11

Principles of Marketing

Pricing Products:
Pricing Strategies

Learning Objectives

After studying this chapter, you should be able to:

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

Chapter Outline

1. **New-Product Pricing Strategies**
2. **Product Mix Pricing Strategies**
3. **Price Adjustment Strategies**
4. **Price Changes**
5. **Public Policy and Pricing**

New-Product Pricing Strategies

Pricing Strategies

- Market skimming pricing
- Market penetration pricing

New-Product Pricing Strategies

Pricing Strategies

Market skimming pricing is a strategy with high initial prices to “skim” revenue layers from the market

- Product quality and image must support the price
- Buyers must want the product at the price
- Costs of producing the product in small volume should not cancel the advantage of higher prices
- Competitors should not be able to enter the market easily

New-Product Pricing Strategies

Pricing Strategies

Market penetration pricing sets a low initial price in order to penetrate the market quickly and deeply to attract a large number of buyers quickly to gain market share

- Price sensitive market
- Inverse relationship of production and distribution cost to sales growth
- Low prices must keep competition out of the market

Product Mix Pricing Strategies

Pricing Strategies

- Product line pricing
- Optional product pricing
- Captive product pricing
- By-product pricing
- Product bundle pricing

Product Mix Pricing Strategies

Pricing Strategies

Product line pricing takes into account the cost differences between products in the line, customer evaluation of their features, and competitors' prices

Optional product pricing takes into account optional or accessory products along with the main product

Product Mix Pricing Strategies

Pricing Strategies

Captive product pricing involves products that must be used along with the main product

- **Two-part pricing** is where the price is broken into:
  - Fixed fee
  - Variable usage fee

Price Adjustment Strategies

Pricing Strategies

By-product pricing refers to products with little or no value produced as a result of the main product. Producers will seek little or no profit other than the cost to cover storage and delivery.

Price Adjustment Strategies

Pricing Strategies

Product bundle pricing combines several products at a reduced price

Price Adjustment Strategies

Pricing Strategies

- Discount and allowance pricing
- Segmented pricing
- Psychological pricing
- Promotional pricing
- Geographical pricing
- Dynamic pricing
- International pricing

Price Adjustment Strategies

Pricing Strategies

Discount and allowance pricing reduces prices to reward customer responses such as paying early or promoting the product

- Discounts
- Allowances

Price Adjustment Strategies

Pricing Strategies

- Discounts
  - Cash discount for paying promptly
  - Quantity discount for buying in large volume
  - Functional (trade) discount for selling, storing, distribution, and record keeping

Price Adjustment Strategies

Pricing Strategies

- Allowances
  - Trade in allowance for turning in an old item when buying a new one
  - Promotional allowance to reward dealers for participating in advertising or sales support programs

Price Adjustment Strategies

Pricing Strategies

Segmented pricing is used when a company sells a product at two or more prices even though the difference is not based on cost

- Customer segment pricing
- Product form segment pricing
- Location pricing

Price Adjustment Strategies

Pricing Strategies

To be effective:

- Market must be segmentable
- Segments must show different degrees of demand
- Watching the market cannot exceed the extra revenue obtained from the price difference
- Must be legal

Price Adjustment Strategies

Pricing Strategies

Customer segment pricing is when different customers pay different prices for the same product or service

Product form segment pricing is when different versions of the product are priced differently but not according to differences in cost

Location pricing is when the product is sold in different geographic areas and priced differently in those areas, even thought the cost is the same

Price Adjustment Strategies

Pricing Strategies

Robert Cross

Revenue management charges the right customer the right price at the right time

Yield management balances price and demand

Price Adjustment Strategies

Pricing Strategies

Psychological pricing occurs when sellers consider the psychology of prices and not simply the economics

- Reference prices are prices that buyers carry in their minds and refer to when looking at a given product
  - Noting current prices
  - Remembering past prices
  - Assessing the buying situations

Price Adjustment Strategies

Pricing Strategies

Promotional pricing is when prices are temporarily priced below list price or cost to increase demand

- Loss leaders
- Special event pricing
- Cash rebates
- Low interest financing
- Longer warrantees
- Free maintenance

Price Adjustment Strategies

Pricing Strategies

Loss leaders are products sold below cost to attract customers in the hope they will buy other items at normal markups

Special event pricing is used to attract customers during certain seasons or periods

Cash rebates are given to consumers who buy products within a specified time

Low interest financing, longer warrantees, and **free maintenance** lower the consumer's "total price"

Price Adjustment Strategies

Pricing Strategies

Risks of promotional pricing

- Used too frequently, and copies by competitors can create "deal-prone" customers who will wait for promotions and avoid buying at regular price
- Creates price wars

Price Adjustment Strategies

Pricing Strategies

Geographical pricing is used for customers in different parts of the country or the world

- FOB pricing
- Uniformed delivery pricing
- Zone pricing
- Basing point pricing
- Freight absorption pricing

Price Adjustment Strategies

Pricing Strategies

FOB (free on board) pricing means that the goods are delivered to the carrier and the title and responsibility passes to the customer

Uniformed delivery pricing means the company charges the same price plus freight to all customers, regardless of location

Price Adjustment Strategies

Pricing Strategies

Zone pricing means that the company sets up two or more zones where customers within a given zone pay a single total price

Basing point pricing means that a seller selects a given city as a "basing point" and charges all customers the freight cost associated from that city to the customer location regardless of the city from which the goods are actually shipped

Price Adjustment Strategies

Pricing Strategies

Freight absorption pricing means the seller absorbs all or part of the actual freight charge as an incentive to attract business in competitive markets

Price Adjustment Strategies

Pricing Strategies

- Dynamic pricing
- International pricing

Price Adjustment Strategies

Pricing Strategies

Dynamic pricing is when prices are adjusted continually to meet the characteristics and needs of the individual customer and situations

Price Adjustment Strategies

Pricing Strategies

International pricing is when prices are set in a specific country based on country-specific factors

- Economic conditions
- Competitive conditions
- Laws and regulations
- Infrastructure
- Company marketing objective

Price Changes

Initiating Pricing Changes

- Price cuts
- Price increases

Price Changes

Initiating Pricing Changes

Price cuts is a reduction in price

- Excess capacity
- Increase market share

Price increases is an increase in selling price

- Cost inflation
- Increased demand and lack of supply

Price Changes

Buyer Reactions to Pricing Changes

- Price cuts
  - New models will be available
  - Models are not selling well
  - Quality issues
- Price increases
  - Product is “hot”
  - Company greed

Price Changes

Responding to Price Changes

Questions

- Why did the competitor change the price?
- Is the price cut permanent or temporary?
- What is the effect on market share and profits?
- Will competitors respond?

Price Changes

Responding to Price Changes

Solutions

- Reduce price to match competition
- Maintain price but raise the perceived value through communications
- Improve quality and increase price
- Launch a lower-price “fighting brand”

Public Policy and Pricing

Pricing Within Channel Levels

Price fixing: Sellers must set prices without talking to competitors

Predatory pricing: Selling below cost with the intention of punishing a competitor or gaining higher long-term profits by putting competitors out of business

Public Policy and Pricing

Pricing Across Channel Levels

Robinson Patman Act prevents unfair price discrimination by ensuring that sellers offer the same price terms to customers at a given level of trade

- Price discrimination is allowed:
  - If the seller can prove that costs differ when selling to different retailers
  - If the seller manufactures different qualities of the same product for different retailers

Public Policy and Pricing

Pricing Across Channel Levels

Retail (resale) price maintenance is when a manufacturer requires a dealer to charge a specific retail price for its products

Deceptive pricing occurs when a seller states prices or price savings that mislead consumers or are not actually available to consumers

Public Policy and Pricing

Pricing Across Channel Levels

Deceptive pricing occurs when a seller states prices or price savings that mislead consumers or are not actually available to consumers

- Scanner fraud failure of the seller to enter current or sale prices into the computer system
- Price confusion results when firms employ pricing methods that make it difficult for consumers to understand what price they are really paying

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