Students' version

International Marketing

11th of September, 2019

LIUC Università


Have a seat with your teammates

Contents of the session

0. Review of previous session
1. Fundamentals of pricing
2. International Pricing Policy
    a. Defining prices for foreign markets
    b. Factors affecting international pricing policy
3. Price escalation
4. Bundling and unbundling

Learning Objective

Understand *the fundamentals of pricing* and *implications of pricing for foreign markets*

Review of the previous session

0. Intro
Open questions to warm-up

What is price?

What is value?

1. Fundamentals of pricing

Price is what you pay. Value is what you get

- Warren Buffett, American investor

1. Fundamentals of Pricing: P&L

P&L (profit and loss) statement is a financial report that summarizes the company's results in a period of time (normally a year)

P&L includes incomes/revenues/total sales, the cost of goods sold (COGS), gross margin, general expenses, net results or net incomes (EBITDA) to yield profit (or loss)

**aka= also known as*

Profit and loss of company XYX

Total revenue	£100,000	Aka Top-line
Cost of goods sold	£20,000	
Gross profit	£80,000	

Operating expenses

Salaries	£10,000
Rent	£10,000
Utilities	£5,000
Depreciation	£5,000
Total operating expenses	£30,000
Operating profit	£50,000
Interest expense	£10,000
Income before taxes	£40,000
Taxes	£10,000

Net income	**£30,000**	Aka bottom-line

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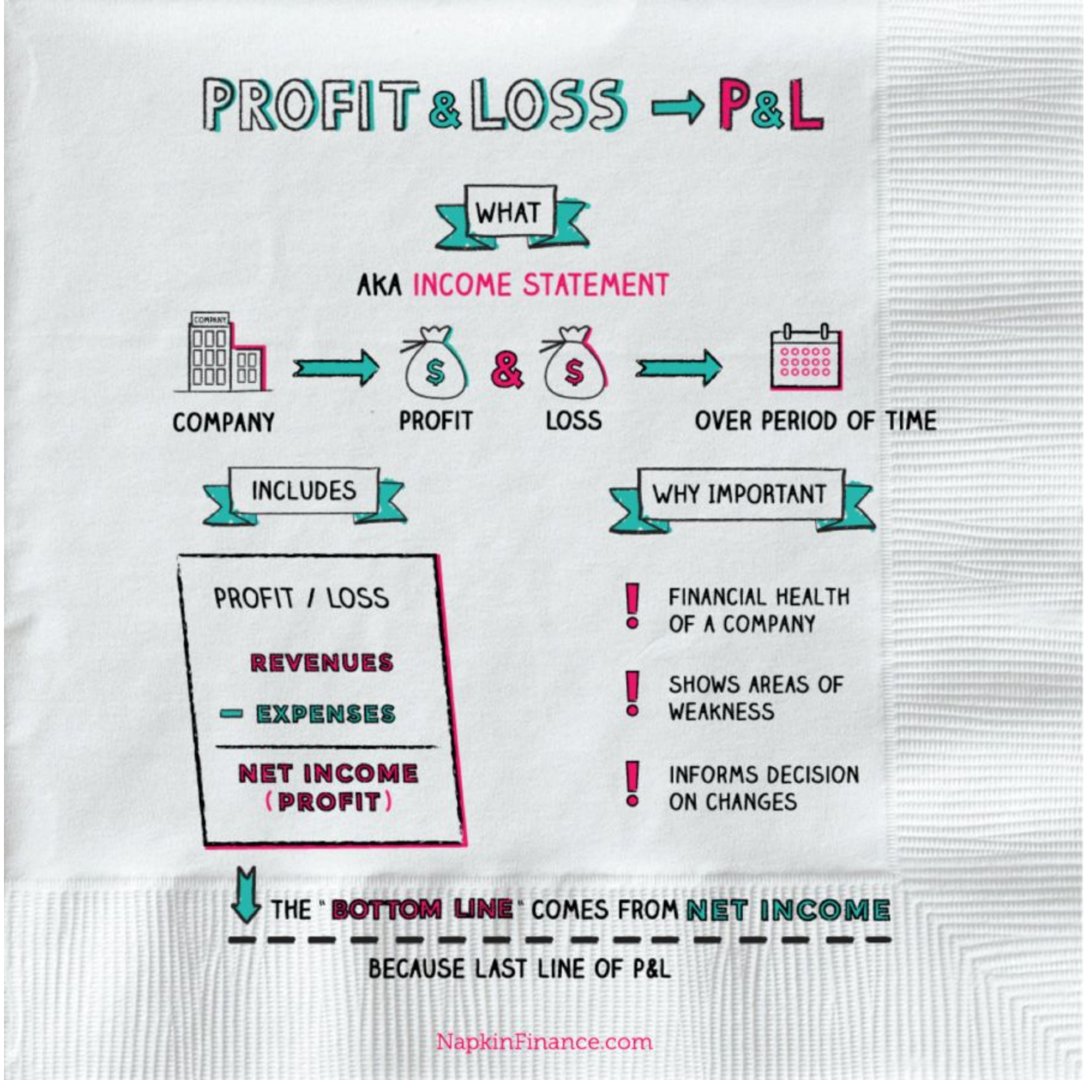

PROFIT & LOSS → P&L
WHAT
AKA INCOME STATEMENT
COMPANY
COMPANY
PROFIT
&
LOSS
OVER PERIOD OF TIME
INCLUDES
PROFIT / LOSS
REVENUES
− EXPENSES
NET INCOME
(PROFIT)
WHY IMPORTANT
! FINANCIAL HEALTH OF A COMPANY
! SHOWS AREAS OF WEAKNESS
! INFORMS DECISION ON CHANGES
THE "BOTTOM LINE" COMES FROM NET INCOME
BECAUSE LAST LINE OF P&L
NapkinFinance.com

1. Fundamentals of Pricing: Profit and costs

Profit = incomes (earnings or sales) - total costs

Earnings: is the total amount of incomes generated by target customers, normally expressed as Unitary price x units sold (=sales)

Fixed cost= is an invariable amount of expense for a given infrastructure (factory, shops, sales team…)

Variable cost= is the direct cost created when the company produces an output (product, service), ie: cars, clothes, yogurts …

Total costs= fixed cost + (variable cost x unit sold)

1. Fundamentals of Pricing: BEP

Break even point (BEP): is the amount of units (cars, perfumes, cookies, computers, number of credit cards customers ...) that a company needs to sell in order to cover the total costs (Fixed costs + variable cost x units) are equal to sales (incomes=price x units).

At BEP there is no profit and no lose because <u>revenues (sales)= total costs</u>

1. Fundamentals of Pricing: 3 approaches to pricing

1. **Cost-based pricing:**

   considering the company's costs⟶ price=costs+markup

2. **Competitive pricing:**

   using rivalry prices for benchmarks

3. **Customer pricing:**

   based on customer willingness to pay for the company's offering

1. Fundamentals of Pricing: 3 approaches to pricing

Optimal price is the one that -combined with other marketing tactics- delivers superior market value

The "optimal price" is a function of the value so, when defining a price, managers must consider all elements in the value creation process:

- Company goals and cost structure
- Collaborators
- Competitors
- Context
- Customers
- Marketing-mix tactics (6 remaining P's)

1. Fundamentals of Pricing: Cost based to pricing

Cost based is driven mainly by company's strategic goals, cost structure, customer's price sensitivity and psychological response to offering's price

Sales volume is a function of price, yielding:

- Skim pricing: setting a high price to "skim the cream" off the top of the market, focusing on customers willingness to pay high price. Normally maximizes profit margins at expense of market share.
- Penetration pricing: sets low prices in an attempt to gain higher sales volume, appropriate when: (1) demand is relatively elastic, (2) target segment becomes increasingly competitive, (3) cost is a function of volume and (4) being market pioneer can lead to sustainable competitive advantage

1. Fundamentals of Pricing: Cost based pricing

Price sensitivity is the degree to which changing the price influences the sales volume:

- Demand is elastic when a small change in price lead to a large change in sales volume
- Demand is inelastic when a profits might be increased by raising the price since the decrease in sales volume resulting from the change in price is likely to be small

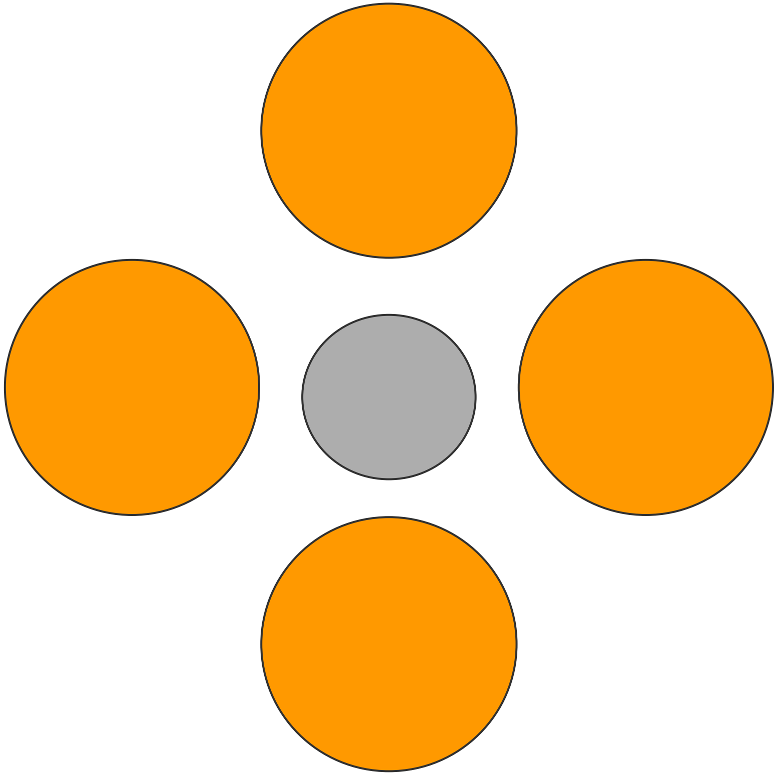
1. Fundamentals of Pricing: Cost based pricing

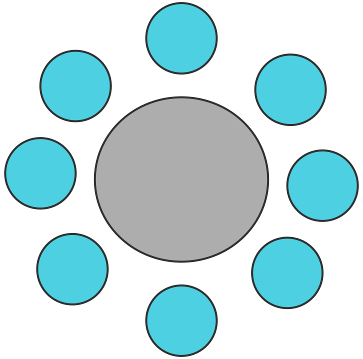
1. Fundamentals of Pricing: Cost based pricing

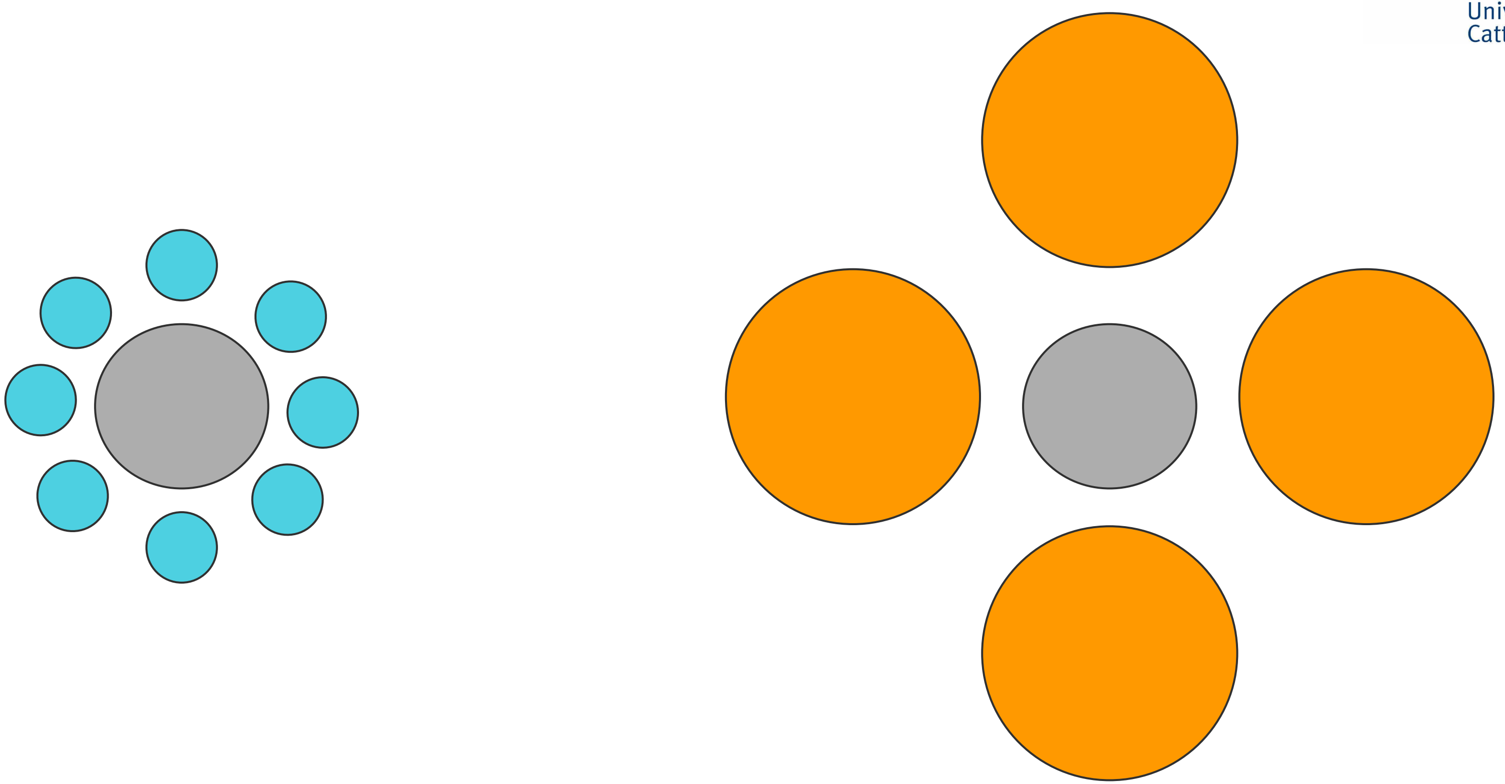
Psychological pricing effects come up because customers do not evaluate prices objectively, and normally depends on various factors:

A) Reference-price effect: we evaluate a price relatively to other prices, which serve as reference points, by comparing it to a more expensive offer

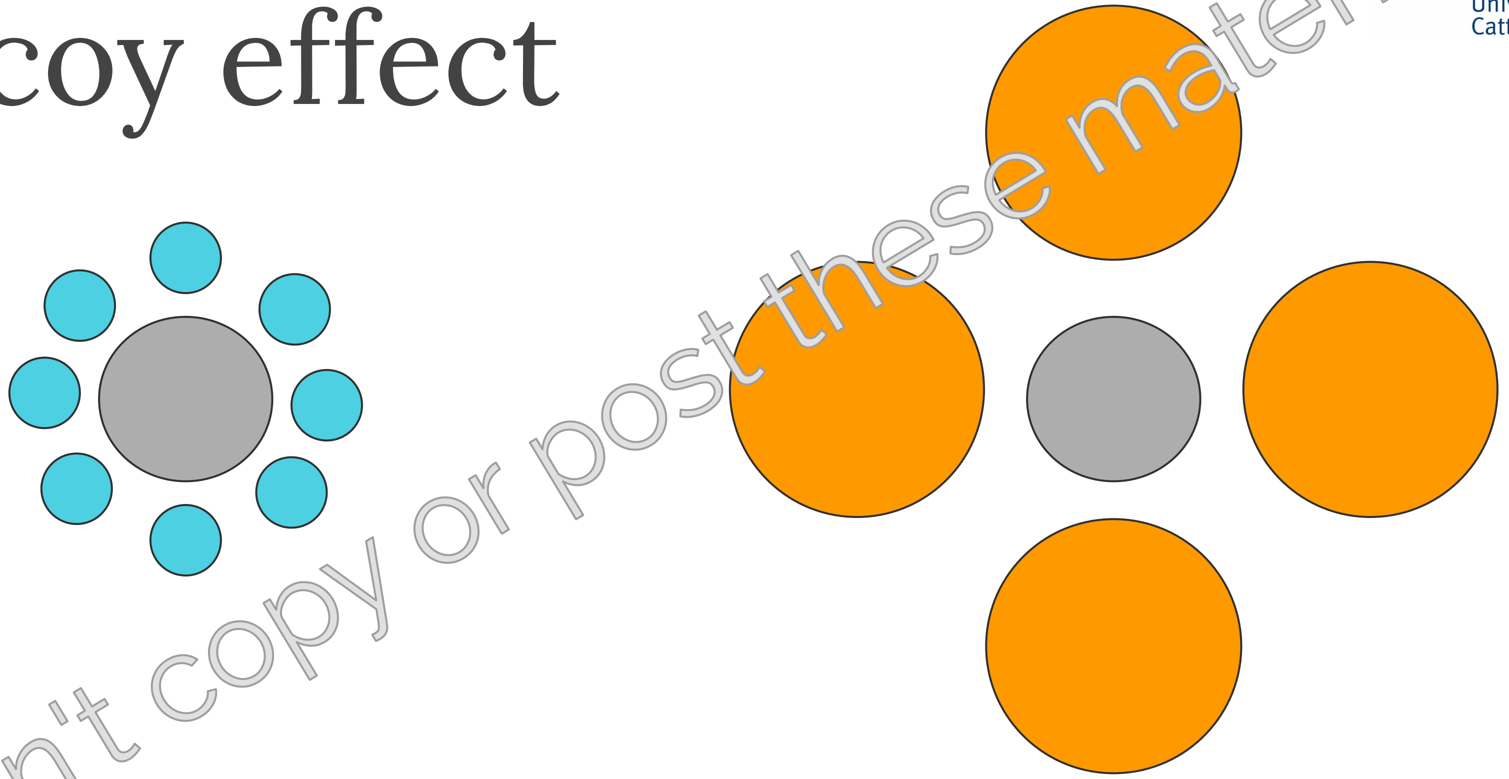
What grey dot is bigger?







Decoy effect



Ariely, Dan (2010). Predictably irrational : the hidden forces that shape our decisions. New York :Harper Perennial,

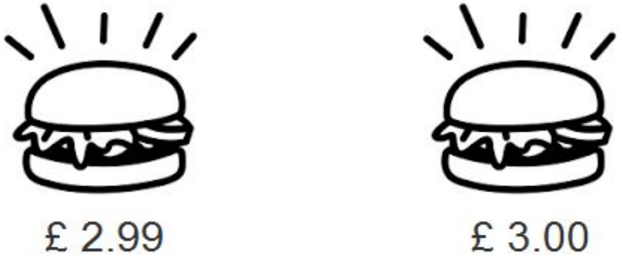
1. Fundamentals of Pricing: Cost based pricing

Psychological pricing comes up because customers do not evaluate prices objectively, and normally depends on various factors:

B) Price-tier effect: customers encode prices in tiers, so an item priced at 1,95€ is typically encoded in the "€1+" price tier, whereas an item priced at 2€ is classified in the "€2+" tier, leading to the paradoxical perception that the difference between items priced at 1,95€ and 2€ is one € instead 1 cent.

C) Price-ending effect (aka odd-ending) is the perception of prices is also a function of price endings. For example, prices ending in "9" often create the perception of a discount whereas prices ending in "0" might create the perception of quality

Tier price effect example



Odd-ending examples

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1. Fundamentals of Pricing: Cost based pricing

Psychological pricing comes up because customers do not evaluate prices objectively, and normally depends on various factors:

D) Product-line effect: because many offerings are available as a part of company product line, their relative prices can influence the demand for these offerings

How expensive is this wine?

780 €


1.220 €
CARRUADES de LAFITE
PAUILLAC

780 €
"UNICO"
Ribera del Duero

1.220 €

780 €

1.795 €

1. Fundamentals of Pricing: Competitive based pricing

This pricing approach involves setting the price of our product in a way that puts *parity* with offering competitors

The grand advantage of this approach is the simplicity in terms of management. The cons is the risk of eroding margins cause there is no control on pricing.

A second risk in competitive based pricing is Price Wars, starting when a competitor is willingness to sacrifice margins to gain sales volume. These Price Cuts are popular in times of crisis among managers because they are super easy to implement and typically produce fast results, resulting good in the short term but very bad in long-term.

1. Fundamentals of Pricing: Competitive based pricing

Likelihood of price wars is a function of:

1. Offering differentiation: price wars are more likely when products are commodities or undifferentiated offerings that can be easily substituted
2. Cost structure: significant economies of scale can be achieved by increasing volume
3. Market growth: stagnant markets
4. Customer loyalty: clients are price sensitive and switching costs are low

1. Fundamentals of Pricing: Competitive based pricing

Facing price wars:

1. Not taking actions
2. Adding a new offering, a downscale extension or "fighting brand"
3. Repositioning the existing offering → increasing benefits
4. Product strategy by customer segment

Price wars lead to Pyrrhic victories!

1. Fundamentals of Pricing: Customer based pricing

Customer pricing based on the client willingness to pay for the company's offering

How do we know willingness to pay?

- Market research
- Focus group
- Data mining

1. Fundamentals of Pricing: putting all together

Price range is a scale that help us to envision all available price options - putting all together

1. Fundamentals of Pricing: exercise

Marcallo SpA is an e-surveillance company that offers devices for industrial perimeters surveillance that are managed through a cloud-based platform. Maria, the Lombardia sales manager, has to set the price for a 4 units RFQ considering the following data:

- There are 171 devices in the italian HQ that had implied a cost of 1.500€/Unit in 2017 and they last 5 years
- On average, each device reduce customers costs from 6.600 €/perimeter/month to 2.200€
- The installation cost/device is 1.200€ including materials and customer training
- Monthly cost by cloud connected device to AWS (Amazon Web Services) is 50€/unit

With this information please estimate the price range to answer these questions:

1. What is the true economic value for the customer?
2. What should be the price for a monthly fee for each device in a 1 year contract? And for a 3 year contract?
3. What could be the minimum price each unit?
4. What is the firm incentive to sell?
5. What is the customer incentive to buy?

1. Fundamentals of Pricing: exercise 2

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Use the previous data of exercise 1 to calculate a BEP with total costs of 3,7 €M/year and ask a team to present the result

An example of dynamic pricing

The scheduled of syllabus topics:

- International pricing policy
- Bundling and unbundling prices
- Price escalation

Will be addressed together with product and brand alternative strategies

Remember:

We r selling

24/7!

Thanks for your attention

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