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.

Case Study

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

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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

Price Adjustment Strategies

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
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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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- 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

Price Adjustment Strategies

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

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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

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"*

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.*

Public Policy and Pricing

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