Marketing systems and Environments:

Pricing

The price

Price is the «hottest» variable of the marketing mix (5P) because it affects, in the most tangible way, the economic result.

Pricing decision is important for the following reasons:

- Business profitability
- Demand level and sales level
- Brand image and positioning with respect to the competitors
- Visibility

Features of price for industrial goods

Negotiation

- The price adopted often is not the list price because a negotiation process occurs.

Price accessory characteristics

- Costs not directly linked to the good itself but that influence the customer: shipping cost, cost for the training of the personnel, installation cost, duration of the warranty, etc.

Features of price for industrial goods

Ratio cost/price

- The buyer is often able to evaluate the production cost for the supplier, who is then required to explain its pricing process or its request for variations.

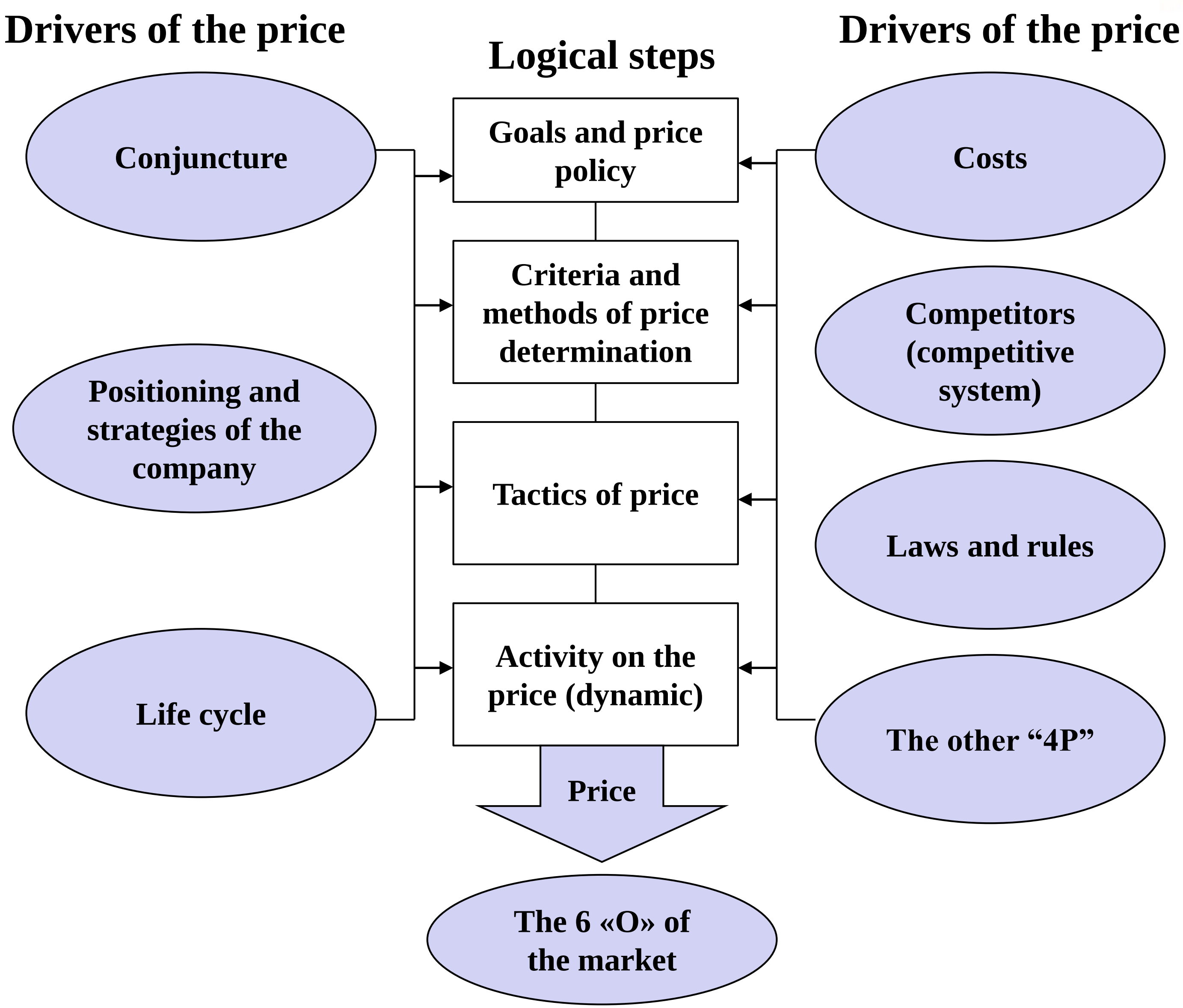
Exchange rates

- They may become an element of active survival or a dangerous trap.

Factors that affect the price determination

- Conjuncture and/or general state of the economy
- Positioning of the company and of the product with respect to the competitors
- Life cycle
- Cost structure
- Behavior of the competitive system
- Laws and rules (regulated prices)

Logical steps for the price determination



Goals and pricing policy

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The pricing policy is the set of decisions on the principles and criteria that, in a company, must drive the phase of prices determination of products and services; therefore, it represents the guidelines on which the future operative decisions must be based. It defines:

- The general level of the prices
- The variability of the prices
- The link to the prices (to the life cycle)

Goals and pricing policy

Orientation	Goal
To the volumes	• Volumes • Market share • Growth rate
To the profit	• Short term profit • Long term profit • Return on the investment • Rapid recovery of the investments in R&D • Premium price
To the external environment	• Brand image • To keep the loyalty towards the distribution channels • To accelerate the exit of marginal competitors • Barriers to potential competitors
To the survival	• Cash Flow • Usage of factories to each cost

Criteria and methods of price determination

In this phase, the criteria and methods of price determination are elaborated. The decision can be based on the three kinds of criteria, plus a fourth one that is their combination.

Criteria oriented…

To the costs

From costs to the selling price, adding a mark-up

To the market

Focus on the customer.
The starting point is the price that the customer is willing to pay for the product; on the basis of it, the effort is to get the maximum acceptable production cost

To the competitive system

Focus on the prices of the competitors as main element of reference

Criteria and methods of price determination (to the costs: ROI and Mark-Up)

«Cost Plus» logic: a margin is added to the unitary cost

<u>ROI Method</u>

Price = Variable Cost + (Fixed Costs / Quantity) + [(Profitability on the Invested Capital*Invested Capital) / Quantity]

<u>Mark-Up Method</u>

Price = [Variable Cost + (Fixed Costs / Quantity)] * [1 + (Mark-Up % / 100)]

Pros:

1) Apparent simplicity
2) Understandability

Criteria and methods of price determination (to the costs: Break-Even)

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The Break-Even point is intended as the minimum volume to be sold in order to reach a determined goal. Such goal can be:

- Real Break-Even: Total Revenues = Total Costs
- A certain level of Operative Profit*, namely Total Revenues = Total Costs + Operative Profit*

For calculating the Break-Even volume, it is necessary to introduce some simplifying hypotheses:

- Production Volume Xp = Volume of sale Xv = Operative Volume X (in other terms, there is not stock)
- It is possible to write the revenues as Total Revenues = $p \times X$
- It is possible to write the costs as Total Costs = $Cf + Cv \times X$
- The company is mono-product

Criteria and methods of price determination (to the costs: Break-Even)

Operative Profit* = Total Revenues – Total Costs = $p \times X - Cv \times X - Cf = (p - Cv) \times X - Cf = m \times X - Cf$

$$\Downarrow$$

1. Operative Profit* =0 $\Rightarrow$ $m \times X - Cf = 0$ $\Rightarrow$ $Xbe = Cf / m$

2. Operative Profit* = $m * X - Cf$ $\Rightarrow$ Xbe = (Operative Profit* + Cf) / m

Tactics of price

They are the operative practice that deal with the «management on the field» of the pricing.

List prices and net prices

- Actions on the discounts
- Advantage of «non-transparency» of the own tools to the competitors

Quantity discounts

- Economies of scale
- Applied on the order or at the end of the year

Commercial discounts

- Are the counterpart of the service made by the distribution channels or by the specialized agents

Tactics of price

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Financial discounts

- Linked to the different values of the money over the time. Discounts are applied in case of advanced payments

Seasonality discounts

- The price changes in relation to the greater or smaller availability linked to the seasonality

Prices guaranteed

- Referred to products and services that are frequently purchased, so that the customer has the certainty of the cost for a long time

Activity on the price (dynamic)

The price is not a static, but an adaptive «mechanism»; over the time, it is necessary to vary either the list price or the discounts-scale or the payment conditions in direction of increase or reduction.

- Modification of the production costs
- Will to acquire a wider basis of customers against the competitors
- Adjustments in comparison with the market leaders
- Adjustments towards the demand