Pricing Products:

Pricing Strategies

Chapter 11

Learning Goals

1. Describe the major strategies for pricing imitative and new products
2. Understand how companies find a set of prices that maximize the profits from the total product mix
3. Learn how companies adjust their prices to take into account different types of customers and situations
4. Explore the key issues related to imitating and responding to price changes

Case Study
Kmart

- Once the top discount retailer in the U.S.
- Wal-Mart positioned on price and Target as "upscale discount"
- Kmart tried a value repositioning approach which turned to a price war with Wal-Mart

- Kmart failed to deliver on its value proposition
- Forced into bankruptcy and closing of nearly 1/3 of stores
- Kmart emerged from bankruptcy in May 2003
- How are they positioned now?

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**

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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 must be segmentable**
  - **Segments must show different demand**
  - **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

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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

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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

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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

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

Price Changes

- **Initiate price cuts when a firm:**
  - **Has excess capacity**
  - **Faces falling market share due to price competition**
  - **Desires to be a market share leader**
- **Initiate price increases when a firm:**
  - **can increase profit**
  - **faces cost inflation**
  - **faces greater demand than can be supplied**

Price Changes

- **Alternatives to Increasing Price**
  - **Explore more cost effective production or distribution**
  - **Reduce product size**
  - **Remove features**
  - **Unbundle 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

- **Responding to competitors' price changes**
  - **Evaluate the competitor's reason for the price change**
  - **Evaluate marketplace response to the price change**
  - **Considers own product's strategy**

Price Changes

- **Four options in responding to competitors' price changes**
  - **Reduce price**
  - **Raise perceived quality**
  - **Improve quality and increase price**
  - **Launch 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**