Global Marketing

Warren J. Keegan   Mark C. Green

Pricing Decisions
Chapter 11

Learning Objectives

- Law of one price
- Price floors & ceilings
- Optimum prices
- Target costing
- Price escalation
- Environmental issues
- Gray market goods
- Dumping
- Price fixing
- Transfer pricing
- Countertrade

Basic Pricing Concepts

- ***Law of One Price***
  - All customers in the market get the best product for the best price
- Global markets
  - Diamonds
  - Crude oil
  - Commercial aircraft
  - Integrated circuits
- National markets
  - Costs
  - Competition
  - Regulation

Fragmented beer market: Budweiser, the leading global brand, has less that 4% of market share.

Heineken's price in Japan is a function of competition with other imports and the national producers.

Global Pricing Objectives and Strategies

- The Global Manager must develop systems and policies that address
  - Price Floor: minimum price
  - Price Ceiling: maximum price
  - Optimum Prices: function of demand
- Must be consistent with global opportunities and constraints
- Be aware of price transparency created by Euro zone, Internet

Global Pricing Objectives and Strategies

- Managers must determine the objectives for the pricing objectives
  - Unit Sales
  - Market Share
  - Return on investment
- They must then develop strategies to achieve those objectives
  - Penetration Pricing
  - Market Skimming

Market Skimming and Financial Objectives

- Market Skimming
  - Charging a premium price
  - May occur at the introduction stage of product life cycle
  - Luxury goods marketers use price to differentiate products
    - LVMH, Mercedes-Benz

Penetration Pricing and Non-Financial Objectives

- Penetration Pricing
  - Charging a low price in order to penetrate market quickly
  - Appropriate to saturate market prior to imitation by competitors

- Packaged food product makers, with products that do not merit patents, may use this strategy to get market saturation before competitors copy the product.

Companion Products or "Razors and Blades" Pricing

- Products whose sale is dependent upon the sale of primary product
  - Video games are dependent upon the sale of the game console
- "If you make money on the blades, you can give away the razors."
- Cellular service providers subsidize the phone and make money on calling plans

The Target-Costing Process

- Determine the segment(s) to be targeted, as well as the prices that customers in the segment will be willing to pay.
- Compute overall target costs with the aim of ensuring the company's future profitability.
- Allocate the target costs to the product's various functions. Calculate the gap between the target cost and the estimated actual production cost.
- Obey the cardinal rule: If the design team can't meet the targets, the product should not be launched.

Export Price Escalation

TABLE 11-2 An American-Built Jeep Grand Cherokee Goes to Japan (estimates)

Item	Amount of Price Escalation	Total
Ex-works price	0	$30,000
Exchange rate adj.	$2,100	$32,100
Shipping	$300	$32,400
Customs fees	$1,000	$33,400
Distributor margin	$3,700	$37,100
Inspection, accessories	$1,700	$38,800
Added options, prep	$3,000	$41,800
Final sticker price	$8,200	$50,000

Export Price Escalation

- **Export price escalation** is the increase in the final selling price of goods traded across borders.

Factors for Pricing on Goods that Cross Borders

1. Does the price reflect the product's quality?
2. Is the price competitive given local market conditions?
3. Should the firm pursue market penetration, market skimming, or some other pricing objective?
4. What type of discount (trade, cash, quantity) and allowance (advertising, trade-off) should the firm offer its international customers?
5. Should prices differ with market segment?
6. What pricing options are available if the firm's costs increase or decrease? Is demand in the international market elastic or inelastic?
7. Are the firm's prices likely to be viewed by the host-country government as reasonable or exploitative?
8. Do the foreign country's dumping laws pose a problem?

Cost-Plus Pricing

- *Cost-based pricing* is based on an analysis of internal and external cost
- Firms using western cost accounting principles use the *Full absorption cost method*
  - Per-unit product costs are the sum of all past or current direct and indirect manufacturing and overhead costs

Cost-Plus Pricing

- *Rigid cost-plus pricing* means that companies set prices without regard to the eight pricing considerations

- *Flexible cost-plus pricing* ensures that prices are competitive in the contest of the particular market environment

Cross International Borders- Terms of Sale

- Obtain export license if required
- Obtain currency permit
- Pack goods for export
- Transport goods to place of departure
- Prepare a land bill of lading
- Complete necessary customs export papers
- Prepare customs or consular invoices
- Arrange for ocean freight and preparation
- Obtain marine insurance and certificate of the policy

Terms of the Sale

- **Incoterms**
  - Ex-works – seller places goods at the disposal of the buyer at the time specified in the contract; buyer takes delivery at the premises of the seller and bears all risks and expenses from that point on.

- Delivery duty paid – seller agrees to deliver the goods to the buyer at the place he or she names in the country of import with all costs, including duties, paid

Incoterms

- FAS (free alongside ship) named port of destination – seller places goods alongside the vessel or other mode of transport and pays all charges up to that point
- FOB (free on board) – seller's responsibility does not end until goods have actually been placed aboard ship
- CIF (cost, insurance, freight) named port of destination – risk of loss or damage of goods is transferred to buyer once goods have passed the ship's rail
- CFR (cost and freight) – seller is not responsible at any point outside of factory

Currency Fluctuations

January 2000	January 2002	January 2007	January 2010
\$1=¥101	\$1=¥130	\$1=¥113	\$1=¥91

Inflationary Environment

- Defined as a persistent upward change in price levels
  - Can be caused by an increase in the money supply
  - Can be caused by currency devaluation
- Essential requirement for pricing is the maintenance of operating margins

Government Controls, Subsidies, and Regulations

- The types of policies and regulations that affect pricing decisions are:
  - Dumping legislation
  - Resale price maintenance legislation
  - Price ceilings
  - General reviews of price levels
- Foreign governments may:
  - require funds to be noninterest-bearing accounts for a long time
  - restrict profits taken out of the country and limit funds paid for imported material
  - Restrict price competition

Competitive Behavior

- If competitors do not adjust their prices in response to rising costs it is difficult to adjust your pricing to maintain operating margins
- If competitors are manufacturing or sourcing in a lower-cost country, it may be necessary to cut prices to stay competitive

Using Sourcing as a Strategic Pricing Tool

- Marketers of domestically manufactured finished products may move to offshore sourcing of certain components to keep costs down and prices competitive
- China is “the world’s workshop”
- Rationalize the distribution system—Toys ‘R’ Us bypasses layers of intermediaries in Japan to operate U.S. style warehouse stores

Global Pricing: Three Policy Alternatives

- Extension or Ethnocentric
- Adaptation or Polycentric
- Geocentric

Mercedes moved beyond ethnocentric pricing when Toyota began offering Lexus—Mercedes value at $20k less. In 1993, Mercedes boosted employee productivity, increased low-cost suppliers and invested in production facilities in the U.S. to move to better pricing.

Extension Pricing

- Ethnocentric
- Per-unit price of an item is the same no matter where in the world the buyer is located
- Importer must absorb freight and import duties
- Fails to respond to each national market

Extension Pricing

"In the past, Mercedes vehicles would be priced for the European market, and that price was translated into U.S. dollars. Surprise, surprise: You're 20 percent more expensive than the Lexus LS 400, and you don't sell too many cars."

-Joe Eberhardt, Chrysler Group Executive Vice President for Global Sales, Marketing, and Service

Adaptation or Polycentric Pricing

- Permits affiliate managers or independent distributors to establish price as they feel is most desirable in their circumstances

- Sensitive to market conditions but creates potential for gray marketing

Geocentric Pricing

- Intermediate course of action
- Recognizes that several factors are relevant to pricing decision
  - Local costs
  - Income levels
  - Competition
  - Local marketing strategy

Gray Market Goods

- Trademarked products are exported from one country to another where they are sold by unauthorized persons or organizations
- Occurs when product is in short supply, when producers use skimming strategies in some markets, and when goods are subject to substantial mark-ups

Gray Market Issues

- Dilution of exclusivity
- Free riding
- Damage to channel relationships
- Undermining segmented pricing schemes
- Reputation and legal liability

Selling drugs out of date leads to lawsuits.

Dumping

- Sale of an imported product at a price lower than that normally charged in a domestic market or country of origin
- Occurs when imports sold in the U.S. market are priced at either levels that represent less than the cost of production plus an 8% profit margin or at levels below those prevailing in the producing countries
- To prove, both price discrimination and injury must be shown

Price Fixing

- Representatives of two or more companies secretly set similar prices for their products
  - Illegal act because it is anticompetitive
- Horizontal price fixing occurs when competitors within an industry that make and market the same product conspire to keep prices high
- Vertical price fixing occurs when a manufacturer conspires with wholesalers/retailers to ensure certain retail prices are maintained

Transfer Pricing

- Pricing of goods, services, and intangible property bought and sold by operating units or divisions of a company doing business with an affiliate in another jurisdiction
- Intra-corporate exchanges
  - Cost-based transfer pricing
  - Market-based transfer pricing
  - Negotiated transfer pricing

Countertrade

- Countertrade occurs when payment is made in some form other than money
- Options
  - Barter
  - Counterpurchase or parallel trading
  - Offset
  - Compensation trading or buyback
  - Switch trading

Barter

- The least complex and oldest form of bilateral, non-monetary countertrade
- A direct exchange of goods or services between two parties

Looking Ahead to Chapter 12

Global Marketing Channels and Physical Distribution