Where are the smiles?

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Dateline: Yourcity, Northeast U.S.A., July 15, 2006
"Customers complaining about how high oil prices are. Threaten to leave companies offering cap prices to companies offering fixed prices."

Dateline: Yourcity, Northeast U.S.A., September 15, 2006
"Customers complaining about falling prices. Want to quit fixed price deals, and go back to cap price offers."

Dateline: Yourcity, Northeast U.S.A., November 15, 2006
"Customers complaining....... because that is what they do!"

Over the past five years, the battle has raged over WHAT pricing structure is best to offer to a customer. For those who are sure that prices will do nothing but rise, the answer would be to lock in prices ahead of time, and to sell the customers a fixed price. For those who are sure that prices will fall, the answer would be to just sell a variable, rack-plus price. The first (fixed price) group suffers the risk that prices may fall, making their offered fixed-price well higher than what others might be paying by the time the winter shows up. The second (variable) group suffers the risk that prices will continue to set record highs each year, and that customers will just leave—in search of a better "program".

In the past, and especially in the last five years, the notion of offering a cap has taken root. The cap has some of the benefits of a fixed price, in that prices, although they can increase a bit, have a ceiling, and will not exceed that ceiling, regardless of how high the cost of oil may go. In addition, and similar to that of variable prices sales, the cap has the benefit that should prices fall, the price to the customer will fall as well.

Sounds simple enough, so why do ANY customers still buy fixed or variably priced oil?

The answer is two-fold. The first part is that customers are, for the most part, creatures of habit, and will listen to the "logic" of their oil dealer. If the dealer says "fixed is the way to go", so be it—we'll go fixed. If the dealer says prices are going to fall, "go variable", then that is the way to go. If companies offer a cap, with an explanation of the benefits of a cap, then, lo and behold, customers sign up for the cap. There is no doubt that owners and managers of companies do have a hard time with "the rest" of the customers—those who don't follow blindly, and, admittedly, that number is increasing each year.

The second reason is that each year, the cost—premium—to offer a cap, instead of fixed or variable, seems to increase. What used to cost 4 or 5 cents per gallon, moved to 10 to 12 cents two years ago, and is now in the 16 to 18 cent per gallon range. So, although the benefits of the cap might sound great, it is quite expensive to offer. This second reason leads to a lot of introspection, along the lines of "Will I be able to collect that extra margin in order to afford the cost (premium) of the cap that I want to offer?"

Sitting here, as NOT an owner of an oil company, it is quite easy for me to espouse all the benefits of the cap, and to point out the great potential for margin increases that fixed-offers don't have, and the peace of mind that variable offers don't have. However, the bottom line still comes back to the conviction of the owners, and the ability to have the thick skin and to recognize that many customers will call, some will be angry, and still others will just quit.

So, why am I looking for smiles, when this summer has been a tough one to market to your own customers, let alone if you are looking to add customers? Over the past few years, most cap-offering companies have suffered through summers in which they were scrambling to keep customers, despite raising the cap level from year to year. On top of that were the annual, "you tell me it's a cap, but I never see prices lower than the cap—just call it a fixed price, already!!" conversations. From the customer's point of view, the thinking is logical. After all, they signed up for a program that was supposed to lower their costs if prices went down. How can it be that prices never fall?

Fast forward to the spring and summer of '06: Prices continued their five-year ascent towards $2.50 per gallon at the rack, and well over $3.00 per gallon retail. Companies, whether they ratably bought—as we strongly recommend—or just pulled the trigger one day, hit the streets with their cap offers, and waited for "it" to hit the fan. In some cases, the customers had been so numbed by what else they saw—gasoline at $3.25/gallon, pending military conflict with Iran, Hezbollah launching rocket attacks against Israel, etc.—that the capped offers, whether at $2.699/gallon or $3.299/gallon-—were just met with a sigh and a signature. In other cases, it was the straw that broke the camel's back, and many long-term customers went shopping.

By this point, especially after seeing retail prices triple in a five-year period, the shoppers weren't looking for better service, they weren't looking to take on the risk that prices might triple yet again, nor were they looking to just save a few cents per gallon. They wanted "real savings"—10-cents, 20-cents, 30-cents per gallon. As many of us have become aware, there is a dangerous, double-edged sword game going around that has some companies offering "new customers" dramatically discounted fixed-prices, with the misguided notion that "next year"—after teaching the new customer the value of shopping for a bargain price—margins would magically increase, and that the customer would be content to stay.... didn't you just get him ONLY because of your low price?!?....but I digress. Inevitably, the "lost customers" found themselves "elsewhere" with fixed-prices, often at least 20 cents lower than the cap levels. Fair enough—decision made.

However, once prices peaked at the end of July and into early August, a funny thing started to happen. Fixed-price customers were paying (as they had contracted for) a fixed-price that did not change despite the 50-cent per gallon drop (as of this writing) in heating oil prices. The capped customers, with those "high" price caps? The caps are still high, BUT the price that the capped customers are paying is well below the cap level, and (here is where it gets to be fun for the cap-offering company) well below the fixed-prices that the customers left for, in the first place.

Yet, there are still complaint calls. However, those calls are from the customers who keep hearing on the news that gasoline prices have fallen 50 cents per gallon, and that crude oil prices have fallen $13 per barrel, and they want to know why the cap isn't lower. So, without ringing their necks (and, unfortunately, some don't even let you explain that that cap is the MOST, and that they are currently paying much less), you still need to take the time to explain that in return for the fact that there is a cost to be a cap customer, the benefit should be as clear as the nose on their face. It's easy to lose your cool when dealing with customers who are being barraged by full-page ads, and telemarketed with "misinformation".

All that said, if you are delivering oil at a lower price than most of the customers who left are paying, and if you are making your full margin-—with the likelihood of widening your margin, and you and your customers have the piece of mind of knowing that IF prices do spike up again to new record highs, that you are covered....."Where are the smiles?"