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Pricing Strategy for Competitive Proposals
(And how to explain that you are not the low-bidder)

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Each Project has a "Winning" Price

For many consultants and contractors, the price they bid on the job is little more than whatever appears in the lower right cell of their spreadsheet. They estimate their staffing requirements, the equipment and materials, and other direct expenses; to these they add overhead and indirect allocations, G&A, and fees. And that is what they bid.

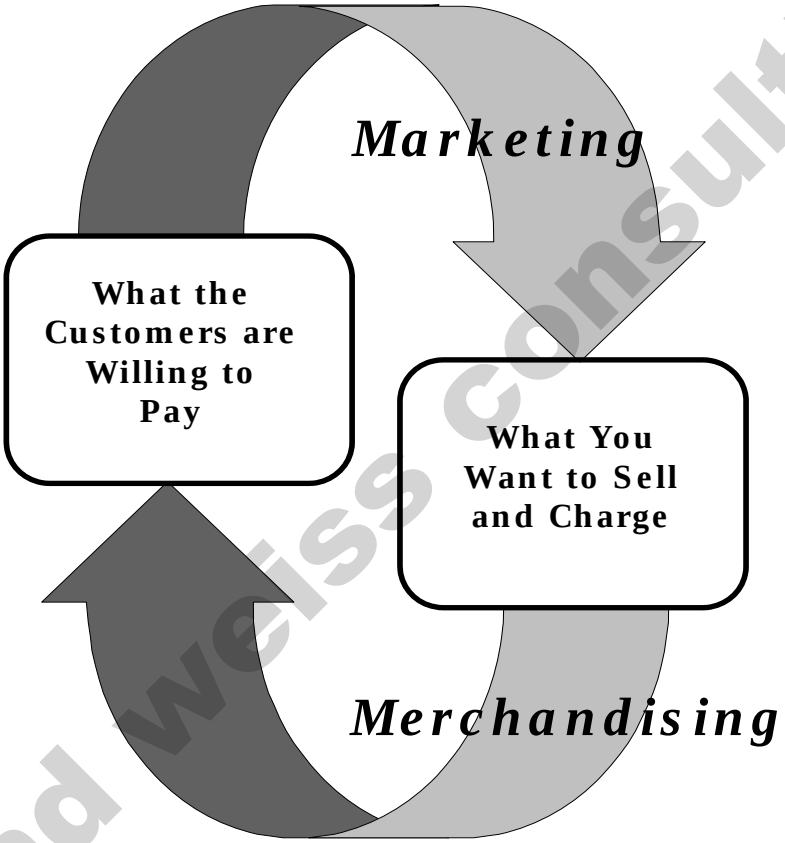
Consultants and contractors who are more successful, though, derive their bid from an estimate of an ideal or "winning" price. As illogical as it may seem at first, successful projects are designed to come in at a price that will make them especially attractive to the client—and almost never substantially more than the client has been authorized (or intends) to spend.

Part of the information gathering known as *customer intelligence* consists in finding the planned or estimated price the client has in mind. In government procurements, this is often a legislated or officially authorized amount, published in government plans or inferable from key phrases in the RFP, such as "estimated person-years of effort." But just because the information is not publicly available does not mean that the successful bidder is excused from intelligence work: finding out how much the client has set aside, how much the client has spent for similar projects or services in the past… Every client with experience develops a sense of how much things usually cost—including what the consultant's daily rates should be—and is not likely to be dissuaded.

To make a sale, then, contractors and consultants must define a price they want to bid and then adjust their offering until it makes sense at that price. If the number in the lower right corner of the spreadsheet is too high, the project must be reconfigured to produce a lower price. And, surprisingly, in most cases, if the number is much less than the client intends to spend, this also requires an adjustment.

Figure 1 illustrates this recursion. *Marketing* consists in trying to persuade the client to buy what you prefer to sell at the price you'd like to charge. *Merchandising*, in contrast, consists in changing the proposal to suit what they client is inclined to pay—either by changing the approach or, simply, charging less. The reluctance to merchandise, an especially common attitude among technical professionals, is a recurring barrier to making the sale.

Figure 1 The Marketing-Merchandising Loop



Twenty-five Pricing Strategies

What the client wants, the Scope of Work, is partly public and partly secret. The public part is revealed in RFPs, IFBs, RFQs, and the whole family of tender documents. What the client *really* wants, or would prefer, or would settle for … these are deduced from intelligence gathering and an informed reading between the lines of the official documents.

Proposal developers, therefore, need to estimate two essential variables: exactly what the client intends to spend and exactly what the client hopes to receive for that expenditure. Given these two estimates—**price** and **scope**—the next task is to develop a pricing strategy based on the intersection of these two targets.

The most obvious strategy—to offer **exactly** what was asked for at **exactly** the intended price—is considered by many consultants a poor strategy. Although this seems a reasonable offer on its face, in most competitive bids it will be bettered by another strategy.

Table 1 shows twenty-five possible pricing strategies. This array assumes that there are five degrees on each estimate: **much less, slightly less, exact, slightly more, and much more.** The shaded cells illustrate that any offer promising **much less** than the client's expected scope of work—irrespective of price—is probably a poor bid; that is, clients do not usually perceive a bargain when they are asked to give up many of the services they were hoping to buy. Similarly, any offer that costs **much more** than the client intends to spend will also have a hard time, since, no matter how attractive the package, the client may be powerless to approve.

It should be obvious to almost anyone who has ever bought or sold anything that these nine cells are a poor offer. Yet, every day, consultants and contractors who are a bad match for the client's requirements offer to do a small fraction of the scope of work. And still others who do not understand the notion of a winning price bid whatever far-fetched amount is in the grand total box of their spreadsheet.

Even after eliminating these nine bad cells from the strategy matrix, though, there are still many choices remaining:

Table 1 25 Pricing Strategies

SCOPE / PRICE	Much Less	Slightly Less	Exactly	Slightly More	Much More
Much Less	-	+	?	?	?
Slightly Less	-	?	+	+	?
Exactly	-	-	- !	+	?
Slightly More	-	-	-	?	+
Much More	-	-	-	-	-

The strongest strategies are in the **+** boxes. Even a shallow examination of the array shows that bidding "slightly less" than the client anticipated is the best strategy, since it leads to two winners. Charging exactly what was planned works only if more service is offered; and charging more than what was planned works only if substantially more service is offered—assuming that the client has any discretion at all in exceeding the pre-set limit.

The **?** cells are strategies of uncertain effect, that is, strategies with very different results for diverse clients. While most clients will accept a slight reduction in service for a substantial reduction in cost, many clients will accept no reduction in service, irrespective of cost.

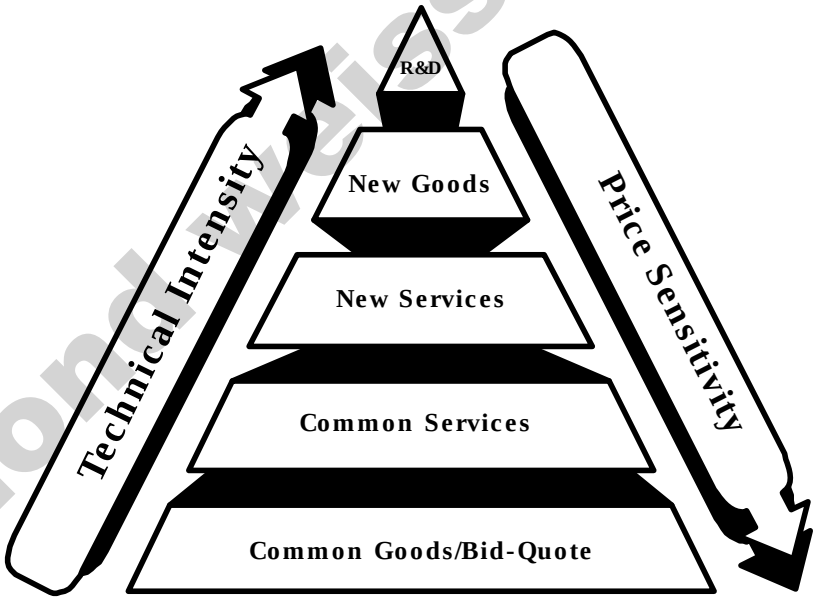
In this connection, there are several questionable strategies involving a "much lower" price. Why? Wouldn't most clients be attracted to an offer well below the authorized amount—a bargain?

The result is quite difficult to predict. Consultants and contractors should remember that the authorization or budget for a consulting contract usually has been requested and defended by the person judging the bid or proposal. In effect, accepting a bid well below the expected cost could embarrass the advocate and undermine his or her persuasiveness in the client organization. There are also many cases (for example, construction projects) where an unusually low bid is interpreted either as incompetence (the contractor misunderstands the project) or as venality (a "lowball," offered with the intention of adding charges later in the project).

Ten Ways to Justify a Higher Price

In competitive bidding, it is not enough to select *a* winning price; the successful offeror must select *the* winning price, the most attractive among the competitors. But, asks the novice, isn't that always the lowest price, or "low bid"? Not necessarily.

The terms "proposal" and "bid" embrace a wide variety of business offers, in only some of which the main determinant of success is the price, the "lowness" of the bid. In other cases, though, where the client is less clear about the work that needs to be done, the race will not always go to the cheapest. Figure 2 depicts the relative importance of price in affecting the client's choice.



This figure illustrates the complementary relationship between technical ingenuity on the one hand, and aggressive pricing on the other. At the top of the pyramid are Research and Development projects and New Hard Goods—the areas in which the client usually has the weakest conception of what needs to be done and how much it should cost. Indeed, for some R&D projects the client is not sure that the final deliverable can be achieved at all!

In effect, the client for such a project is a novice. Now matter how experienced the client firm, it cannot rely comfortably on its past to estimate the complexity and risk of solving a frontier engineering problem or designing a new generation of machines. In these cases, the client depends on the consultant to define the scope and price. (And, in fact, the favored consultant has often been involved in writing parts of the Request for Proposals.)

Generally, the newer the problem, the less familiar the domain of inquiry, the less compelling is a low bid. As I'll discuss below, a more expensive offer from a firm that *reduces the decision anxiety for the client* will often prevail over the low bid.

High prices are far more problematical in the lower half of the pyramid. Here, the clients know more precisely what they want and are mainly looking for a bargain. In extreme cases, they are able to shop from catalogs of standard products (machine parts) or commodity-like services (testing labs). These offers are more correctly understood as "bids," rather than "proposals," since the price page is often the only part of the document the client cares about.

When the offered price is slightly higher than the client intended to spend, the consultant must offer slightly more (or perhaps much more) service than the client expected. When, in a competitive bid, the offered price is higher than that of a credible competitor, then the consultant must offer at least slightly more than the competition. Either through explicit promises (when appropriate) or implicit assurances (when explicit promises are inappropriate) the consultant should use one of the ten basic arguments below to justify the fact that, although the bid is not the lowest, it is the *best*. Table 2 summarizes these "appeals":

The first nine of these ten appeals are, clearly, variations on the same theme: exceeding the scope of work, doing more than required by codes, standards, or procurement regulations. In each appeal, the client receives either a material benefit (such as reduced downstream costs) or a nonmaterial benefit (such as political favor). In competitive proposals, it is also useful to contrast these benefits with the smaller benefits in the competitors' offers.

The tenth appeal—Implied Service—also promises to exceed the scope of work—but in a more complicated and potentially inappropriate way. It argues, in effect, that most projects will not proceed as planned by either the client or the consultant/contractor, that changes are inevitable, even in uncomplicated short-duration engagements. Moreover, it presumes that contract modifications and change orders are anxiety causing for the client, sometimes even embarrassing or harmful. (That is why,in my own projects, I nearly always budget enough to allow for these contingencies; my business practice is to grant nearly all requests from a client without requiring a change order. Of course, I also adjust schedules to reflect the changes.)

But how can the consultant communicate this argument? Surely, no one suggests telling the client that the budget is deliberately heavy to allow for contingencies!

Alas, the only way to exploit this justification for higher cost is to have a relationship in place with the client, a record of past engagements, so that the client understands the consultant's attitude toward changes and modifications. In these circumstances, the client—trading money for reduced anxiety—will be less put off by the price and less inclined to shop for a lower bid.

During my years of helping R&D firms write proposals to government agencies, I became aware that a reputation for doing "only what is in the contract" eventually harms contractors, even when they bid a lower price than their competitors. Most clients—no matter what they say in public—prefer a little higher price and the far lower stress associated with a more loosely budgeted project.

Table 2 Arguments Supporting a Higher Price

Appeal	Explanation
Precision	The project exceeds the specifications, especially when the client asks only for "code" minimums and the consultant disputes the wisdom of these standards.
Redundancy	The design contains added layers to provide safety margins and minimize downtime for repairs and maintenance or scheduling surprises.
Durability	The consultant will use such methods and materials and anticipate downstream events so as to ensure the viability of the project beyond the planning horizon of the client organization.
Scarcity	The consultant reminds the client that certain personnel and materials are, at the moment, in short supply and must be obtained at a premium.
Guarantees	The consultant or contractor warrants the products and service in some exceptional way, removing some of the downside risk to the client by making all or part of the fee contingent or refundable, or by guaranteeing later maintenance and support services at no charge.
Top People	The consultant has selected this project as a showcase, promising special attention from the corporate leadership and pledging to staff it with "star" investigators and researchers—in effect assigning people who are overqualified and, therefore, exceed the specification.
Offset	The project uses materials and methods that eliminate other costs, such as goods with a much longer duty cycle, technology without "consumables," or internal subsystems that eliminate the need for certain external systems, such as inspection and security.
Job Creation	The consultant or contractor promises to staff some of the project with local workers, chosen in conjunction with the client (even though the local labor rates are not the most attractive or the local workforce the best qualified), thereby providing a strong political benefit to the client.
Social Benefit	The consultant or contractor is a "socially deserving" businessperson, entitled either to official government set-asides or to unofficial special consideration, the social benefits offsetting some of the diseconomies.
Implied Service	The most delicate of all arguments is the notion that the project budget is high enough to support changes and additions without the need for change orders or contract modifications, an arrangement that especially appeals to many government clients.

Best and Final…

Once a proposal is on the verge of acceptance by a client, the consultant/contractor will often be asked for the "best and final offer," the lowest price he or she will accept for the engagement. Here, the conventional wisdom is that the winner will nearly always drop the price slightly. The rationale is that most clients who buy professional and technical services believe that the estimates are inflated a bit and can be trimmed. Over the years, of course, this becomes a self-fulfilling prophecy as bidders anticipate the best and final transaction and inflate their estimates in response.

My "final" advice is that *consultants and contractors should always reduce their bids slightly at this point, but also should remove an item or two from the Statement of Work, typically items included in the plan for just that purpose*. Of course, everyone knows that estimates are imprecise and everyone knows that there is often extra money for "implied service." But it is still best, though, to sustain the fiction that the budget is austere and based on an objective analysis of the tasks to be performed, rather than on what usually wins: a intelligence-based estimate of the winning price.

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Does Grammar Count in the Era of E-Mail?

Is e-mail the end of 'correct' communication? Do spelling, punctuation, and grammar matter anymore? Only as much as the recipient of the message matters. All professionals should care about the image they communicate, even in their informal messages.

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The most important technical question is "How's Business?" Technical professionals must learn to pitch improvements and changes in their departments through business-savvy business cases: proposals aimed at one's own management. Business cases must show how the new procedures or technology will either make or save money, and within an acceptable number of months.

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