Business-to-business Pricing using EVC Analysis

Analysing economic value to the customer (EVC) is a useful aid to setting prices for business-to-business organisations. This example concerns the pricing of panel presses, which are supplied to the car parts business. The analysis focuses on the market leader and two other competitors.

The analysis begins by considering a reference product against which the costs of competing products are compared. In this case, the market leader is used as the reference product. In this example, a car parts company buying the panel press from the market leader would expect to pay the following costs. The purchase price of the press is £60,000. Start-up costs such as installation charges, staff training and lost production during installation are £20,000, and post-purchase costs including operating costs such as labour, servicing/maintenance and power are £130,000. This means that, over its life cycle, the panel press will cost the car parts company a total of £210,000.

Companies competing with the market leader present the customer with a different profile of costs. Company A has, by incorporating a number of new design features, managed to cut the start-up costs for a comparable panel press to £10,000 and reduced post-purchase costs to £105,000. This means that the total costs for the press are £35,000 less than those for the market leader. The result is that Company A's press offers the customer an EVC of £210,000 less £115,000, which equals £95,000. Assuming that Company A charged a purchase price of £95,000 for the panel press, the customer would face total life-cycle costs that were equivalent to the market-leading product. If, however, Company A decided to offer the panel press at a purchase price of only £80,000, the lower life-cycle costs of the product would give the customer a considerable financial incentive to buy.

Consider the position of a second competitor, Company B, with similar start-up and post-purchase costs to the market leader. This company has, through certain technological advances, increased the rate at which the press can be operated, potentially increasing productivity and therefore revenue for the customer. As a result, the press has the potential to offer an additional £50,000 profit contribution over the presses of the market leader and Company A. The EVC associated with this is £110,000, because this is the highest price the customer may be expected to pay.