U.S. Producer Price Index for Management Consulting Services

Roslyn Swick
Chief, Branch of Industry Pricing
Producer Price Index
Topics

- Output Definition
- Classification
- Pricing Methodology
- Quality Assessment
Output Definition

Provision of advice and assistance on management and general business issues and problems
Output Definition

More specifically . . .

Provide objective information, advice and guidance to clients, and, when requested, assist in the implementation of their recommendations.
Output Definition

Areas of advice include . . .

- High level strategic & organizational planning
- Business financing
- Budgeting
- Employee hiring
- Benefits & compensation issues
- Marketing
- Production & logistics
Output Definition

Also includes the distinct activity of executive search consulting according to NAICS

Executive search is the identification and evaluation of candidates for senior-level executive positions
Classification

- PPI for Management Consulting Services corresponds to the 5-digit NAICS code 54161

- In order to be consistent with PPI systems, this has been re-coded with the “false” NAICS code 541610
Classification

The five 6-digit NAICS industries that compose 54161 are included as product line detail . . .

- Administrative Management and General Management Consulting Services
- Human Resources and Executive Search Consulting Services
- Marketing Consulting Services
- Process, Physical Distribution, and Logistics Consulting Services
- Other Management Consulting Services
Classification

- 6-digit detail exactly matches turnover data collected by Census

- No turnover data collected for detail below the 6-digit level
Classification Issues

- Companies transitioning from pure advice to *implementation* as well . . .
  - Business process management services
    NAICS 518210
  - Computer systems design
    NAICS 541512
- More difficult to classify companies
Classification Issues

- Executive search services moved to this industry with implementation of NAICS.

- In 2007, executive search services reclassified as a unique 6-digit industry in the Administrative and Support Services subsector.

- Easy to implement this change since executive search companies provide this service only.
Pricing Methodology

Unit of measure is per project or engagement . . .

- Series of time-based (hourly) fees for the individual professionals working on the project

- Unit fees may also be charged in addition to professionals’ hourly rates
Pricing Methodology

Realization Rates

Percentage of hourly rates actually received for providing service

For example . . .

If a consultant lists a rate of $100 per hour and records a realization rate of 80%, he is receiving $80 per hour.
Pricing Methodology

Two pricing options . . .

- Average realization rate - *preferred*
  Compares total revenue for all projects within a service area to total amount that would be received if billing at listed rates

- Project-specific realization rate

Both options are model prices
Pricing Methodology – Example


Partner $200/hr x 20 hours = $ 4,000
Associate $125/hr x 60 hours = $ 7,500
Jr. associate $ 75/hr x 90 hours = $ 6,750
Support staff $ 20/hr x 20 hours = $  400
Total = $18,650

Service line average realization rate = 65%

Total realized billed rate = $12,122.50
Transportation – travel expenses = $  2,500.00
Telephone expenses = $  650.00
Total price = $15,272.50
Pricing Methodology – Example

Price change

Technology improves and the *exact same service* can be provided in less time

This is a price change . . .
Pricing Methodology – Example


Partner $200/hr x 10 hours = $ 2,000
Associate $125/hr x 50 hours = $ 6,250
Jr. associate $ 75/hr x 80 hours = $ 6,000
Support staff $ 20/hr x 10 hours = $ 200
Total = $14,450

Service line average realization rate = 65%

Total realized billed rate = $ 9,392.50
Transportation – travel expenses = $ 2,500.00
Telephone expenses = $ 650.00
Total price = $12,542.50

Price change = -17.88%
Pricing Methodology – Example

Quality change

Technology changes such that the client no longer requires assistance with implementation resulting in less time needed to provide the service

This is a quality change . . .
Pricing Methodology – Example


<table>
<thead>
<tr>
<th>Role</th>
<th>Hourly Rate</th>
<th>Hours</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Partner</td>
<td>$200/ hr</td>
<td>10</td>
<td>$2,000</td>
</tr>
<tr>
<td>Associate</td>
<td>$125/ hr</td>
<td>50</td>
<td>$6,250</td>
</tr>
<tr>
<td>Jr. associate</td>
<td>$75/ hr</td>
<td>80</td>
<td>$6,000</td>
</tr>
<tr>
<td>Support staff</td>
<td>$20/ hr</td>
<td>10</td>
<td>$200</td>
</tr>
<tr>
<td><strong>Total staff</strong></td>
<td></td>
<td></td>
<td><strong>$14,450</strong></td>
</tr>
</tbody>
</table>

Service line average realization rate = 65%

Total realized billed rate = $9,392.50
Transportation – travel expenses = $2,500.00
Telephone expenses = $650.00
Total price = $12,542.50

Price change = 0%
Pricing Methodology

Respondent updates . . .

- Hourly rates for each professional
- Realization rate
- Estimated cost of travel and business expenses
Pricing Methodology

Average Realization Rate

Advantages . . .
- Price includes discounts
- Reflects broader range of services

Disadvantages . . .
- Inappropriate if mix of clients and/or hours billed affects price charged
Pricing Methodology

Project-Specific Realization Rate

Advantages . . .
- Continuously price a unique service
- Alleviates respondent burden

Disadvantages . . .
- Discounting not readily captured
- Substitutions are difficult; difficult to assess quality differences
Pricing Methodology

Executive Search Services

- Model price
- Percentage of total first year compensation of placed executive
- Update estimate of compensation and percentage fee
Quality Assessment

Lower score for preferred price
81.25 compared to 87.5 – both Type B deflators

Why?

- Mix of contracts is non-homogeneous
- Flaw in weighting of model prices
  Model price is never Type A with current weighting scheme