Pricing Projects and Decisions

Demand Driven Strategic Planning
Chapter: 10

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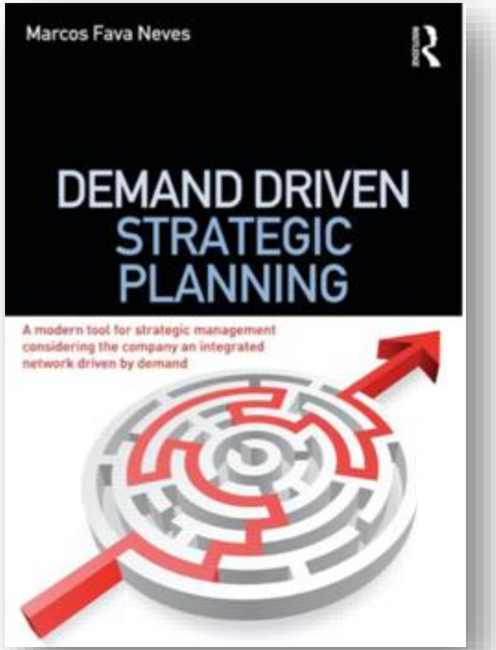

Exercise in Group to Deliver
4 or 5 members (40 minutes)

- Find a company that you think has a creative pricing process, and make comments of this process, based on the strategic pricing method on slide 20 with explanations at 21, 22, and 23.

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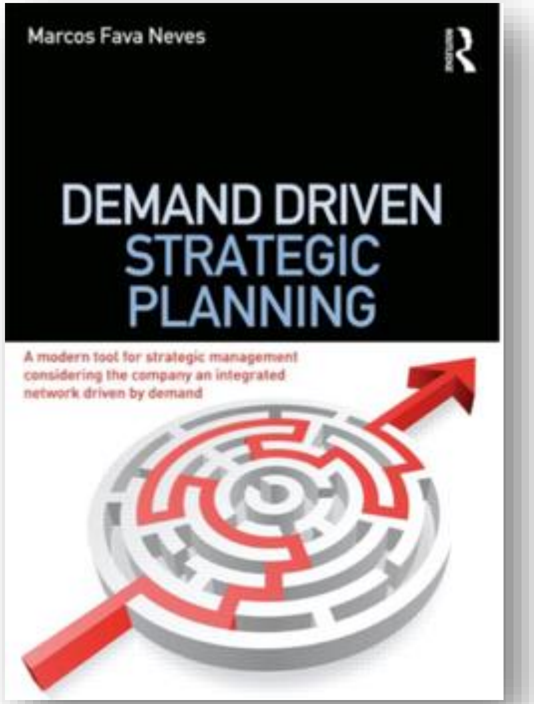
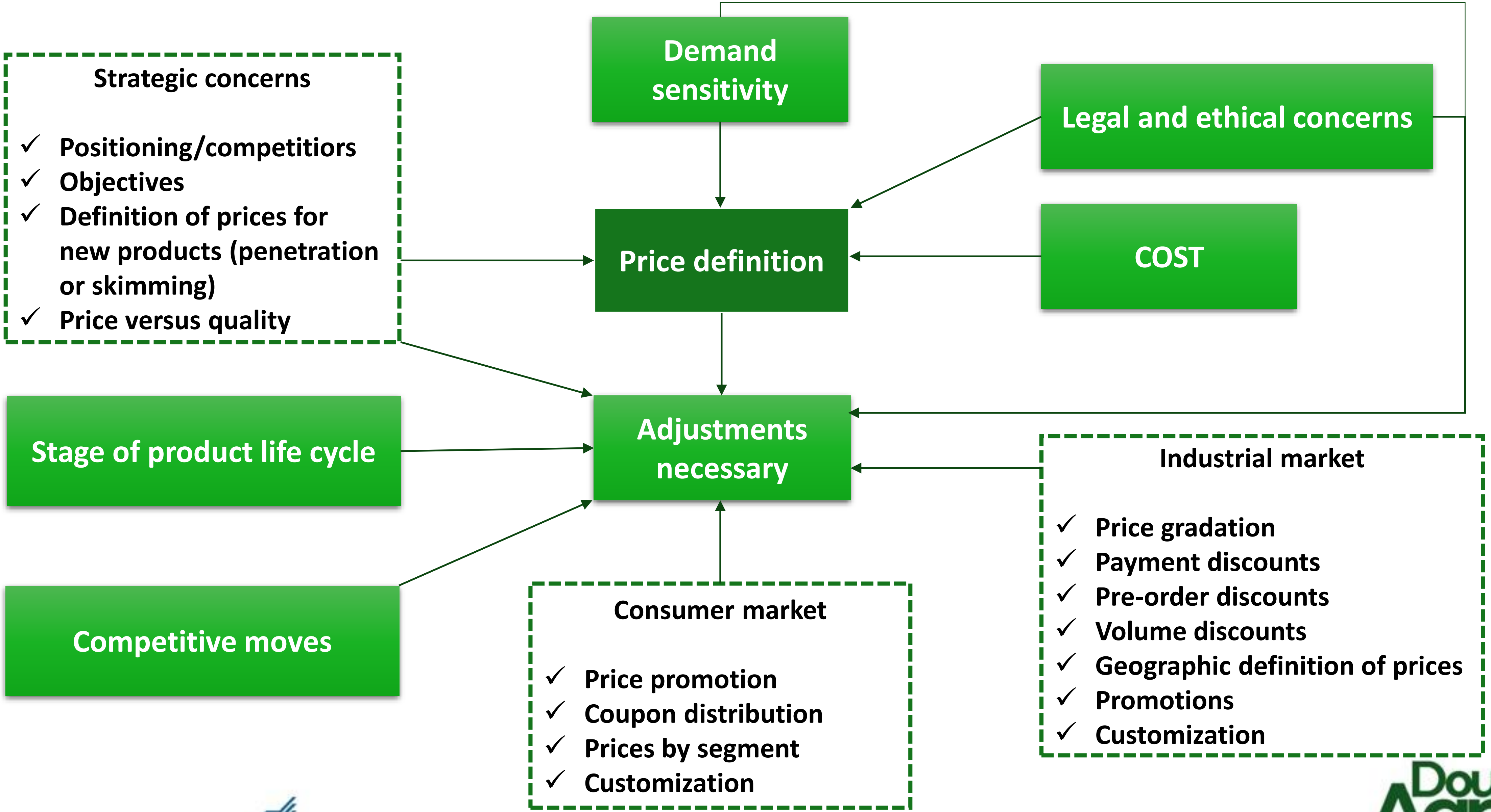
10.7 – Final Price Setting and Adjustments

10.8 - Ideas for Collective Actions in Pricing

10.9 – CPS – Creative Pricing Strategies



Factors Which Determine and Influence Price Definitions



Source: Czinkota (2010:443)

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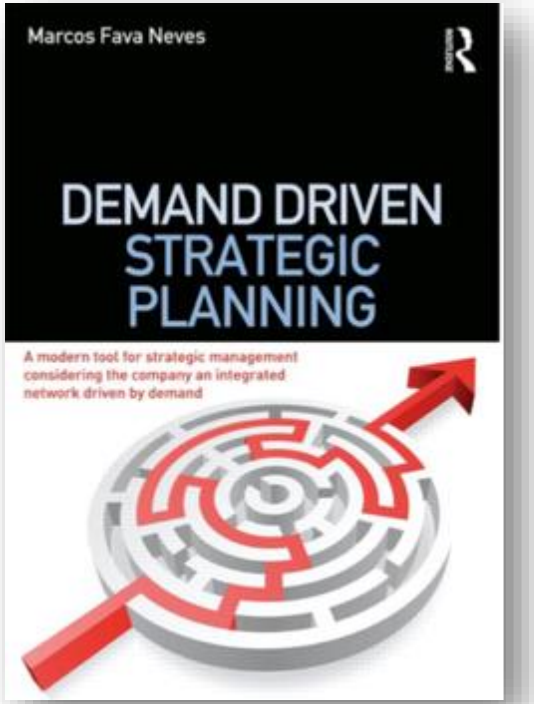

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Pricing Objectives

In general, there are five objectives in determining price (Kotler, 1997; Etzel *et al.*, 2001; Lambin, 2000; Czinkota, 2010): (1) *survival*, a short-term objective mainly practiced when there is surplus production, intense competition or a change in consumers' needs; (2) *profit maximization*, when the demand and costs are estimated for alternative prices, a level that maximizes profit is chosen, and a specific level of profit is established as objective; (3) *revenue maximization*, estimating only the demand and establishing the price that maximizes revenue or market share; (4) *maximization of sales growth* or maintenance and/or increase of market share, which due to the learning curve, can lead to smaller unit production costs; and (5) *maximization of market utilization*, used when there is a higher price; given the comparative benefits in relation to substitutes available, then the company reduces the price to conquer the segment immediately below, in other words, seeking price stability and

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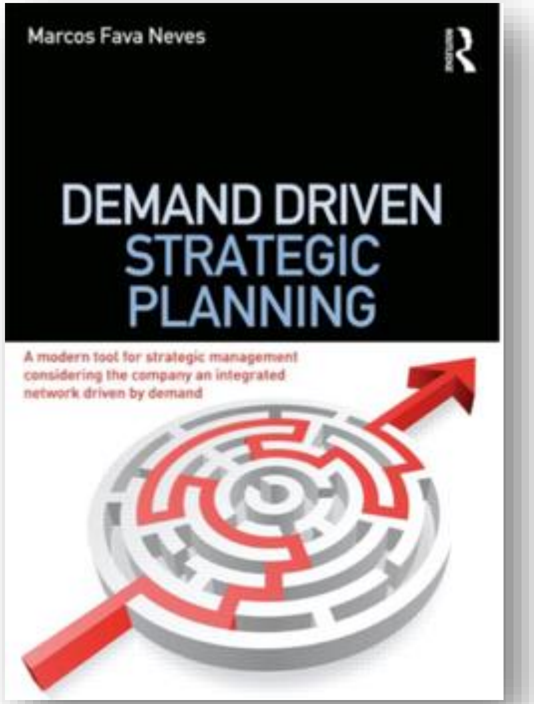

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Price Sensitivity Factors

Factors that reduce price sensitivity	How can your company use this factor?	Ideas for your Company
1. The product is exclusive: unique value.	How to create unique value for the customer?	
2. Buyers have less knowledge of the existence of substitutes.	How to make substitute product comparison difficult?	
3. Buyers cannot compare the substitute's quality.	How to create a unique and superior category?	
4. The price is small in relation to total income.	How to make the company's product part of a larger expense in which the consumer does not directly evaluate its cost?	
5. The product's final benefit is large.	How to increase the customer's perception that the benefit created by the product is of great value?	
6. The product's cost is shared with a third party.	How to involve different partners in the sales negotiation?	
7. The product is used in conjunction with previously bought assets.	To which product already bought by the customer can we associate ours?	
8. The product presents more quality, prestige or exclusivity: Price-Quality.	How to create a unique value?	
9. Buyers cannot stock the product.	How to avoid having our customers stocking our product and therefore having more power to negotiate future purchases?	

Source: Developed by the author based on Nagle's and Holden's items (1994).

Table 10.1 Price sensitivity factors.

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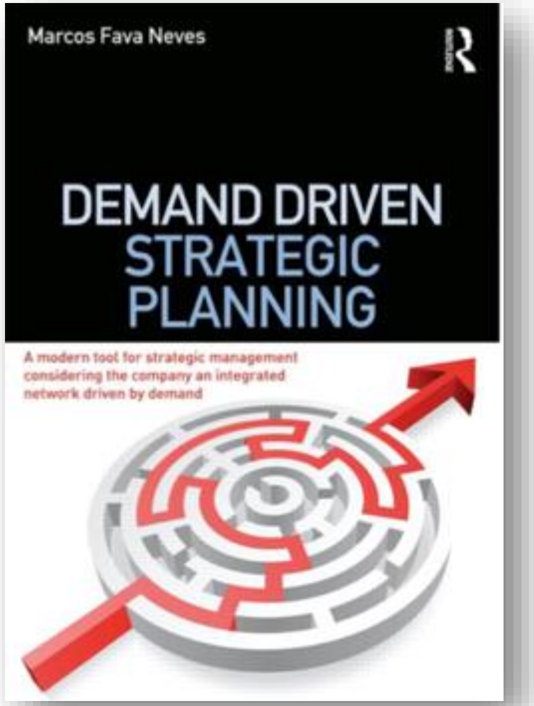

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Cost Analysis

Typical Cost Structures - Mature Companies	Traditional Biz Model
Total Revenue	**100**
Cost of Revenue - Total	**75**
Gross Profit	**25**
Gross Profit Margin %	***25,0%***
R&D (Research & Development)	5
% of revenue	*5,0%*
Sales & Marketing	9
% of revenue	*9,0%*
General & Administrative - Total	3
% of revenue	*3,0%*
Other Operating Expenses	1
% of revenue	*1,0%*
Operating Profit	**7**
Operating Profit Margin %	***7,0%***

Raw Materials	45.98%
Labor	21.00%
Advertising & Marketing	9.00%
R&D	8.50%
Interest Expenses	3.44%
Transportation	2.90%
Health & Safety	1.60%
Energy	1.53%
Environmental	1.48%
Land & Rent	1.46%
Utilities	1.16%
Software	0.80%

		Bread	Apples	Eggs	Mince	Pasta
TESCO	Sep 07	£0.54	£1.59	£2.15	£1.40	£0.44
	Sep 08	£0.72	£1.49	£2.58	£2.20	£0.69
ASDA	Sep 07	£0.54	£1.18	£2.15	£1.40	£0.44
	Sep 08	£0.72	£1.41	£1.88	£2.20	£0.69
Sainsbury's	Sep 07	£0.54	£1.19	£2.15	£1.40	£0.45
	Sep 08	£0.75	£1.49	£1.93	£2.20	£0.79

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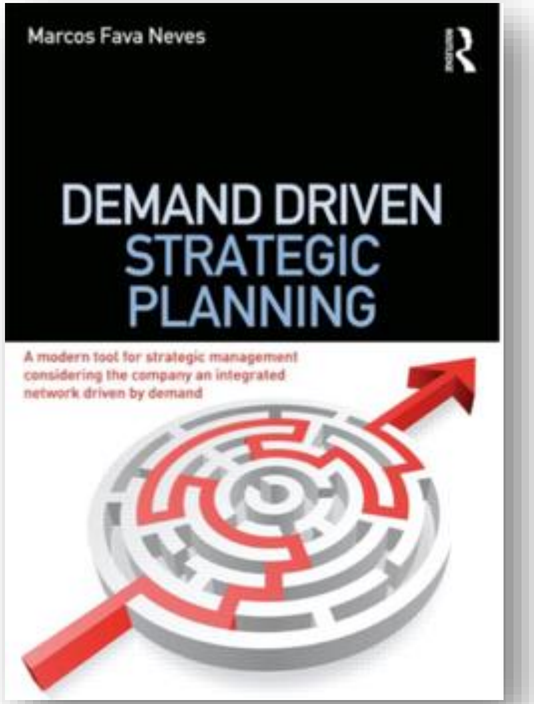

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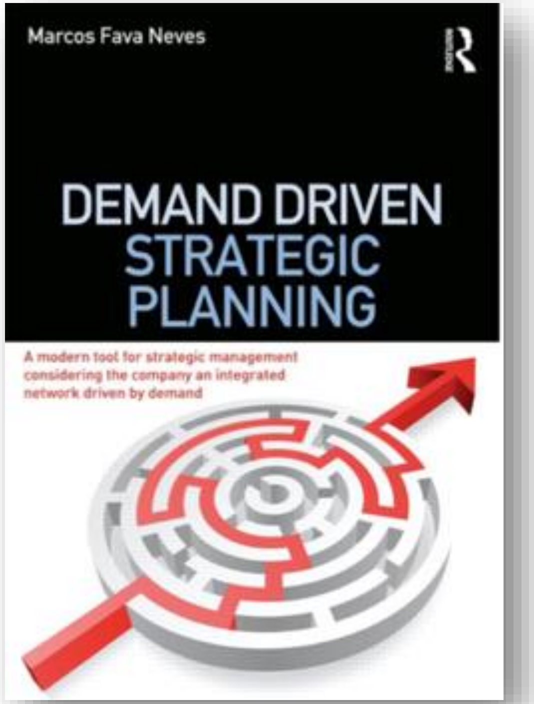

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Price Adjustment Strategies

Strategies	Considerations	Is this pricing strategy applicable to your company? If so, note necessary adjustments in the established policies
1- Geographical pricing	Considers transportation costs to the consumer, which grow in importance when the freight is a large component of the total variable cost. There are two geographical strategies: 1. By production point, when the product is picked up at the factory. 2. Flat delivery price, in which the quoted price is the same for all buyers regardless of their location.	
2 - Discounts and concessions	Discounts for payments in cash, discounts for quantity, functional discounts (offered to the members of the distribution channel), seasonal discounts and concessions.	
3 - Promotional pricing	Bait pricing, occasion pricing, discount coupons, low interest finance, longer term payments, warranty and service contracts, psychological discount (use of an artificial high price which is reduced drastically).	

Table 10.5 Price adjustment strategies.

Price Adjustment Strategies

Strategies	Considerations	Is this pricing strategy applicable to your company? If so, note necessary adjustments in the established policies
4 - Discriminate pricing	Pricing by consumer segment, pricing by product version, image pricing, location pricing, period pricing. Segmentation must be possible, impossible to resell, must be legalized and attuned to the institutional environment.	
5 - Product mix pricing	The product is part of a mix and the company seeks a price that maximizes this mix in the following ways: ✓ Product line pricing: each successive version of the product has extra characteristics, allowing higher prices. ✓ Sub product pricing: sale of sub products allows reduction of the price of the main product. ✓ Package pricing: gathering of several products that are sold more cheaply than if sold separately.	

Source: Developed from Kotler (2000) and Etzel; Walker and Stanton (2001).

Table 10.5 Price adjustment strategies.

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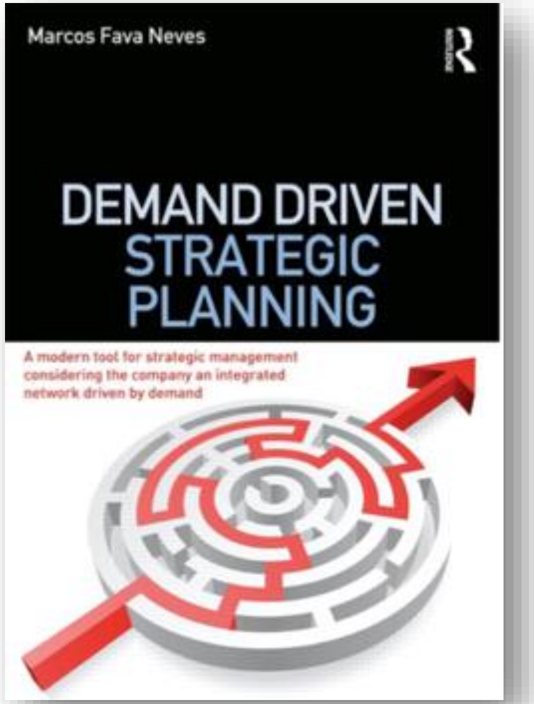

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Motives for Using the Network and Collective Action Perspective for Pricing

Actions	Description and Examples	Ideas for the Company
To increase the value perceived by the customers	– Offer a Package of Products and Services A package of products and services has more value as it makes the purchasing process easier for the consumer, bringing more convenience. It also transmits more trust, for the package can be constructed especially for their needs. The example of bundling in the agricultural inputs area (products and services package offer) uses this strategy.	
To reduce the price sensitivity in segments served	– Offer a Package of Products and Services Following from earlier points, there is a significant chance that the customer's price sensitivity is reduced, allowing the company to charge more for the package, in comparison with separate product. – Joint loyalty programs As strategies for joint discounts and network benefits, companies can share discounts (through loyalty cards, for example) where the benefit of using the network overcomes the competitor's offer. Airline companies have used this concept through associations with telephone companies, credit card companies, Internet providers, newspapers, among several others. – Difficulty in comparing substitutes The network offer makes the comparison with other offers harder, for networks are harder to compare than isolated products.	

Source: Developed by the author.
Table 10.6 Motives for using the network and collective action perspective for pricing.

Motives for Using the Network and Collective Action Perspective for Pricing

Actions	Description and Examples	Ideas for the Company
To reduce costs	– Joint actions in reduction of marketing expenses Promotional joint actions, in sales management, market research and so forth, have a great potential of saving expenses. – Outsourcing processes and activities Process outsourcing or the use of private brands, for the company that produces as well as for companies that "order the production", has a good potential to reduce costs either because they optimize the production or because they focus on their core competencies. These processes demand, and benefit, from the network coordination. – Joint purchasing offices Companies that buy jointly increase their bargain power with suppliers, besides benefiting from a common purchasing structure, they obtain scale advantages.	
To compare competition costs and prices	– Getting market information from other networks through members that cooperate with market information The companies from the network can use one another to get privileged cost structure and price information from competing companies. Actions with not exclusive distribution channels can facilitate obtaining information, as well as with non exclusive suppliers. Legal and ethical limits should be scrupulously observed in such cases.	

Source: Developed by the author.
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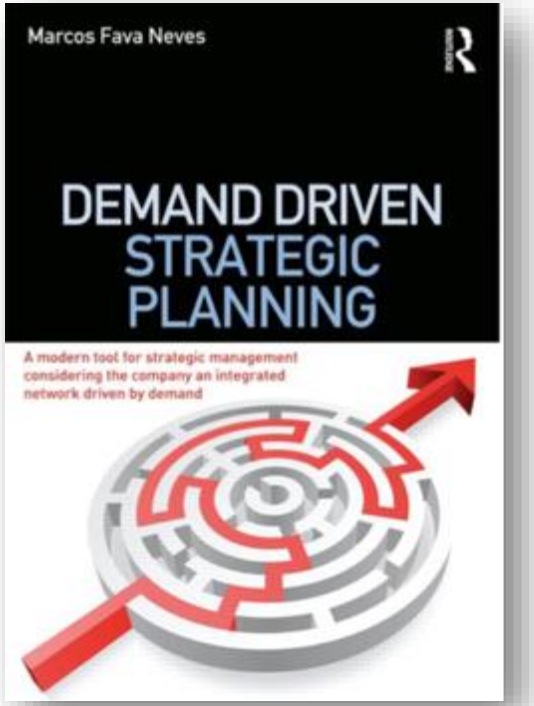

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*** “Hands - On” Method – How to Strategically Set Prices? ***

Phase 1. Understanding Value Given by Consumer

1. Analysis of the External Environment - PEST Analysis (Chapter 2 DDSP)
2. Analysis of Risks and Barriers to Purchase (Chapter 2 DDSP)
3. See the Competitors’ Offers (Visits, Markets, Web, Simulate purchase)

Phase 2. Strategies for Increasing the Value

4. Reduce the Importance of Substitutes (Table 10.1 and Networks)
5. Cost Analysis and Comparisons (Produce MP, MO)
6. Lock-In Strategies
7. Communicate the Importance of Attributes
8. Solving Problems and Mitigating Risks (Solutions for item 2)
9. Value Capture with Innovators (market skimming)
10. Synthesis of Benefits Offered by the Company

Phase 3. Strategic Pricing Movements

11. Untecipate and Monitor Competitors' Movements (avoid price wars)
12. Plan Possible Discounts and Promotions Policies (table 10.5 Slides 12/13)
13. Integrated Product/Service Approach and Adaptations
14. Permanent Use of the WEB – for "alerts, monitoring”
15. Possible Collective Actions in Pricing (slides 15/16)
16. Price Management, Changes, Meetings

Source: Prof. Marcos Fava Neves
Figure 10.2 The price setting process.

Some Details of the Method... How to Strategically Set Prices?

Phase 1 — Understanding the initial value given by the consumer.

1. Before any pricing decision is taken, a company must analyze the external environment: economic, income and demand conditions.
2. After this, a company should try to understand the behavior of the target consumer, his perception of the reasonable price (using surveys, experts, "food labs") and carry out a survey of initial pricing experiences in different marketing channels. The company should also analyze the total consumer costs when buying the product (money needed, time expended, knowledge acquisition, training costs, and psychological costs) that may be working as "buying barriers." All the consumer's risks in buying the company's product or service should be explored.
3. The third analysis in this phase is related to competitors, competing products/solutions and their prices, and how the consumer values and compares the product

Phase 2 — Strategies for increasing the value

4. Companies should research and try to create a unique value position for their products. This can be achieved by reducing the importance of substitutes and comparison possibilities (from the minds of the consumers), thus blinding the consumers to competitors.
5. Another opportunity is to compare the cost of the product as a proportion of the consumer's income or total expenditure, measuring and communicating.
6. Companies may use "lock in strategies," to market their products as being complementary to products already acquired by consumers.
7. Companies should communicate the importance of their products' attributes and the risks that may arise upon consumers if such attributes, for instance quality and safety, are neglected by competitors.
8. Companies may also consider offering a "solution-driven" package of products and services to conquer the buyers (sometimes called as "bundling").
9. Mitigating consumer's buying risks, as discussed in Phase 1, is also an idea worth pursuing.
10. Some markets offer possibilities of skimming price strategies for new solutions (image, status, and exclusivity). This benefits the companies to capture value from innovative consumers, first movers and status-oriented market segments.
11. Companies could also offer economic benefits to consumers (like lower production costs) in buying their products along with simple messages and credible commitments.

Phase 3 — Strategic pricing movements

This phase requires companies to:

12. Monitor and preview competitor's pricing movements.
13. Establish discount policies and promotions analyzing seasonality and other factors.
14 Invest in an integrated product line approach and pricing Interactions.
15. Implement pricing adaptations when the market faces any macro-environmental (economy) changes;
16. And finally, using web-based strategies, provide services and pricing options.

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- Marcos Fava Neves is an *international expert* on global agribusiness issues and a part-time professor of planning and strategy at the School of Business (FEARP) of the University of São Paulo (USP) and FGV Business School, both in Brazil. He graduated as an agronomic engineer from ESALQ/USP - Piracicaba in 1991. He earned his master’s degree in 1995 and his doctorate in management in 1999 from the FEA/USP School of Economics and Business – São Paulo. Marcos completed postgraduate studies in European agribusiness at ESSEC-IGIA in France in 1995 and in chains/networks at Wageningen University, in the Netherlands (1998-1999). In 2013 he spent the year as a visiting international professor at Purdue University (Indiana, USA) where he maintains the linkage as a permanent International Adjunct Professor. Since 2006 he is an international professor at the University of Buenos Aires, Argentina.

- He has *specialized in strategic-planning* processes for companies and food chains and works as a board member of both public and private organizations, being member of mor than 10 international boards since 2004. Also in 2004, he created the Markestrat think tank with other partners, today employing around 60 people and doing international projects, studies and research in strategic planning and management for more than 250 agri-food business organizations. Some of these projects were very important in suggesting public policies for food chains that were implemented in Brazil with economic and social impacts.

- Also as an experience in the private sector, from 1992 to 1993 he worked in citrus juice exporter and from 1994 to 1995 in a veterinarian company. In 2008, he became CEO of Brazil’s second-largest biofuel holding company, a position he occupied until 2009, when he returned to the University of São Paulo (USP) and Markestrat.

- At the academic side, since 1995 (when he was hired by USP), Marcos has advised more than 30 doctorate dissertations and master’s theses and helped to form around 1200 Bachelors in Business Administration in Brazil with around 120 courses taught to undergraduates at USP.

- His writings are strongly focused on supplying simple and effective methods for business. He has published more than 100 articles in international journals and has been author and editor of 63 books by 10 different publishers in Brazil, Uruguay, Argentina, South Africa, Singapore, Netherlands, China, the United Kingdom and the United States. He is also a regular contributor for China Daily Newspaper and has written two case studies for Harvard Business School (2009/2010), one for Purdue (2013) and five for Pensa/USP in the nineties. Recognized as the Brazilian academic with the largest number of international publications about orange juice and sugar cane chain and one of the top 3 most cited Brazilian authors in the area of food and agribusiness. He has reached more than 4000 citations in Google Scholar index.

- Marcos is one of the most active Brazilian speakers, having done more than 1050 lectures and presentations in 25 countries. He received around 150 recognitions from Brazilian and international organizations, and is considered a “Fellow” of the IFAMA (International Food and Agribusiness Management Association), title received in Minneapolis - 2015.

- Coming from a family of farmers, he is a worldwide defender of agriculture and farmer’s role in the development of the society. In the social side, together with his parents, Marcos is one of the creators and maintainers of Mucapp, a NGO that in 20 years has built more than 450 houses for families in Brazil that face very unfavorable conditions.

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