

# Report on the strategic environment of ie and what course should the company take...

[Business](#), [Strategy](#)



A pricing strategy can be considered the most important aspect of your business, as well survival tool for some companies. Since physical products consist of direct materials and indirect cost it is important to understand the costs structure to determinate the selling value that at least covers all of them. When it comes to services, there is more challenging part, mostly because of subjective evaluation of the final output. The problem that I address in this report is which approach should be implemented by IE when pricing their MBA program. Should it be target pricing or cost-plus pricing system? Which is the most suitable taking into consideration the specific environment, competitors, costs, and overall industry of the higher education. Understanding pricing is essential to the success of any business.

A small group of Spanish entrepreneurs, who envisioned a dynamic and innovative institution driven by academic excellence and an entrepreneurial mindset, created IE in 1973. Since then, the visionary leadership has shaped the school into one of the leading educational institutions worldwide. The level of quality of IE master's and executive education programs have placed IE among the best in the class in international rankings brought up each year by important publications that include Financial Times, BusinessWeek, Forbes, The Economist and more. IE is not only known for its innovative approach diversity and the urban campus located in the center of Madrid, but also for its entrepreneurial mindset and great program curriculum. As for today, approximately 1, 900 students from 90 countries undertake degree programs at IE each year.

## **Strategic environment IE**

Business School has a powerful brand and international recognition across the globe. Price of the program itself reflects the high quality of the service and is very strongly aligned with the customer's perception when completing the purchase. Each year institution revises the final amount of tuition fees relying on the benchmark process of direct competitors. However, costs of the program vary from one year to another. For example, due to the expulsion from the FT ranking, some departments spend a lot more of a planned budget on specific activities to ensure the minimum amount of the students enrolled in the program. Moreover, special sections and task forces were created just for the crisis management as well as promotional activities were implemented marketing division. In this case, the numbers should be reviewed on that matter so calculate correctly the cost of each department taking part in the creation of the final product – the delivery MBA program.

### **The structure of the company and cost composition**

Different departments at IE Business School are involved in the creation of the final product, which is MBA program. Some of them work closely on the execution such as program management, faculty body, student services or campus life. The other divisions put all the efforts prior and post the program to ensure the highest quality of the service: admissions, international development, business innovation, IT, HR, controlling, administration, alumni etc. When taking a depth look into MBA program itself we can recognize some of the direct costs that can be traced as well as indirect ones that need to be allocated. I will try to differentiate some of them:

Ø direct costs: faculty payments, materials needed for the class, salaries of academic team, equipment.

Ø indirect costs: maintenance of the buildings, rent of different spaces, bills for energy and light, general office expenses, cleaning services.

A unit cost (average cost) can be calculated by dividing the total cost by the related number of educational services produced. Decision rule: choosing the program that produces the highest contribution margin per unit of the constraining resource. It is important to keep in mind non-quantitative factors, which are extremely important in an evaluation process, (yet do not show up directly in calculations) in IE Business School case. Quality Requirements, Rankings, History & Reputation, Location is something that goes beyond a clear numerical calculation and adds value to the customer's journey.

### **ABC costing at IE**

More and more programs are constantly added to IE higher education offer due to the constant changes in the market, therefore I would also consider the use of ABC (activity-Based Costing) to determine the right allocation of indirect costs to IE services (based on the factors that most influence) and to control the use of resources in particular activities. Only in 2017, students were able to choose from a greater variety with five new proposals within the school of masters. Even though it takes time to recognize profitability on the new entries, the company should be aware of which products are more and less productive over time. Moreover, with such a wide offer range, there are still business units, which devote more attention and work to individual

products/services, therefore, required time to perform the work differ on each cost object.

In addition, Different academic units consume resources in different proportions This means that costing process in the organization needs to be forward-looking, and ABC is a tool for such analysis. Steps of application ABC costing approach at IE:

Identifying cost objects – for example the cost of delivering single MBA cost. The cost unit would be calculated as cost per student.

Identifying activities – what activities are need to deliver the desired results (course/program). Some of the activities for allocating indirect costs to products: design, student services, admissions, administration, HR, IT etc.

Allocating resources and making cost pools – depending on the direct/indirect costs recognition, resources cost are allocated to cost pools (recognizing cause-and-effect relationship between the cost-allocation base for an activity and the cost)

Linking Indirect Costs Allocated to the Products 5. Total Cost of the Products by Adding All Direct and Indirect Costs Assigned to the Product ABC Cost system should be very profitable for product managers at IE, thanks to valuable information of accurate cause-and-effect relationship for each activity pool. Since there is a significant amounts of indirect costs related to the service, it would help to realize top products of IE´s portfolio as well as focus on how and where to reduce cost without compromising student

perceived value. Always following the Decision Rule, which emphasize the selection of the option that will provide the firm with the lowest cost, and therefore the highest profit.

## **What approach should ie take in order to price the service of the higher education?**

**The reasons why IE should go for the target pricing instead of cost-plus approach:**

- Ø Price is largely determined by supply and demand;
- Ø Perceived value plays a crucial role in the price setting process;
- Ø Competitors use benchmark to update the tuitions fees every year;
- Ø Reputation and international recognition add value from the consumer's perspective;
- Ø Production of quite homogeneous products;
- Ø The intensity of the competition;
- > Ø MBA program is periodically reinvented and aligned with market changes that is why product's planning and design phase are crucial in the life cycle of the product;
- Ø Existence of the locked-in costs.
- Advantages for IE business school
- Ø future product development and cost reduction;
- Ø greater profitability;
- Ø requires and pushes for innovation to keep competitive advantage;
- Ø involves customer in the service design – that is why the program in 2016 was updated;
- Ø greater collaboration between departments.

**Disadvantages**

- Ø price is limited by the perception of the market – negative impact when FT IMBA got expelled from the ranking;
- Ø Time-consuming, requires on-going research and data analysis;
- Ø must be a highly disciplined process, difficult to reach a consensus.

Pricing decision is a complicated process that involves both quantitative and qualitative factors. The specific character of the top-quality service at IE Business School and competitive environment require a depth look into costing system to ensure a company's profitability in the long term. The theory learned along the managerial Accounting course, led me to conclusions that organization that I am currently working for should implement both ABC costing system as well as follow target costing approach for the existing and new programs joining the composition of the masters portfolio.