

# ***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

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- *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

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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

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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

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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*