

Designing Pricing Strategies and Programs

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Some important pricing definitions

- Utility: The attribute that makes it capable of want satisfaction
 - Value: The worth in terms of other products
 - Price: The monetary medium of exchange.
- Value Example:
Caterpillar
Tractor is \$100,000 vs.
Market \$90,000
\$90,000 if equal
7,000 extra durable
6,000 reliability
5,000 service
2,000 warranty
\$110,000 in benefits -
\$10,000 discount!

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Synonyms for Price

- Rent
- Tuition
- Fee
- Fare
- Rate
- Toll
- Premium
- Honorarium
- Special assessment
- Bribe
- Dues
- Salary
- Commission
- Wage
- Tax

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Common Pricing Mistakes

- Determine costs and take traditional industry margins
- Failure to revise price to capitalize on market changes
- Setting price independently of the rest of the marketing mix
- Failure to vary price by product item, market segment, distribution channels, and purchase occasion

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Consumer Psychology and Pricing

- Reference prices
- Price-quality inferences
- Price endings
- Price cues

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Possible Consumer Reference Prices

- “Fair price”
- Typical price
- Last price paid
- Upper-bound price
- Lower-bound price
- Competitor prices
- Expected future price
- Usual discounted price

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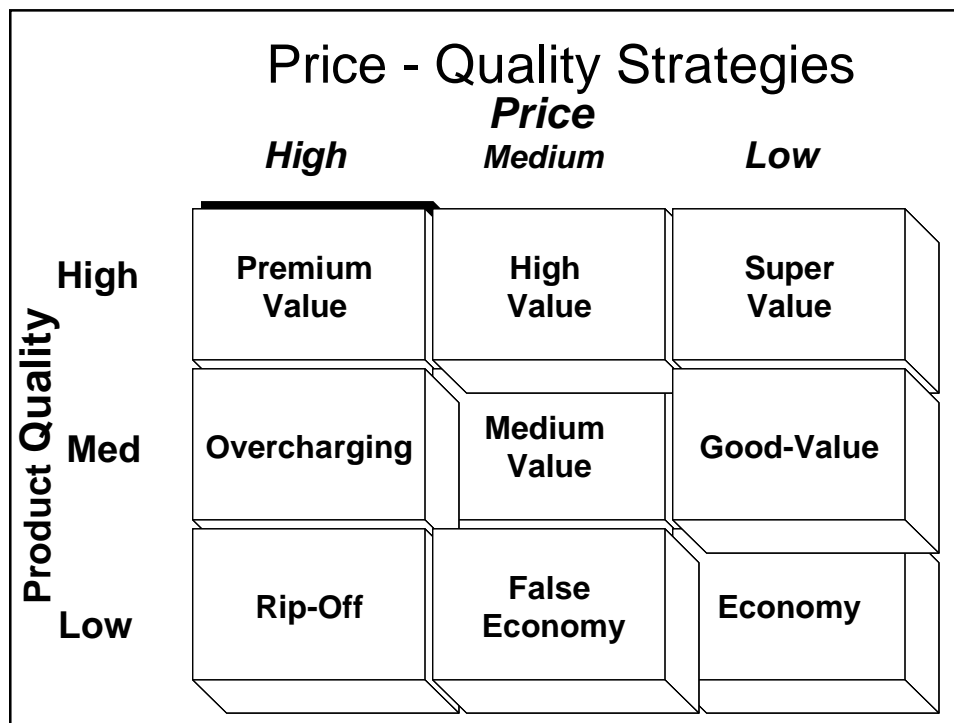
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Price Cues

- “Left to right” pricing (\$299 versus \$300)
- Odd number discount perceptions
- Even number value perceptions
- Ending prices with 0 or 5
- “Sale” written next to price

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Setting Pricing Policy

1. Selecting the pricing objective

2. Determining demand

3. Estimating costs

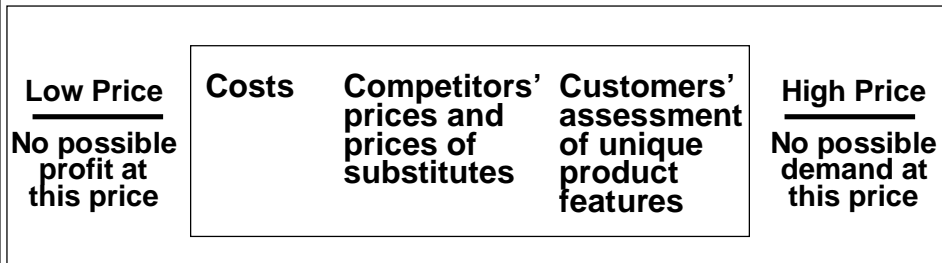
4. Analyzing competitors' costs, prices, and offers

5. Selecting a pricing method

6. Selecting final price

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The Three C's Model for Price Setting



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Step 1: Selecting the Pricing Objective

- Survival
- Maximum current profit
- Maximum market share
- Maximum market skimming
- Product-quality leadership

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Step 2: Determining Demand

- Price sensitivity
- Estimating demand curves
- Price elasticity of demand

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Step 3: Estimating Costs

- Types of Costs
- Accumulated Production
- Activity-Based Cost Accounting
- Target Costing

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Types of Costs

Fixed Costs (Overhead)

Costs that don't
vary with sales or
production levels.

Executive Salaries
Rent

Variable Costs

Costs that do vary
directly with the
level of production.

Raw materials

Total Costs

Sum of the Fixed and Variable Costs for a Given
Level of Production

Cost Terms and Production

- Fixed costs
- Variable costs
- Total costs
- Average cost
- Cost at different levels of production

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Step 5: Selecting a Pricing Method

- Markup pricing
- Target-return pricing
- Perceived-value pricing
- Value pricing
- Going-rate pricing
- Auction-type pricing

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- Markup Pricing = $\frac{\text{unit cost}}{(1 - \text{desired return on sales})}$
- Target Return Price
= unit cost + $\frac{\text{desired return} \times \text{invested capital}}{\text{unit sales}}$

Auction-Type Pricing

- English auctions – ascending bids
- Dutch auctions – descending bids
- Sealed-bid auctions

Step 6: Selecting the Final Price

- Impact of other marketing activities
- Company pricing policies
- Gain-and-risk sharing pricing
- Impact of price on other parties

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Price-Adaptation Strategies

- Geographical pricing
- Discounts/allowances
- Promotional pricing
- Differentiated pricing

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Price-Adaptation Strategies

Countertrade

- Barter
- Compensation deal
- Buyback arrangement
- Offset

Discounts/ Allowances

- Cash discount
- Quantity discount
- Functional discount
- Seasonal discount
- Allowance

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Promotional Pricing Tactics

- Loss-leader pricing
- Special-event pricing
- Cash rebates
- Low-interest financing
- Longer payment terms
- Warranties and service contracts
- Psychological discounting

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Differentiated Pricing and Price Discrimination

- Customer-segment pricing
- Product-form pricing
- Image pricing
- Channel pricing
- Location pricing
- Time pricing
- Yield pricing

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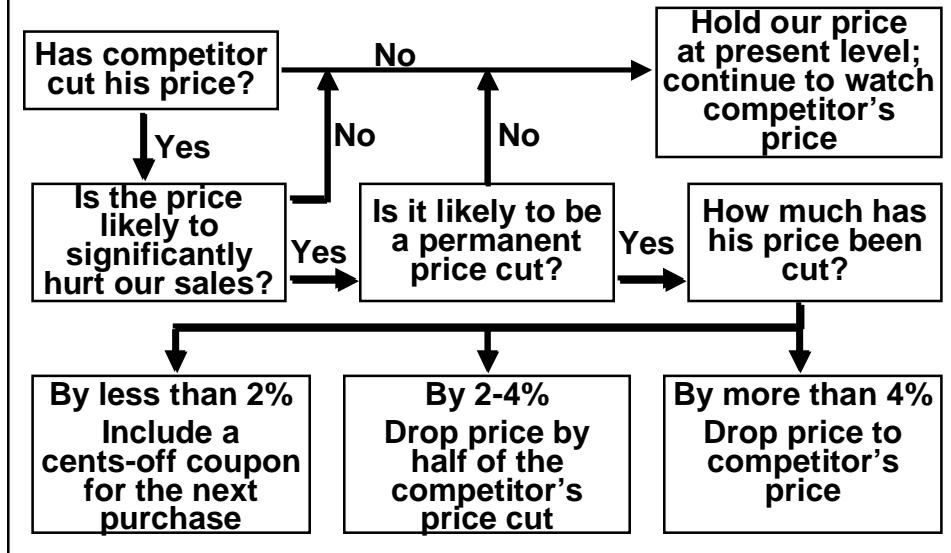
Increasing Prices

- Delayed quotation pricing
- Escalator clauses
- Unbundling
- Reduction of discounts

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Price-Reaction Program for Meeting a Competitor's Price Cut



Brand Leader Responses to Competitive Price Cuts

- Maintain price
- Maintain price and add value
- Reduce price
- Increase price and improve quality
- Launch a low-price fighter line

Review

- Setting the Price
- Adapting the Price
- Initiating & Responding to Price Changes