

SUMMARIZING PRICING

CONTENTS

1. Pricing Aim	1
2. Pricing Menu	2
3. 10 Challenges to Pricing Intuition	3

1. PRICING AIM

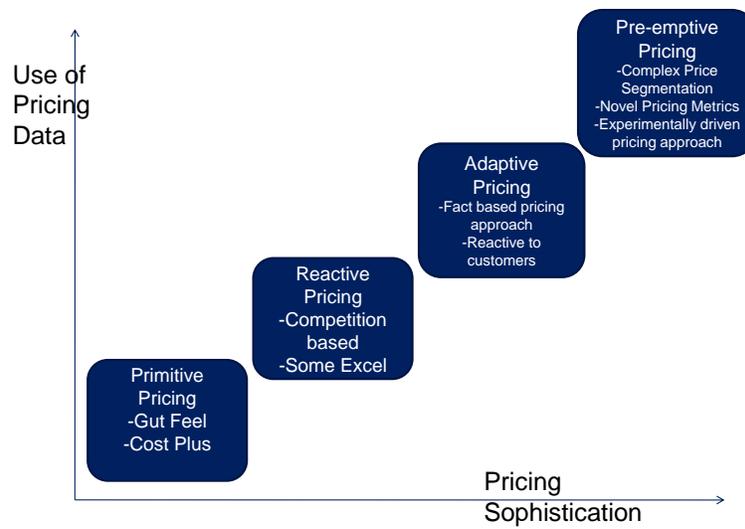


FIGURE 1. A taxonomy of pricing strategies

2. PRICING MENU

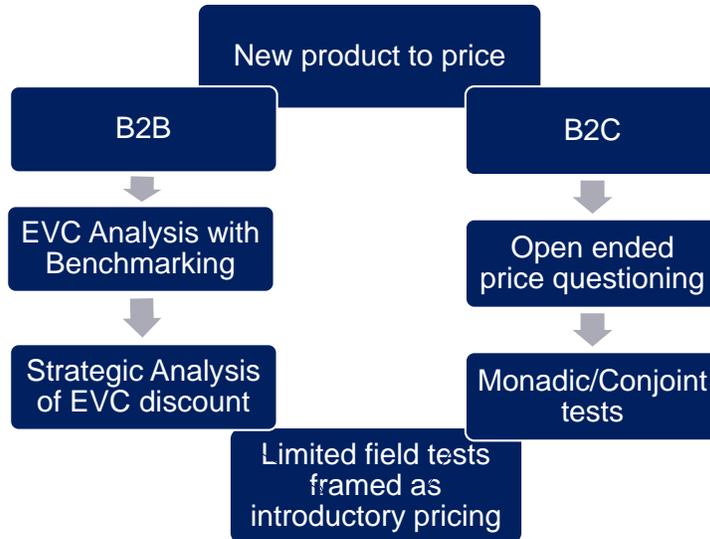


FIGURE 2. Pricing a new product

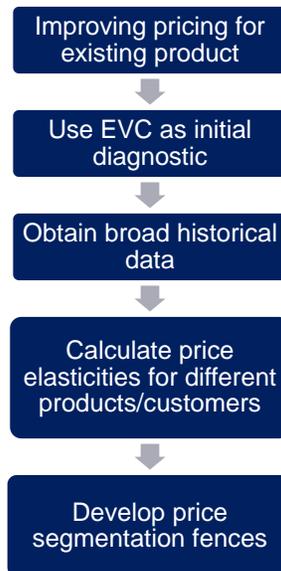


FIGURE 3. Pricing an existing product

3. 10 CHALLENGES TO PRICING INTUITION

- (1) If we use cost-plus pricing, we will make a profit
 - Only if you are incredibly accurate with your sales projections
- (2) Our customers always prefer low prices
 - Customers will always say they like lower prices. However, in many markets price serves as a guide to quality, and pricing too low can send out a negative signal.
- (3) Our customers do not know prices, so our pricing strategy is unimportant.
 - Lack of customer price knowledge makes how you present the price even more important. This is where strategies such as good-better-best and price ending cues are key.
- (4) Simpler pricing structures are better.
 - You always want three prices. Simplifying pricing structures means giving away money. Due to the taxi-meter effect, customers may not always appreciate it when firms do price simply.
- (5) If we are profitable, we do not need to price-discriminate.
 - On the contrary: Price segmentation is actually going to be most effective for already-profitable firms, because effective segmentation requires the market power implied by profitability.
- (6) Razor Blade pricing works because our customers are stupid
 - Razor blade pricing works because it is actually subtle price segmentation. High-value, high-usage customers pay more. Low-value, low-usage customers pay less.
- (7) Our product has network effects, so we need to set a low price
 - Your product may well not have network effects at all.
 - Even when a product has network effects, price segmentation is key. The crucial questions for network goods are: Whom do I set a low price to and whom do I set a high price to?
- (8) Firms need to adjust prices until I fill capacity.
 - It can be more profitable to have unused inventory or capacity.
- (9) Industries need to work together to ensure that they avoid harmful price wars
 - Statements like this lead to jail time. It is the responsibility of the firm, and the firm alone, to avoid a price war.
- (10) Our competitors understand our pricing strategy
 - Firms have to actively manage perceptions of their pricing by competitors, regulators and other stakeholders.

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