PROFESSIONAL PPS PRICING SOCIETY™

The PRICING ADVISOR

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In this article, the author explores why currency risk management should become an integral part of a pricer's risk assessment process. Stephan M. Liozu is Chief Value Officer of the Thales Group. He is also an Adjunct Professor & Research Fellow at the Case Western Research University Weatherhead School of Management. He holds a Ph.D. in Management from Case Western Reserve University (2013), is a Certified Pricing Professional (CPP), a Prosci® certified Change Manager, and a Strategyzer Business Model Innovation Coach. He authored three books, Dollarizing Differentiation Value *(2016),* The Pricing Journey *(2015) and* Pricing and Human Capital *(2015). He sits on the Advisory Board of LeveragePoint Innovation and of the Professional Pricing Society. He is a Strategic Advisor to 360pi, The Kini Group, and PriceSenz. He can be reached at sliozu@gmail.com.*

Agile Pricing in an Age of Currency Volatility

Over the past three years, we have witnessed a series of dramatic changes in global business dynamics. We all know the world of business is changing faster every year. We have to anticipate even more turbulence with the rise in protectionism and in regionalization of certain components of our marketing strategies. **One of the most powerful changes is in the area of currency volatility and how it impacts pricing management.** Over the past few years, certain world leaders have started using currencies as a competitive weapon to reinforce national interest and to stimulate slowing economies. Currency forecasting in business planning has been difficult in light of political instability and radical shifts in trade policies. Although as pricing professionals we do not control currencies, there are questions to ask ourselves and steps we can take to better control the impact of currencies on pricing and profit levels.

The Forces of Disruption

Whether your business is local, international, or global, you will be impacted by currency swings. It is inevitable. The impact may be frontal in your purchasing of products (raw materials, equipment) and services (shipping, outsources IT services) or it might be indirect when inflation rises due to the rising cost of your supplies. Businesses have to be ready to face more pressure and to plan to manage the impact. In fact, currency disruption is only one of the forces of disruption impacting profitability and pricing these days. I list five of the most potent ones below.

Greater currency "manipulation": There is no doubt that keeping the value

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of a currency low provides an advantage to export for the firms residing in that specific country. I am not going to mention any country names but it is obviously one of the most direct ways to give an unfair advantage to exporting businesses. For countries with weaker innovation and industrial policy, it is also the easiest way to stimulate GDP growth.

1. **Regionalization of needs and national preference:** Some global businesses export in US dollars or Euros and compete against local producers which sell in local currencies. Recent elections in developed countries tell us that there is a return towards national preferences and things made locally and also priced in local currencies. Some call it Globalization 4.0 which consists of global business strategies and a very local footprint.

2. **Unfolding of economic alliances (Brexit):** The Brexit came as a surprise for many people in Europe. Other countries might leave the Euro block and return to their local currencies. This reinforces point 3 in this list and a potential return to more local economies. In such a scenario, the impact on firms' go-to-market strategies can be dramatic.

3. **Government intervention in sensitive areas:** Recent developments in the health care and pharmaceutical US markets have shown that pricing is a sensitive topic and one that raises ethical concerns. The US is not alone and governmental interventions can take a toll in an industry especially when the country GDP relies on it. Generally, that also depresses currencies as it reduces investors' confidence in the country institutions.

4. **The foreign exchange (FX) market:** Like any financial sector, the FX market has become an area of high speculation within financial markets. Changes in currencies are not necessarily the reflection of a world event, a decision, or any other rational episode. They can come from the buy/sale of currency positions leading to currency price variations. The winners in this area are high frequency FX traders. We need to learn from them and accept that currencies are changing dynamically and so should our pricing models if currencies impact them.

Control what you Can Control

While we do not control currencies, we have to adopt a proactive and intentional strategy which reflects the potential exposure to our business. In fact, currency risk management should become an integral part of the risk assessment process. I propose six areas where business professionals can improve their readiness level:

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1. **Traditional foreign exchange tools are not enough:** You cannot manage this new level of currency volatility using the traditional hedging and FX management tool. In fact, these days, hedging might be more dangerous and risky. Your commercial banks might also not be able to provide relevant risk management when currencies are fluctuating fast and political events are unfolding in a surprising way. Finally, parking your cash in foreign country might also increase your exposure to continued currency conflicts. In 2017, currencies seemed to have stabilized in more predictable ranges after two years of chaotic environment.

2. **Get your pricing, sourcing, and finance teams aligned:** When your business is exposed to currency war and rapid swings, your teams have to be even more connected. I often recommend the creation of a currency management task force within or separate from the pricing council to evaluate the on-going currency impact in the business from finance, supply chain, and pricing. This task force can propose to leadership the quick adjustments needed due to currency changes and also communicate proactively to the global business.

3. **Accelerate the speed of your decision making process and tactics:**

   When currencies change daily on a business around the world, business leaders need to establish more agile organizations and processes to make quicker pricing adjustments. This is a potential limitation of a centralized or center-led pricing organization. Local business and commercial leaders cannot wait for input from a central team to make necessary adjustments to pricing when they are competing with local companies. That might explain why some of the largest global companies are in the process of moving pricing authority to regions and local business units so that they can react faster within new pricing guidelines.

4. **Prepare a robust pricing tool box:** Control what you can control. Have a tool box ready with all relevant tools and methods to manage currency changes in a proactive fashion. This tool box might include:

   - A currency dashboard communicated on a weekly basis and readily available to all business leaders.

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- New long-term pricing agreements with relevant currency clauses to manage the need for pricing renegotiation and potential exit from the agreement.
- Template for currency-based formulas to be used in new agreements whether long-term or short-term.
- Dynamic pricing guidelines describing the threshold for price adjustments when needed.
- Standard communication bullet points to handle pricing objections and currency questions.
- Value maps in local currencies to position competing brands in a local market.
- Guidelines to manage increased premium differentials versus locally-made products and services.

5. **Take the opportunity to establish local business:** The recent political environment around NAFTA has created a currency threat for US business exports but also an opportunity to establish local base for business when currency is moving in a favorable position. No one can predict the future of NAFTA but what is for sure is that US business will continue to do business in Canada and Mexico. It might time for leaders to establish more solid businesses by wisely investing in infrastructure and conducting business in local currency.

6. **Train local leaders who might be exposed to currency swings:** As you better control what can be controlled, one of the critical efforts is to get local teams trained to the volatile nature of the currency and pricing relationship. Currency volatility is here to stay. It needs to be managed holistically and dynamically. Training programs need to include topics related to currency, inflation, protectionism, and national preference.

Conclusions

You may think you are not in control of currencies. Of course you are not. My view is to control what you can control, then prepare for the worst and hope for the best. You have to get proactively ready for the next wave of currency disruption which might happen in the near term. This is what I call "agile pricing management." As currencies are used more and more as trade and competitive weapons, it is up to us to prepare our teams and our management for the dramatic implications of currency tensions. Think about the implications to your bottom line when the Euro collapsed from 1.45 for 1 US dollar to 1.10 for 1 US dollar. What is the next currency to rise or collapse? How ready are you?