Price vs Cost

- Pricing serves many purposes
  - New customers, competition, move inventory, and sometimes make a profit
- Price is arbitrary
  - Prices can be negotiated
- Costs are business expenses
  - Costs must be mitigated or avoided

Agenda

1. Why Cost?
2. Direct vs Indirect Costs
3. Strategies and Tactics
4. Path Forward & References
Pricing Models

- Market based
- Market share
- Competition based
- Loss Leader

Seller Costs = Buyer Price

- Direct
- Adders
  - Labor
  - G & A
  - Fee
  - Overhead

Real Life Tactics

- Baker’s Dozen
- Buy 11 – get one free
- Price Break if you buy 12
  - Do these tactics increase sales?
  - Why do they work?
  - Is the supplier negotiating?
  - What is supplier leveraging?
Why Cost Analysis

- **Why Cost Analysis**
  - www.mltweb.com/tools/why_cost.htm
- Changes which can increase TCA/TCO
- Price escalation
- Post award changes, rejections, partial cancellations, spare parts, reorders, outages

Direct Materials

- Raw materials needed to make the product
- As a large/small percentage of total cost
- Material substitution, subcontracting, strategic materials, inventory value, acquisition costs

Direct Cost items

- Position numbers for Spare Parts
Direct Labor

- Labor to fabricate and provide service
- As a large percentage of total cost
- Labor categories
- Learning Curve, setup time, efficiency

Indirect Costs

Why Negotiate Cost?

- Contract relationship = exchange of value
- Quality / Accuracy = more cost
- Motivation / speed = more cost
- Risk avoidance = more cost
- Contingencies / unknown factors > cost
- Cost Value is relative
When General Mills & Costco team up to sell consumers an 8lb box of Cheerios

- What are they using for leverage?
- Do we buy it?

- Are we negotiating?

## Negotiation Strategy

- Aim to reduce Total Cost of Acquisition
- Look for opportunities to avoid direct costs
- Look for ways to leverage expenditure to maximize the return
- Increase the contract value by including extras
- Evaluate Seller’s costs

## Gathering Data

- The power of a solicitation
- Fact finding
- Factory visits
- Industry news
- Asking questions
- Separating facts from fiction
- Purchasing Records
Manipulating Price

- What is the value to seller of offering quantity discounts?
- What does it cost the seller to offer quantity breaks?
- Parametric Pricing
- Bulk pricing
- Distributor discounts

Break Even Analysis

- Fixed Costs vs. Variable Costs
- Calculating profitability and quantity
- From a buyer’s perspective to amortize direct costs of special tooling

Cost Variables

- **100 or Not**
  - www.mltweb.com/tools/100_or_not.htm
- Scrap and rework
- Residual value & beneficial reuse
- Quantity and trade discounts
- Consolidated purchasing agreements
- Long term-relationships
The Federal Government

- CAS & disclosure statement
- Certified cost & pricing data
- TINA
- DCAA, ASPM & DCAA audit guidelines
- GAO & IG
- FAR part 30 (CAS) & 31 (financing)
- Buyer determinations

We Care About Supplier Cost

- Cost Counts
  - www.mltweb.com/tools/costcounts.htm
- Direct impact to selling price
- Long Term impact to Supply Chain health