Product Development and Pricing Strategies

Better Business

2nd Edition

Solomon (Contributing Editor) • Poatsy • Martin
Learning Objectives

1. How is a product distinguished from a total product offer?
2. What is product differentiation, and what role does it play in product development?
3. What are the different classifications of consumer products and business-to-business products?
4. Why is branding beneficial to both buyers and sellers, and what are some branding strategies?
5. What steps take place during new product development, and what is the product life cycle?
6. What are some pricing objectives, and how do they relate to the marketing mix?
7. What are the three major approaches to pricing strategy, and what are some pricing tactics used to launch a new product, impact price perceptions, and adjust prices?
Total Product Offer

Product levels
- Core: basic
- Actual: tangible
- Augmented
  - core + actual + all real and perceived benefits
Product Differentiation

• The process of distinguishing a product from its competition
  - With physical or intangible differences
• Critical for a product’s success
  - Helps motivate customers to buy
• Companies define a target market and create total product offerings
  - Consumer input helps
Product Lines and Product Mix

• **A product line** is a group of similar products marketed to one general market
  - Product line length is the number of products in a product line

• **A product mix** is the combination of all product lines offered for sale by a company
  - Product mix width refers to the number of different product lines a company offers
## Consumer and B2B Products

<table>
<thead>
<tr>
<th>Consumer</th>
<th>Business to Business</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Purchased by households for personal consumption</td>
<td></td>
</tr>
<tr>
<td>• Traded in consumer markets</td>
<td>• Sometimes called <em>industrial products</em></td>
</tr>
<tr>
<td></td>
<td>• Purchased by businesses for further processing, resale, or as supplies</td>
</tr>
<tr>
<td></td>
<td>• Traded in B2B markets</td>
</tr>
</tbody>
</table>

Can an item be a consumer product *and* a B2B product too?
Consumer Product Classifications

Convenience goods and services

Specialty goods and services

Shopping goods and services

Unsought goods and services
B2B Classifications

- Equipment
- Maintenance, Repair, Operating (MRO)
- Raw and Processed Materials
- Component Parts
- Specialized Professional Services
Branding

• Brand
  - Is a name, term, symbol, or design that distinguishes a company and its products from all others
  - Is an important product differentiation tool

• Brand extension

• Trademark
  - Knockoff brands
Brand Loyalty & Brand Equity

• Brand loyalty
  - Brand recognition
  - Brand preference
  - Brand insistence

• Brand equity

• Brand awareness

• Brand association
Figure 13.2
Branding Strategies

- Manufacturer's Branch
  - Family Brands
    - Bic makes:
      - pens
      - lighters
      - razors
  - Individual Brands
    - Sarah Lee makes:
      - Ball Park
      - Hillshire Farm
      - Klw
      - Ironkids
- Private Brands
  - Sears has:
    - Kenmore
    - Craftsman
    - Die Hard
- Co-Brands
  - Intel & Dell
  - Gillette & Duracell
  - Healthy Choice & Kelloggs
- Generic Brands
  - Cokes
  - Medicine
  - Paper Towels
  - Cola
Packaging

• Crucial to success of product, because customers typically see the packaging before they see the product

• Packaging
  - Contains/protects product
  - Facilitates use/convenience
  - Promotes product
  - More emphasis on being environmentally friendly
The Importance of Labels

- Labeling serves two functions: to inform and to persuade
- Fair Packaging and Labeling Act of 1966 requires
  - The product identity
  - Name and place of business
  - Net quantity
- Nutrition Labeling and Education Act of 1990 requires consistent nutrition and health claims
- Labels promote the product’s features, benefits, and brand
New Product Development

Step 1: Idea Generation
- Brainstorm new product ideas
- Think of ways to improve an existing product

Step 2: Idea Screening
- Ask yourself: will my target market benefit from this product?
- Ask yourself: can this product be competitive with similar products?

Step 3: Product Analysis
- Determine a desired sale price
- Assess the cost of production

Step 4: Development and Testing
- Produce a virtual or conceptual prototype
- Get feedback from potential customers

Step 5: Product and Marketing Mix Development
- Produce physical prototype
- Obtain more feedback from potential customers

Step 6: Market Testing
- Place product in select target market
- Virtual reality or simulated tools can help customers

Step 7: Commercialization
- Introduce the product to the market
- Begin the rollout process
## The Product Life Cycle

<table>
<thead>
<tr>
<th>Characteristics</th>
<th>Time</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td>Low sales</td>
</tr>
<tr>
<td></td>
<td>Radically rising sales</td>
</tr>
<tr>
<td></td>
<td>Peak sales</td>
</tr>
<tr>
<td></td>
<td>Declining sales</td>
</tr>
<tr>
<td>Costs</td>
<td>High cost per customer</td>
</tr>
<tr>
<td></td>
<td>High cost per customer</td>
</tr>
<tr>
<td></td>
<td>Low cost per customer</td>
</tr>
<tr>
<td></td>
<td>Low cost per customer</td>
</tr>
<tr>
<td>Profits</td>
<td>Negative</td>
</tr>
<tr>
<td></td>
<td>Rising</td>
</tr>
<tr>
<td></td>
<td>High</td>
</tr>
<tr>
<td></td>
<td>Declining</td>
</tr>
<tr>
<td>Customers</td>
<td>Innovators</td>
</tr>
<tr>
<td></td>
<td>Innovators</td>
</tr>
<tr>
<td></td>
<td>Middle majority</td>
</tr>
<tr>
<td></td>
<td>Laggards</td>
</tr>
<tr>
<td>Competitors</td>
<td>Few</td>
</tr>
<tr>
<td></td>
<td>Growing number</td>
</tr>
<tr>
<td></td>
<td>Stable number beginning to decline</td>
</tr>
<tr>
<td></td>
<td>Declining number</td>
</tr>
</tbody>
</table>

### Marketing Objectives

<table>
<thead>
<tr>
<th></th>
<th>Create product awareness and trial</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Maximize market share</td>
</tr>
<tr>
<td></td>
<td>Maximize profit while defending market share</td>
</tr>
<tr>
<td></td>
<td>Reduce expenditure and milk the brand</td>
</tr>
</tbody>
</table>

### Strategies

<table>
<thead>
<tr>
<th>Product</th>
<th>Offer a basic product</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Offer product extensions, services, warranty</td>
</tr>
<tr>
<td></td>
<td>Diversity brands and models</td>
</tr>
<tr>
<td></td>
<td>Phase out weak items</td>
</tr>
<tr>
<td>Price</td>
<td>Charge cost-plus</td>
</tr>
<tr>
<td></td>
<td>Price to penetrate market</td>
</tr>
<tr>
<td></td>
<td>Price to match or beat competitors</td>
</tr>
<tr>
<td></td>
<td>Cut prices</td>
</tr>
<tr>
<td>Distribution</td>
<td>Build selective distribution</td>
</tr>
<tr>
<td></td>
<td>Build intensive distribution</td>
</tr>
<tr>
<td></td>
<td>Build more intensive distribution</td>
</tr>
<tr>
<td></td>
<td>Go selective; phase out unprofitable outlets</td>
</tr>
<tr>
<td>Advertising</td>
<td>Build product awareness among early adopters and dealers</td>
</tr>
<tr>
<td></td>
<td>Build awareness and interest in the mass market</td>
</tr>
<tr>
<td></td>
<td>Stress brand differences and benefits</td>
</tr>
<tr>
<td></td>
<td>Reduce to level needed to retain hard-core loyalists</td>
</tr>
<tr>
<td>Sales Promotion</td>
<td>Use heavy sales promotion to entice trial</td>
</tr>
<tr>
<td></td>
<td>Reduce to take advantage of heavy customer demand</td>
</tr>
<tr>
<td></td>
<td>Increase to encourage brand switching</td>
</tr>
<tr>
<td></td>
<td>Reduce to minimal level</td>
</tr>
</tbody>
</table>
# Marketing Decisions Affect a Product’s Life Cycle

<table>
<thead>
<tr>
<th>Marketing Decision</th>
<th>Example</th>
</tr>
</thead>
<tbody>
<tr>
<td>Extend life of an existing product</td>
<td>Automobile discounts, rebates, and low-interest loans</td>
</tr>
<tr>
<td>Create new uses</td>
<td>Arm &amp; Hammer baking soda as a refrigerator deodorizer</td>
</tr>
<tr>
<td>Create new markets</td>
<td>Home Depot and Lowe’s do-it-yourself training</td>
</tr>
<tr>
<td>Extend technology</td>
<td>Jell-O gelatin to puddings and other snacks</td>
</tr>
<tr>
<td>Repackage</td>
<td>Coca-Cola 6-oz bottles to 8-oz cans</td>
</tr>
<tr>
<td>Reposition</td>
<td>“This isn’t your father’s Oldsmobile” campaign</td>
</tr>
</tbody>
</table>
Product Pricing & Pricing Objectives

1. Maximizing profits
2. Achieving greater market share
3. Maximizing sales
4. Building traffic
5. Status quo pricing
6. Survival
7. Creating an image
8. Achieving social objectives
Pricing Strategies: Cost-Based Pricing

• Charging a price in relation to the costs of providing a good or service
• Simple and popular pricing strategy

• Advantages
  - Easy to calculate and administer
  - Requires minimum information

• Disadvantages
  - Ignores consumer price expectations and competitors’ prices
  - Provides little incentive to keep costs low
Cost-Based Pricing Example

You make 100 units of a product at a total cost of $2,000
   Per unit cost is $2,000 / 100 = $20

   To make a unit profit margin, or markup, of 20%:
      \[ 0.20 \times 20 = 4 \]

   You need to charge:
      \[ 20 + 4 = 24 \]

   Total revenue = 100 \times 24 = 2,400
   Profit = 2,400 – 2,000 = 400
Demand-Based Pricing

• Sometimes called value-based pricing
• Pricing a good or service based on the demand for the product or its perceived value
• Target costing: estimates value
• Price discrimination: Charging different prices for different customers
## Competition-Based Pricing

- Prices based on what the competition charges

<table>
<thead>
<tr>
<th>Type of Competition</th>
<th>Pricing Strategy</th>
</tr>
</thead>
<tbody>
<tr>
<td>Monopolistically competitive markets</td>
<td>• Firms with successful product differentiation strategies charge higher prices</td>
</tr>
<tr>
<td></td>
<td>• Some firms may charge lower prices to get an edge on the competition.</td>
</tr>
<tr>
<td>Oligopolies</td>
<td>• Do not compete on price to avoid price wars, competing on product differentiation instead</td>
</tr>
<tr>
<td></td>
<td>• Periodically, a <em>price leader</em> may emerge and others will drop their prices</td>
</tr>
<tr>
<td>Monopoly</td>
<td>• No competition, so has greatest price-setting ability</td>
</tr>
<tr>
<td></td>
<td>• May see <em>predatory pricing</em>, the practice of charging very low prices with the intent to destroy the competition</td>
</tr>
</tbody>
</table>
Pricing Strategies

• When launching a new product
  - Price skimming
  - Penetration pricing
• Everyday low pricing (EDLP)
• Strategies to impact price perceptions
  - Prestige (premium) pricing
  - Psychological pricing
  - Loss leader pricing
  - Reference pricing
Cost-Based Pricing: Break–Even Analysis

• Total costs
  \[ \text{Total costs} = \text{Total fixed costs} + \text{total variable costs} \]

• Break-even volume of production
  \[ \text{Break-even volume of production} = \frac{\text{Total fixed costs}}{\text{Price} - \text{Average variable costs}} \]

• Example
  Total fixed costs = $600, selling price = $24, and average variable costs = $14
  Break-even volume = \[ \frac{\$600}{($24 - $14)} = 60 \text{ units} \]
Adjusting Prices

Price Adjustments

- Discounts
  - Cash
  - Quantity
- Rebates
- Bundling
- Dynamic
- Allowances
- Seasonal
Chapter Summary

1. How is a **product** distinguished from a **total product** offer?
2. What is **product differentiation**, and what role does it play in product development?
3. What are the different classifications of **consumer products** and **B2B products**?
4. Why is **branding** beneficial to both buyers and sellers, and what are some different types of brands?
5. What steps take place during new product development, and what is the **product life cycle**?
6. What are some pricing objectives, and how do they relate to the marketing mix?
7. What are the major approaches to pricing strategy, and what are some pricing tactics used to launch a new product, impact price perceptions, and adjust prices?
This work is protected by United States copyright laws and is provided solely for the use of instructors in teaching their courses and assessing student learning. Dissemination or sale of any part of this work (including on the World Wide Web) will destroy the integrity of the work and is not permitted. The work and materials from it should never be made available to students except by instructors using the accompanying text in their classes. All recipients of this work are expected to abide by these restrictions and to honor the intended pedagogical purposes and the needs of other instructors who rely on these materials.