PRICING AT GENVET PHARMACEUTICALS*

PRODUCT:

Genvet Pharmaceuticals Inc. sells many products in the veterinary pharmaceutical market, both for the cure and prevention of disease (e.g., antibiotics) and to increase productivity in the raising of farm animals (e.g., hormones, mineral supplements). GENVET's new product, Tymacin, is a growth hormone for cattle and hogs. The hormone increases productivity in two ways:

1. by reducing the amount of time that an animal must be kept in a feedlot before reaching it's optimal weight for slaughter, and
2. by increasing the "feed efficiency," the amount of weight gained for every pound of feed that an animal eats.

COST:

The cost of developing and testing Tymacin was approximately $32M. The incremental cost of producing and marketing it is approximately $7 per pound.

MAJOR CUSTOMERS:

Tymacin could be used by both hog farmers and cattle ranchers. Both currently purchase competitive growth hormones and other veterinary pharmaceuticals through independent distributors of agricultural supplies. In most cases, the same distributors carry products for both of these markets.

VALUE IN THE HOG MARKET:

The value of Tymacin to hog farmers is fairly easy to calculate. The cost of competing growth hormone is $11 per pound. Optimal growth is achieved with six pounds of the competitive hormone per ton of feed. Since Tymacin in more concentrated, each ton of feed would require only three lbs. of Tymacin for equal effectiveness. The corresponding reference value of Tymacin is, therefore, $22/lb. Since Tymacin is no more effective than competing products designed to make hogs grow faster and bigger, it has no differentiation value.

* Source: Nagle and Holden, The Strategy and Tactics of Pricing Instructors Manual, 2nd Edition (2002).

VALUE IN THE CATTLE MARKET:

Tymacin is worth more when fed to cattle for two reasons:

1) It is more costly to add weight to cattle than to hogs because the cattle eat more expensive feed.
2) The amount of Tymacin added to cattle feed for optimal growth is only two pounds/ton, rather than three pounds/ton in the case of hogs.

The savings to a cattle rancher from adding Tymacin to cattle feed is $76 per ton, or $38 per pound of Tymacin, when compared with the cost of feeding grain without any hormones. The most effective growth hormone available from a competitor also requires only two pounds per ton of feed, but is less effective at increasing "feed efficiency" than is Tymacin. The competitive product saves the farmer only $62 per ton of feed, and costs $24 per pound.

VOLUMES:

The North American sales potential for Tymacin is approximately 3.1 million pounds for the hog market and 1.8 million pounds for the cattle market.

THE MARKET:

While cattle and hog farmers generally have little interaction, they buy their feed and feed additives from the same distribution companies. Distributors are knowledgeable about the products they carry. Moreover, this market is regulated by the FDA. Under FDA regulations, generic products must be approved separately for each type of animal based upon independent tests. The approval, however, is by chemical composition, not by brand name. Consequently, while GENVET could market the product under different names to the two segments, it could not keep customers in one market segment from buying and using the product intended for the other segment.

QUESTIONS

1. What is the economic value of Tymacin in the cattle market?

2. How would you segment this market and price this product to maximize profitability?