THE QUALITY PULSE

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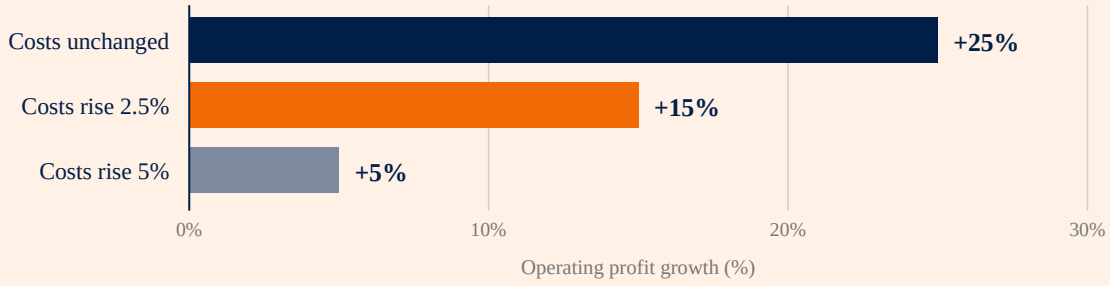
The Hidden Value of Pricing Power

Why the ability to raise prices without losing customers supports durable profitability

A price increase puts a customer relationship to the test. The customer can pay more, buy less or look elsewhere. A business with pricing power can raise the price while preserving enough demand to strengthen its economics over time. That ability deserves close attention: it can protect profits when costs rise and help earnings grow without a matching expansion in factories, inventories or staff.

Consider a company with an operating margin of 20%. If it raises prices by 5%, sells the same quantity and keeps costs unchanged, operating profit rises by 25%. Its margin increases to 23.8%. The gain is disproportionate because the extra revenue arrives without the cost of producing more units. This is an illustration, not a forecast, but it explains why modest price increases can matter so much to shareholders. Price-driven growth can increase earnings without a proportional increase in invested capital, supporting higher returns on capital and long-term value creation.

A 5% price rise can have very different profit outcomes



Illustrative author calculations, not a forecast. Starting operating margin 20%; price +5%; unchanged volume and mix.

SOURCE: HQAM, ILLUSTRATIVE CALCULATION

INVESTMENT PERSPECTIVE

Pricing power is most valuable when customers keep buying after prices rise. For investors, the test is whether a company can protect profits while preserving future demand – and whether its share price already assumes too much.

Sources numbered [1]–[10]: full references on page 4

Inflation makes the distinction more important. Raising prices merely to recover higher wages or material costs may preserve earning power rather than improve it. During shortages, even ordinary businesses can charge more until supply catches up. Durable pricing power survives beyond those favourable conditions because customers continue to value the product more highly than the alternatives.

The arithmetic also explains why headline pricing can mislead. In the same example, if all operating costs rise by 5%, operating profit grows by only 5% and the margin stays at 20%. Customers may also buy fewer units or wait longer between purchases. A successful price increase must therefore be judged alongside costs, volumes and the investment needed to keep the product attractive.

WHY CUSTOMERS ACCEPT A HIGHER PRICE

That value takes different forms. A trusted consumer brand can reduce the perceived risk of choosing badly. A specialised component may cost little relative to the equipment it protects. Software embedded in daily operations can be expensive and disruptive to replace. In each case, the customer weighs more than the purchase price. The strength of the advantage depends on how difficult it is for a competitor to offer a convincing substitute. Döpper et al. (2025) find that rising markups in US consumer goods were associated with declining consumer price sensitivity as well as lower marginal costs. Understanding the source of that reduced sensitivity matters more than observing high margins alone. [8]

Luxury provides particularly fertile ground for pricing power. Buyers pay for craftsmanship and design, but also for identity, heritage and the experience of owning something distinctive. Those qualities cannot be replicated simply by producing a cheaper object with the same practical use. Several leading luxury houses therefore have the foundations for lasting pricing power. Yet the advantage belongs to individual brands and products; membership of the luxury industry does not confer it automatically.

Hermès illustrates how those foundations are maintained. Its integrated production model, investment in artisan training and gradual addition of workshops support quality as the business expands. For its most coveted bags, limited availability also reduces the need to compete for customers through price. The economic logic is that growth should preserve the characteristics people value. Expanding output too quickly could undermine the desirability that makes the business so profitable. [1]

The financial evidence is consistent with that logic. Hermès increased prices by around 6–7% in 2025, while revenue grew 8.9% at constant exchange rates and its recurring operating margin reached 41.0%, versus 40.5% in 2024. [1, 7] These figures support the case for pricing power, although they do not isolate volume growth: product mix also matters. High margins are supporting evidence, rather than proof on their own.

WHEN PRICE RUNS AHEAD OF VALUE

Burberry’s earlier experience shows what happens when that link between price and perceived value weakens. In November 2024, its new chief executive, Joshua Schulman, acknowledged: “We took pricing too high across the board.” The company’s strategy review was especially clear about leather goods: prices had not always matched the brand’s authority in that category. Burberry had a strong heritage in outerwear and scarves, but customers did not automatically assign the same value to its handbags. Its attempt to move further upmarket also moved away from familiar designs and core customers. [5, 6]

In the half-year to September 2024, comparable retail sales fell 20%, while the adjusted operating margin declined from 15.9% to −3.8%. Pricing was only part of the problem; weak luxury demand and inconsistent execution also contributed. The lesson is nevertheless clear: management cannot create customers’ willingness to pay simply by choosing a higher price. Rotemberg (2005) models how perceived unfairness can provoke customer anger at price increases, highlighting the importance of customers continuing to regard prices as justified. [9] Burberry’s response was to refocus on its strengths and align prices more closely with its standing in each category. [5]

Sources numbered [1]–[10]: full references on page 4

6–7%
Hermès price increases in 2025, while revenue grew 8.9% at constant exchange rates
SOURCES: HERMÈS [1], REUTERS [7]

41.0%
Hermès recurring operating margin in 2025, versus 40.5% in 2024
SOURCE: HERMÈS [1]

−20%
Burberry comparable retail sales in the half-year to September 2024
SOURCE: BURBERRY [5]

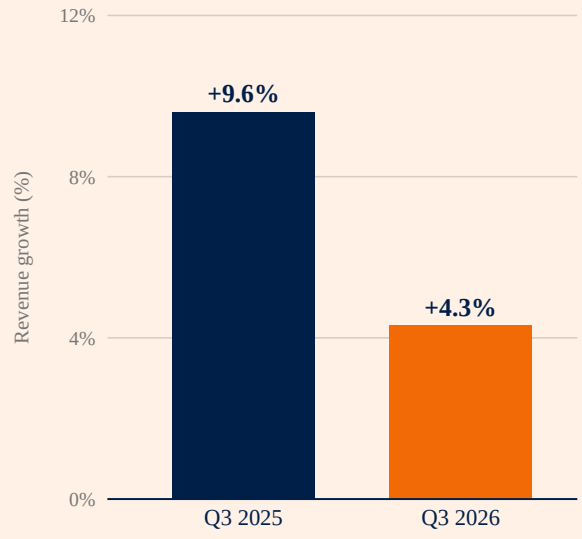
−3.8%
Burberry adjusted operating margin in the same half-year, down from 15.9%
SOURCE: BURBERRY [5]

WHAT THE 2026 MARKET REVEALS

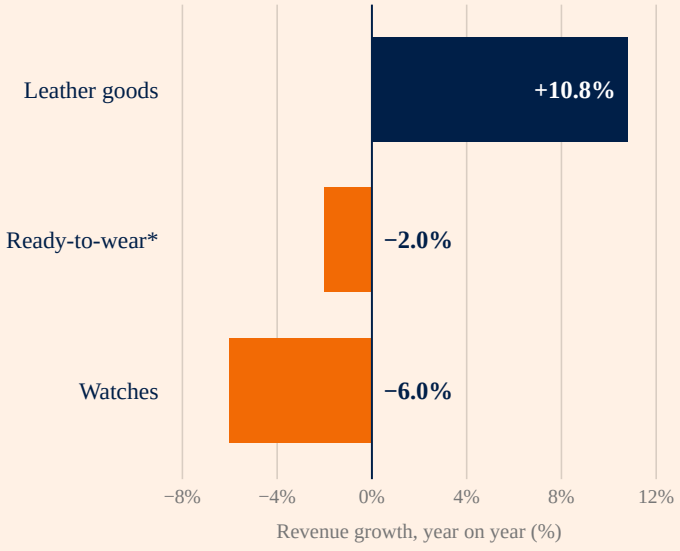
The contrast between Hermès and Burberry raises a question: how far can a brand push prices before customers reconsider? In 2026, luxury shoppers are becoming more selective. Although Bain expects modest growth for the industry overall, many fashion and leather-goods brands are still struggling. Customers may be willing to pay more for something they truly want, while postponing another purchase or deciding it no longer feels worth the money. A famous name alone does not settle that decision. [4]

Even Hermès is experiencing this shift. Its coveted handbags continued to sell strongly in the third quarter, while sales of clothing, accessories and watches declined. Overall revenue growth slowed; the latest reported half-year profitability remained exceptionally high. [1, 2, 3] This helps explain both the value and the limits of pricing power. A strong brand can give a business room to protect its profits when spending weakens, but it cannot make every product equally desirable. Customers still have to feel that what they receive is worth what they pay – and that judgement is renewed with every purchase.

Hermès group revenue growth



Hermès Q3 2026 by product category



*Year-on-year growth at constant exchange rates. *Including accessories.*
SOURCES: HERMÈS [1, 2]

THE VALUE OF PRESERVING THE RELATIONSHIP

For investors, the most useful evidence appears after the price increase. Are customers returning? Are volumes and market share holding up relative to the market? Is revenue growth supported by higher realised prices, or by selling a more expensive mix while fewer people buy? Rising discounts, unsold stock and weaker repeat purchases can reveal damage before it is obvious in headline profits. A strong quarter is less persuasive than repeated acceptance across different economic conditions.

Good management also recognises that the maximum achievable price need not be the best long-term price. In a randomised field experiment, Anderson and Simester (2010) found that customers exposed to lower subsequent prices for previously purchased products reduced future purchases. Although this concerns price reductions rather than increases, it illustrates the lasting consequences of perceived pricing unfairness. [10] Leaving customers with a sense of value can encourage repeat purchases and make it harder for rivals to gain a foothold. Pricing power must be renewed through product quality, service and innovation. These investments cost money, but help protect the customer relationship on which future margins depend.

Some of this value remains unused. A company that has preserved customers' willingness to pay may have room to recover an unexpected cost increase without sharply reducing investment or accepting much lower profitability. That flexibility is difficult to identify from a single year's accounts. It becomes more visible when conditions worsen and competing businesses must choose between sacrificing margins and losing customers. Restraint today can therefore support resilience tomorrow. From an owner's perspective, unused pricing power is a form of strategic optionality: its value lies not only in current earnings but also in the choices available when conditions deteriorate.



THE PULSE

The hidden value of pricing power may lie in the price increase a company has not yet taken.

By leaving customers with a good reason to stay today, a business preserves room to respond when costs rise or conditions become more difficult.

The objective is not to maximise the price of the next transaction, but the long-term economic value of the customer relationship.

For investors, the question is: if costs rose tomorrow, would the company still have room to raise prices, or has it already asked as much of its customers as they are willing to pay?

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Sources checked to 24 November 2026.

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