

Pricing Strategies

Chapter 12

Objectives

- Learn the major strategies for pricing imitative and new products.
- Understand how companies find a set of prices that maximizes the profits from the total product mix.

Objectives

- Learn how companies adjust their prices to take into account different types of customers and situations.
- Know the key issues related to initiating and responding to price changes.

mLife: AT&T Wireless

- Price is #1 factor influencing choice of cellular companies
- Prices in wireless industry dropped 25% in three years
- Few companies were profitable
- mLife ad campaign attempted to build the AT&T wireless brand so consumers would consider value rather than just price
- Campaign met with strong initial success

Definitions

- Market-Skimming Pricing
 - Setting a high price for a new product to skim maximum revenues layer by layer from segments willing to pay the high price.
- Market-Penetration Pricing
 - Setting a low price for a new product in order to attract a large number of buyers and a large market share.

Product Mix Pricing Strategies

- Product Line Pricing
 - Setting price steps between product line items.
 - Price points
- Optional-Product Pricing
 - Pricing optional or accessory products sold with the main product

Product Mix Pricing Strategies

- **Captive-Product Pricing**
 - Pricing products that must be used with the main product
 - High margins are often set for supplies
 - Services: two-part pricing strategy
 - Fixed fee plus a variable usage rate

Product Mix Pricing Strategies

- **By-Product Pricing**
 - Pricing low-value by-products to get rid of them
- **Product Bundle Pricing**
 - Pricing bundles of products sold together

Price Adjustment Strategies

Strategies

- **Discount / allowance**
- *Segmented*
- *Psychological*
- *Promotional*
- *Geographical*
- *International*

- Types of discounts
 - Cash discount
 - Quantity discount
 - Functional (trade) discount
 - Seasonal discount
- Allowances
 - Trade-in allowances
 - Promotional allowances

Price Adjustment Strategies

Strategies

- *Discount / allowance*
- **Segmented**
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- Types of segmented pricing strategies:
 - Customer-segment
 - Product-form pricing
 - Location pricing
 - Time pricing
- Also called revenue or yield management
- Certain conditions must exist for segmented pricing to be effective

Conditions Necessary for Segmented Pricing Effectiveness

- Market is segmentable
- Lower priced segments are not able to resell
- Competitors can not undersell segments charging higher prices

- Pricing must be legal
- Costs of segmentation can not exceed revenues earned
- Segmented pricing must reflect real differences in customers' perceived value

Price Adjustment Strategies

Strategies

- *Discount / allowance*
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- **Psychological**
- *Promotional*
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- The price is used to say something about the product.
 - Price-quality relationship
 - Reference prices
 - Differences as small as five cents can be important
 - Numeric digits may have symbolic and visual qualities that psychologically influence the buyer

Price Adjustment Strategies

Strategies

- *Discount / allowance*
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- **Promotional**
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- Temporarily pricing products below the list price or even below cost
- Loss leaders
 - Special-event pricing
 - Cash rebates
 - Low-interest financing, longer warranties, free maintenance
- Promotional pricing can have adverse effects

Promotional Pricing Problems

- Easily copied by competitors
- Creates deal-prone consumers
- May erode brand's value
- Not a legitimate substitute for effective strategic planning
- Frequent use leads to industry price wars which benefit few firms

Price Adjustment Strategies

Strategies

- *Discount / allowance*
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- **Geographical**
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- Types of geographic pricing strategies:
 - FOB-origin pricing
 - Uniform-delivered pricing
 - Zone pricing
 - Basing-point pricing
 - Freight-absorption pricing

Price Adjustment Strategies

Strategies

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- Prices charged in a specific country depend on many factors
 - Economic conditions
 - Competitive situation
 - Laws / regulations
 - Distribution system
 - Consumer perceptions
 - Cost considerations

Price Changes

- Initiating Price Cuts is Desirable When a Firm:
 - Has excess capacity
 - Faces falling market share due to price competition
 - Desires to be a market share leader

Price Changes

- Price Increases are Desirable:
 - If a firm can increase profit, faces cost inflation, or faces greater demand than can be supplied.
- Methods of Increasing Price
- Alternatives to Increasing Price
 - Reducing product size, using less expensive materials, unbundling the product.

Price Changes

- Buyer reactions to price changes must be considered.
- Competitors are more likely to react to price changes under certain conditions.
 - Number of firms is small
 - Product is uniform
 - Buyers are well informed

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Price Changes

- Respond To Price Changes Only If:
 - Market share / profits will be negatively affected if nothing is changed.
 - Effective action can be taken:
 - Reducing price
 - Raising perceived quality
 - Improving quality and increasing price
 - Launching low-price “fighting brand”

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Public Policy and Pricing

- Pricing *within* Channel Levels
 - Price-fixing
 - Competitors can not work with each other to set prices
 - Predatory pricing
 - Firms may not sell below cost with the intention of punishing a competitor or gaining higher long-run profits or running a competitor out of business.

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Public Policy and Pricing

- Pricing *across* Channel Levels
 - Price discrimination
 - Retail price maintenance
 - Deceptive pricing
 - Bogus reference / comparison pricing
 - Scanner fraud
 - Price confusion

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Keywords

- Market-skimming pricing
- Market penetration pricing
- Product line pricing
- Price points
- Captive product pricing
- 2-part pricing (fixed + variable)
- By-product pricing
- Cash discount
- Quantity discount
- Trade discount
- Seasonal discount
- Segmented pricing (customer, location, time)
- Revenue/yield management
- Price-quality relationship
- Psychological Price
- Promotional price
- Geographical
- Price cuts
- Price increases
- Price fixing
- Predatory pricing

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