over time will win the war.

Reducing prices don't necessarily cause a pricing war. It also depends on where the product is positioned. If it is the highest-priced product, dropping the price to be more competitive will probably not result in a price war. If you are the lowest-priced competitor, you may serve a different customer segment and your competitors may not respond.

Some factors that increase the likelihood of a price war in a given market are:

- A perception by managers that pricing is an easy to implement and reversible tactic
- Commoditized products that customers cannot differentiate between them
- Multiple competitors with manufacturing over-capacity
- Low switching costs between products
- High price sensitivity

One of the ironies of price wars is that while price wars are usually started as an attempt to increase market share, when the dust settles, the respective market shares of the players tend to remain constant but at lower prices and margins.

## Gray markets

A gray market is created when a product that costs less in one market is sold to another market where prices are higher through unofficial channels. There are multiple pressures that can foster the creation of gray markets. These include price differentials or an authorized retailer that can't sell all its inventory and may move the leftovers to unauthorized dealers.

A classic example is the current sale of pharmaceuticals from Canada to the U.S. Canada places limits on the prices of pharmaceuticals and so they are significantly cheaper than they are in the U.S. This creates a strong motivation for U.S. customers to import drugs from Canada. Another example is Amazon.com®. Books sell for different prices on the local Amazon websites. What prevents a German customer from buying a book on the American Amazon website and having it shipped to her home in Germany if she can save money? When it comes to consumer software, where delivery costs are zero, the problem is more pronounced.

Gray markets can damage channel relationships but the aspect that is relevant to this article is the undermining of the segmented pricing schemes. An important aspect of international pricing is the ability to price at the level that each market can bear. When a gray market forms, it can limit the company's ability to charge a premium in a given market.

Gray markets aren't always bad. As long as they do not directly clash with the existing channels, there can be beneficial sides to them such as incremental sales and the ability to reach into untapped markets.

## Price capping

At times, customers may ask for a cap to future price increases. Pricing caps are a negotiation issue. As in all negotiations, never give away something for nothing. Agree to the price cap in return for something that is important to you. This could be a press release, closing the deal by the end of quarter, etc. One trick is to agree to a maintenance cap only if the customer will commit to a number of years or whatever term for which the customer wants price protection.

Just remember that like any forward-looking commitments, potential buyers of your company would not appreciate long-term price commitments that cap your revenue.

One way to reduce the impact of a price cap is to price new features separately. Instead of adding a great new feature into the base product, consider making it an extra option. Offering the feature separately gives you price negotiation flexibility and makes you seem like a larger company with more products. You can always turn back around and offer a discounted "bundle" that includes both the base product and the extra option.

## Two additional issues

- By offering price caps, you may get into legal problems with other customers (see the Robinson-Patman Act).
- If you cap increases to customers, make sure to factor in any up-stream, third-party fees that you owe your suppliers. For example, if you can only increase your price by 5% per year and your suppliers do not have caps on their price increases, your margins could shrink. One way to avoid this is to exclude third-party fees from the price cap.

## How pricing affects sales methods

As a rule, the lower the price of the product, the less effort vendors can spend selling it. Enterprise applications are costly to sell. Marketing programs for generating leads can cost anywhere from $20 to thousands of dollars per lead at targeted tradeshows. Then there is the time spent by the sales rep qualifying the prospect and traveling to meet him. An onsite sales call typically costs them $2,000 to $5,000. It costs roughly $2,000 per day to send a B2B sales rep into the field. If the sales rep takes a sales engineer with her, this will entail an additional $2,000. Then there is the rep's compensation to factor in. The bottom line is that fully-ramped sales reps can cost a company $200,000 to $250,000 a year and more. Therefore, a direct sales force selling $2,000 software is simply not a tenable situation.

Companies selling mid-ranged products usually have inside sales reps that prospect and take orders over the phone. When enterprise-wide deals come up, a specialized sales rep is sent onsite. For smaller software packages that vendors want to sell directly, the only solution is to offer the software online and through indirect sales channels such as Amazon.com and CompUSA®.

# Retail pricing

## Natural price points

Natural price points are prices at which there are discontinuities in the price/demand curve. Customers expect to see commodity software products priced at natural price points that are traditionally, $19.95, $29.95, $49.95, $99, $199, $495, etc. The effect of increased demand for a $19.95 mouse vs. one that costs $20 may stem from an underestimation mechanism. One explanation is consumers' tendency to round prices down and to compare prices from left to right.

## Temporary discounts

Temporary discounts are used to stimulate short-term increases in sales and for enticing price-sensitive buyers that would otherwise be reluctant to buy at the regular price. A temporary discount can increase customer demand for a product. However, this peak in demand is usually temporary and will many times decrease future short-term demand. Price promotions may entice new, price-conscientious buyers, but they can actually hurt future sales to the existing customer base. Promotions are tactical, not strategic, and they need to be managed that way.

By reducing the price of a product, ISVs reduce the risk to consumers trying an unfamiliar product. Assuming that the consumer has a good experience with the product, they will be more likely to purchase it the next time, even without a discount. This is especially true if by using the product, there are significant switching costs for the customer. From a competitive perspective, rebates and other forms of temporary discounts are used to lower prices while attempting to avoid a price war.

When executing a promotion, vendors have to beware that:

- By reducing the price of their product, even temporarily, vendors risk implying that their product has inferior value.
- If a temporary price promotion goes on for too long, customers may begin to expect the lower price. The "reference" price is then perceived as expensive and customers are reluctant to pay it.
- The promotion must be targeted to new buyers and not to repeat buyers.

One way to meet these criteria is by creating a trial offer. This is basically a type of temporary discount. Usually, a condition is attached to emphasize the trial offer's "special nature." This can be done by setting an expiration date to the offer, requiring an additional purchase (a form of bundling) or an exchange of something of value. For example, the customer's agreement to present at a tradeshow on the vendor's behalf.

## Rebates and coupons

Rebates and coupons are discount mechanisms. There are several ways rebates and coupons work:

- A discount at the register. This has a 100% redemption rate and is therefore not used very frequently.
- Coupons at the shelf presented at check-out.
- Mail-in rebates.

Another type of rebate is given to the retailer. These are given after the consumer's purchase and are a form of a discount to the retailer. These rebates are used primarily for adjusting prices to fit the closest natural price point.

Another factor to consider is the cost of administrating mail-in coupons. The cost averages between $1.50 and $3, depending on the processing services offered with the rebate program.

## Charging for beta software

Most companies do not charge for the Beta versions of their software. Another approach is to charge the customer for the Beta version and then offer a substantial discount for the final release. The company gets to use the beta version of the product, pays for it and is used as a reference account. When the official version is released, the customer will then "buy" it. How long the reduced price is offered once the product has been released is a matter of negotiation.

## Revenue recognition

If a contract calls for onsite training and service to a customer as part of the deal, the revenue cannot be booked until the service is delivered. A simple email from a sales rep stating that they will send someone onsite to help with the implementation can cause problems since it would be considered as an element of the transaction and the revenue would have to be deferred until the company delivered the service.

Make sure the product roadmap doesn't end up in the contract. If the contract mentions future product features or that it will support a new operating system, the revenue cannot be booked until those capabilities are available in the product.

## Pricing post mortem

After setting a pricing model, it is always useful to go back and look at a deal's closing price. In many cases, you will see two things: the average price that deals close at is lower than the list price and a distribution curve of prices. Low closing prices indicate a lack of discipline in the sales force or a price that is set unrealistically high.

When the deal prices fit a wide curve, this is a negative indicator and can be caused by:

- Lack of sales process discipline. Sales reps are closing deals as they see fit, squeezing as much (or as little) as they can from customers.
- Customers varying in the value they perceive and therefore the price they are willing to pay.
- Fragmented buying power. The product is being sold into market segments that significantly differ in their ability to pay for a solution.

## Testing the validity of the pricing model

The pricing model should always be tested against sales scenarios. The best fit should be within the target market. Most models will not be optimized for some segments. In some cases, it may cause money to be left on the table or deals to be lost due to too high of a price. One way to test the fit is to list various sales scenarios and compare the effect on revenue caused by changes of the pricing model and the price points that feed into it. This exercise should be repeated at least twice a year. The assumptions used in the comparison should be validated and the model should be tested on the previous quarters' sales.

Another test for the fit of the pricing model and price point within a market segment is that a comparison with the competitors pricing must be made. Take into account the pricing differential based upon positioning and functional differences. If the differences between your price and that of your competitors' cannot be justified, you will either have to change the model or the pricing factors in it.

The last test is the market. Make sure that your prospects and customers "get it." The pricing model should be simple to explain. If you need more than a couple of sentences to explain the pricing model, it is too complex.

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More on this article is available online at http://www.shefer.net/Articles/Pricing_for_Software_Product_Managers.pdf

## Summary

Understanding pricing is critical to Product Managers. Pricing goes beyond setting a numerical value for the product. It sets customers expectations, positions the product and impacts the way it is sold. Successful pricing is an ongoing effort and should be reexamined continuously as the product goes though its life cycle to ensure congruency among all elements.

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