Pricing
Overview

Equate marginal costs and marginal revenue

Costs

Demand
  – Lack of data
  – Price perceptions
  – Vary prices across segments

How do managers work all of this out?
Costs

Many firms do not know their costs

Easier to determine than demand
  – Firms have cost data
  – Additive not multiplicative

Interested in variable costs
  – Not fixed costs
  – Not sunk costs
Demand: Lack of Data

Availability of data:

- No data available for some products
- Data only valid within relevant range
- Data may not capture all effects (e.g. store count)
Demand: Price Perceptions

Coke

Baking Soda
Price Cues

Prices they do know

“Sale” claims

$9 price endings

Price guarantees
Demand for Corduroy Duster

Regular: 100 units

Pre Season Sale: 157 units
$9 Endings

Same shirt

3 price conditions:
  – $34
  – $39
  – $44
Price Perceptions: Summary

Items with poor price knowledge
  – More sensitive to price cues than actual prices
  – Avoid overuse
  – Monitor quality perceptions

Items with good price knowledge
  – Not sensitive to price cues
  – Use to generate a favorable price image
Price Discrimination

UPS Prices: Rochester NY to Chicago

![Graph showing price discrimination]

- Price range from $0 to $60
- Weight of Package range from 0 to 160

The graph illustrates the price increase with the weight of the package, showing the price discrimination strategy.
Price Discrimination

Target marketing:
– different segments have different demands
– different segments have different competition (UPS)

Must be able to restrict resale:
– size of product prevents re-shipment (cars)
– FDA or regulatory controls (crimps on toothpaste)
– perceived difference (dental products)
Can Managers Work All of This Out?

Much to consider: costs
demand elasticities
cues (customer inferences)
competitive reactions

Begin simply: cost plus
match competitors
manufacturers' recommendation

Fine tune: need detailed response information
biased if feedback incomplete
What are the variables costs?

Is there sufficient demand data – if not begin by varying prices?

How well do customers know prices?

Do you have different customer segments – if so how can you discriminate?