

Pricing

Pricing - Basics

Price: (short definition) Amount of money charged for a product
(also called: rent, tuition, fare, interest, commission, salary etc.)

- Customers make inferences based on price
- Easier to change compared to other Ps

Considerations in Pricing



1. Cost-Based Pricing Issues

- Types of costs: fixed, variable
- Cost changes in the short term (scale, production level)
- Cost decreases in the long term (learning, experience)

Cost-Plus Pricing

Price = Cost + Mark-up

- Why is it popular?
 - Simple
 - Sellers are more certain about costs than value to the customer
 - Reduces price competition
 - Could be perceived as fair to both buyers and sellers
- Does it make sense?

Break-Even Analysis

BE Analysis for pricing: Evaluating various prices by looking at BE Volumes.

Ex: A manufacturer incurs a fixed cost of \$300,000. Charges \$20 per unit, unit variable cost is \$10. How many units should be sold to break even?

2. Value-Based Pricing

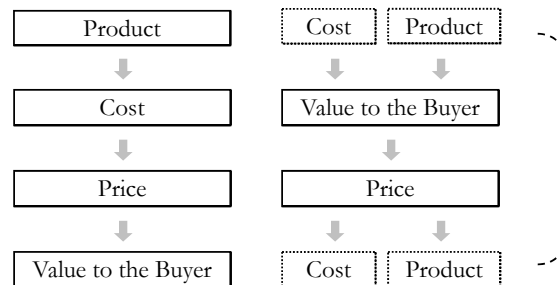
- Rationale: Customers generally don't know your margins or costs. Customer assessments of value are based on their gains and losses provided by competing alternatives.
- Determine price using perceived value to buyers. Hence, start by analyzing customer needs and value perceptions. How do you find out Value?

Example: Value Based Pricing



A Comparison

Cost-Based Pricing vs. Value-Based Pricing



3. Competitors' Offerings, Prices, Costs

- Consumers compare the Perceived Value of the alternatives
Market share depends on the “Perceived Value / Price” ratio
- What do we gain by learning competitors’ costs, margins?
 - How low can they cut prices?
 - Profits made, market entry / exit ?
- How can you estimate competitors’ costs?
 - Reverse engineering
 - Public data



Marketing Strategy, Objectives, Mix

- Price should be consistent with the marketing strategy and objectives
Price must be coordinated with other 3Ps
 - Keep in mind positioning & the target market
- Segmentation affects pricing because price varies over segments.
 - Price discrimination: Charging different prices to segments according to their price elasticity or sensitivity.

Organizational Considerations

- Who has the authority?
- Organizational design?

Market and Demand

- Nature of the Competition / Market
- Demand curve / price elasticity

pure competition
monopolistic competition
oligopolistic competition
pure monopoly

Other External Factors

- economic conditions
- distribution channel needs
- social concerns
- etc.

Pricing Strategies

Pricing Strategies for New Products

▪ Market Skimming

Setting a high price to obtain maximum revenues from segments.

(decrease price over time to reach layers / segments)

➤ Results in fewer sales, higher unit margins.

▪ Market Penetration

Setting a low price in order to attract a large number of buyers.

➤ Results in a larger market share.

Pricing for Multiple Products

- Pricing a Product Line
- Pricing Optional Products
- Pricing Captive Products
- Pricing Product Bundles



Prices Adjustments

- Discount (cash, quantity, etc.)
- Prices for Segments
- Pricing for Different Regions / Countries
- Price Promotions (short term)
- Price Changes: cuts, increases
(medium term, or for an unspecified period)
- Dynamic Pricing

Price Cut - Negative Buyer Reaction?

When Gibson lowered its prices, sales fell.

Any explanations?

For what other products can this be observed?



Buyer Reaction to Price Promotions

- Promotions :
 - consumers may switch to the promoted brand
 - consumers may buy more than usual of the promoted brand (stockpiling)
 - may reduce the value of the brand in the eyes of the buyers
 - may create “deal prone” customers (bargain hunters, or promotion oriented customers) who wait for promotions
 - customers may expect lower prices in general

Dynamic Pricing

- Monitoring demand / price continuously
 - e.g. pricing of airline tickets
 - can create customer dissatisfaction, protests

Psychological Aspects of Price

- Price-Quality inference
- Just-below pricing (\$19.90 etc)
- Reference prices
(consumers evaluate a prices relative to a benchmark for comparison)

