Making Sure The Price is Right

By Robin C. Johnston

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Price, one of the Marketing Mix's "Four Ps", is an often-misunderstood weapon in the marketer's arsenal. Too often, small- and medium-sized enterprises rely on Price to carry the weight for its "little brothers" - Product, Place, and Promotion - in the firm's marketing battles. This is because of many firm's misconception that they have little choice but to make sure their prices are comparable to those of the competition.

Of course, a price that is way too high may simply make the product unaffordable. On the other hand, a low price provides little opportunity for new product development, expanded product placement, or creative promotional initiatives. As a result, once they start down the price spiral, firms often perceive the necessity to compete on price alone. This couldn't be further from the truth.

The truth is that Product, Place, and Promotion are marketing weapons at least as valuable as Price. The trick is to learn how to use them well.

Customer Delivered Value
Contrary to the conventional wisdom, customers buy a product because of its value proposition, not it's low price. The value proposition is the net benefit consumers realize when they complete an exchange: some amount of their money in return for some package of products and services that we provide when and where they want them.

Marketing guru Philip Kotler explains it this way:

"Total Customer Value is the bundle of benefits customers expect from a given product or service. Total Customer Cost is the bundle of costs customers expect to incur in evaluating, obtaining, and using the product or service. Customer Delivered Value is the difference between Total Customer Value and Total Customer Cost."

The key, therefore, is to maximize Customer Delivered Value. Clearly, this can be achieved by offering greater Total Customer Value as well as by making products available at a lower Total Customer Cost. There's simply no reason to get hung up on the cost side of the equation.

This is precisely why we see limitless variations of some of the products we buy. Each variation is an attempt to avoid price competition by offering something unavailable from other retailers or service providers. You can get a briefcase at Wal-Mart for less than $50, but if you want a genuine Samsonite™ hard-sided case with special hinges to prevent it from opening while it's upside-down, you're going to have to ante up and pay the price. Those features cost a little more.

Similarly, customers will pay more for a product that's available where they need it. Camera film retailers are aware that we will pay more for film at points of interest such as Niagara Falls, the Grand Canyon, or the Eiffel Tower. While we might complain as we pull out our wallets, we must admit that the value added by not having to drive 20 miles back into town or walk 10 blocks into a residential district is well worth the extra dollar or two we pay for the film.

Promotional efforts also enhance the value proposition. Through the Promotion Mix, firms can subtly or not so subtly introduce customers to the idea that the product is of higher quality, or provides greater value. Is a shirt made by Ralph Lauren really better than one made by someone else? Many people think so, but others have their doubts. Somehow much of the shirt-buying public has been convinced that there is additional value there, but only textile professionals and clothing connoisseurs know for sure. In any event, Ralph Lauren can, and does, charge more.

There are other pricing considerations. Should you vary your prices for different geographic markets, at different times of the day or week, or for different customer groups? Will you give a cash discount to promote prompt payment? What about a quantity discount for high-volume buyers? Will seasonal discounts help clear out hard-to-sell seasonal merchandise? These questions, and scores of others, must be carefully considered when adopting a pricing strategy.

When You've Made The Decision To Lower Your Prices

In general, there are three situations when you should consider a price decrease. These are when you have excess plant capacity, when you are experiencing declining market share, and when you wish to make a drive to dominate the market through a low-cost strategy.

The low-cost strategy carries risks, however.

First of these is the low-quality trap. We often associate price with quality. After a substantial price decrease, it is quite possible that consumers will assume that the quality of your products is below that of the higher-priced competitors and, consequently, choose not to buy your products.

A second risk is the fragile-market-share trap. This is common in highly competitive industries where aggressive competitors have gone through successive rounds of discounting in an effort to win share. The result is that the low prices buy market share, but not customer loyalty. Customers become conditioned to switch to the next low-price firm that comes along.

Finally, there is the danger of falling into the shallow-pockets trap. In response to your discounting strategy, higher-priced competitors may cut their prices and may have longer staying power because of deeper cash reserves. In essence, they'll just match your discount, and wait you out.

While the pricing decision is a big one, it is important not to forget the power of Product, Place and Promotion. Maximize Total Customer Value and you are equipping yourself to become your industry's market share leader.

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