Rethinking Sales Targets and Pricing Strategy in a Crisis

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APEC SME Crisis Management Workshop: Marketing Strategy
Today’s SMEs Face a Turbulent Environment

- Increased globalization of the world economy
- Devastating impacts of butterfly effects from corners
- Frequent financial crises
- Development of new and discontinuing technologies
- More demanding customers

What should they do in their marketing operation?
Back to Basics

- “Exchange” - the core concept of marketing- is the process of obtaining a desired product from someone by offering something in return.
- Only when the firm’s product/service value meets customer perceived value, the exchange can be achieved.
- Exchange is a value-creating process because it leaves both parties better off.
- Customers are only and the only source of a firm’s revenue and profit.
Exchange of Value: The Core of Marketing

Value creation: The value chain activities

Brand/Product & Service (at $xx) (4Ps)

Target Customer (Buyers)

Value set of Demand

$
What Is Customer Value?

- Customer value (CV) triad - Quality, Service and Price.
  - \( CV = \frac{\text{(Quality, Service \& Delivery)}}{\text{Price}} \)
- Customer Value = \( \frac{\sum\text{Benefit}}{\sum\text{Costs}} \)

Where,

\( \sum\text{Benefit} = \text{Functional Benefit} + \text{Emotional Benefit} + \text{Social Benefit} + \text{Experiential Benefit}; \)

\( \sum\text{Costs} = \text{Monetary Costs} + \text{Time Costs} + \text{Physical Costs} + \text{Psychic costs} \)
Customer Satisfaction in Value Terms

Perceived Value $\geq$ Expected Value

After purchased and used/consumed the product and service

From the references such as competitors’ prices, past experiences, alike products...
Exchange of Value: The Core of Marketing

Value creation: The value chain Activities

Repeat exchange of value

Brand/Product & Service (at $xx) (4Ps)

Target Customer (Buyers)

Value set of Demand

Customer Satisfaction (Perceived Value > Expected Value)

Competitors

Seller
Understanding Pricing

- Price - critical element of marketing mix
- Only one of 4Ps - produces revenue; the rest produce costs
- Price is part of customer value.
- Profitable pricing should start with customer value analysis.
Cost-Based versus Value-Based Pricing

(Traditional Cost-Based Pricing)

Value-Based Pricing
Formulating a Profit-Driven Business Strategy

I. Seller’s Objectives and Capabilities (Current & Potential)
   New Product Development
   Viable Product Concept
   Competitor’s Capabilities and Intentions
   Economic Value
   Cost Levels, Structure, and ROI Hurdles

II. Target Segments and Pricing Objectives
Formulating a Profit-Driven Business Strategy (Cont’)

II. Target Segments and Pricing Objectives

- Value-Based Price Structure
- Segment-Specific Product Variations

III. Distribution
- Goals
- Partners

Price Management
- Goals
- Policies

Communication
- Goals
- Media

IV. Performance Measurement and Feedback
- Influencer Tactics
- Price Points
Customers’ Perceptions of Value

Thus buyers’ perceptions of value represent a mental trade-off between the quality or benefits they perceive in the product relative to the sacrifice they perceive by paying the price:

\[
\text{Perceived value} = \frac{\text{Perceived benefits (gain)}}{\text{Perceived sacrifice (give)}}
\]
This model suggests that buyers may use price as an index of perceived product quality as well as an index of the perceived sacrifice that is made when purchasing a product or service.

Perceived value represents a trade-off between buyers’ perceptions of quality and sacrifice and is positive when perceptions of quality are greater than perceptions of sacrifice.
Buyers are assumed to assess product or service quality by the use of cues.

Products, services, or retail stores can be conceptualized as consisting of an array of cues that may serve as indicators of quality.
Quality Cues

<table>
<thead>
<tr>
<th>Extrinsic cues</th>
<th>Intrinsic cues</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Price</td>
<td>• Product-related attributes, such as:</td>
</tr>
<tr>
<td>• Brand Name/ Store Name</td>
<td>• Reliability</td>
</tr>
<tr>
<td>• Packages</td>
<td>• Duration</td>
</tr>
<tr>
<td>• Warranty</td>
<td>• Weight</td>
</tr>
<tr>
<td>• Country of Origin</td>
<td>• Size</td>
</tr>
</tbody>
</table>

...
Price-Perceived Value and Willingness to buy

- Perceived store name
- Perceived warranty
- Perceived country of origin
- Perceived brand name
- Perceived quality
- Maximum acceptable quality
- Perceived acquisition value
- Perceived monetary sacrifice-actual
- Perceived monetary sacrifice-reference
- Actual Price
- Perceived Price
- Perceived Reference Price
- Willingness to buy
The process (5-steps) of Value-Based Pricing

1. Conceptualize Customer Value
2. Understand the Key Value Drives for Customers
3. Calculate Customer Value
4. Communicate Value to Customers
5. Continuously Develop Ways to Capture Customer Value
Step 1: Conceptualize Customer Value

- Customers do not know how to quantify the benefits into monetary terms. The sellers must translate the benefits and attributes into perceived benefits for perspective buyers. Particularly, the seller must conceptualize how the services it provide along with the product offer benefits to customers.

- The seller must compare the relative benefits of its offering to the benefits of competitive offerings to establish the equivalent value.
Step 2: Understanding the Key Value Drivers for Customer segments

For a seller’s products and services,

\[
\text{customer value } i = \frac{\Sigma \text{ Benefits}}{\Sigma \text{ Cost}} \neq \text{ customer value } j = \frac{\Sigma \text{ Benefits}}{\Sigma \text{ Cost}}
\]

- Not all buyers benefit from the same attributes equally. Buyers do not attach the same weight to the sacrifices required to obtain the product.
- Thus, it is important to develop a value profile of the firm’s customer segments.
- Sales teams and members of the management may first co-develop each segment’s value profile from their own perceptions of what they believe their customers value. Then, they compare their delved customer value with what the customers reveal themselves.
Step 3: Calculate Customer Value: Value-in-Use Analysis and Value Mapping

Value-in-Use Analysis:

- Firms must determine customer value segments and estimate the economic value they provide to these different segments.
- For B2B marketing it is important that the firm determine how it influences customers’ costs and revenues or cash flows. Sellers must identify and quantify how their customers can reduce and avoid costs.
- When doing this analysis, it is helpful to determine what customers’ costs are a function of customers’ requirements.
- It is also useful to determine how competitors affect the customers' cost.
### Finding the sources of customers’ value in use

#### Cost-Based Sources of Value
- Productivity increases
- Training/ Learning savings
- Maintenance/ Set-up Savings
- Hiring/ Turnover Savings
- Material Handling Savings

#### Revenue-Based Sources of Value
- Helping Customers:
- Gain a cost advantage
- Gain new customers
- Change to a more profitable customer mix
- Increase their sales volume or market share
- Improve the performance capability of their products
Step 3-2 : Value-in-Use Analysis

Determining Maximum acceptable price to customers

Life- cycle costs

Purchase Price

Post-purchase cost (discounted)

Start-up costs

Product X “Old” (Reference product)  Product X “New”

Purchase Price

Post-purchase cost (discounted)

Start-up costs

$ 1,000

$ 400

$ 300

$ 300

$ 300

$ 200

$ 200

$ 200

Improvement Value

Relative economic value $800

$ 400

$ 300

$ 300

$ 200

Relative economic value

$ 800

$ 400

$ 200

$ 300

$ 300

$ 200

$ 200
Step 3-3: Value-in-Use Analysis

Determining Seller’s Price

Maximum Price

- $800
- $400

Seller’s Pricing discretion

- $200

Direct variable costs

- $400

Customer’s Inducement (Buyers’ surplus)

Contribution margin

- $200

Seller’s price

- $400
Economic Value Analysis

Differentiation Value is the value to the customer (both positive and negative) of any differences between your offering and the reference product.

Reference Value is the cost (adjusted for differences in units) of the competing product that the customer views as the best alternative for this one.
## Economic Value Estimation for Advertising

<table>
<thead>
<tr>
<th></th>
<th>Competing Magazine</th>
<th>Our Magazine</th>
<th>Advantage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Circulation</td>
<td>1,400,000</td>
<td>1,550,000</td>
<td>11%</td>
</tr>
<tr>
<td>Readers per copy</td>
<td>1.8</td>
<td>2.1</td>
<td></td>
</tr>
<tr>
<td>Readership</td>
<td>2,520,000</td>
<td>3,255,000</td>
<td>29%</td>
</tr>
<tr>
<td>% See ad</td>
<td>9.2%</td>
<td>14.50%</td>
<td></td>
</tr>
<tr>
<td>% Motivated/ ad seen</td>
<td>1.60%</td>
<td>2.20%</td>
<td></td>
</tr>
<tr>
<td>% Sold/ motivated</td>
<td>20%</td>
<td>20%</td>
<td></td>
</tr>
<tr>
<td># Readers sold</td>
<td>742</td>
<td>2077</td>
<td>180%</td>
</tr>
<tr>
<td>Sales per customer</td>
<td>$180</td>
<td>$200</td>
<td></td>
</tr>
<tr>
<td>Gross margin</td>
<td>30%</td>
<td>30%</td>
<td></td>
</tr>
<tr>
<td>Value of ad</td>
<td>$40,062</td>
<td>$124,601</td>
<td>211%</td>
</tr>
<tr>
<td>Cost of ad</td>
<td>$29,000</td>
<td>$67,400</td>
<td></td>
</tr>
<tr>
<td>Return on ad</td>
<td>$11,062</td>
<td>$57,201</td>
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</table>
Step 3- 4 : Value Mapping

Developing a customers’ value map

A value map illustrates the way customers in a value segment trade off perceived benefits against perceived price.
Step 3-4: Data collection for Value Mapping

- Sellers (firms) can use customer interview and focus groups to get the necessary information. From these interviews, the firm seeks to obtain a comprehensive history of the features and attributes of the products and services that customers consider important when making purchase decisions.

- Customers should be asked to list all suppliers (competitors) that they consider when making such decisions.
## Step 3: Value Mapping - Example

<table>
<thead>
<tr>
<th>Incremental Benefit</th>
<th>Improvement Factor, %</th>
<th>Benefit weight</th>
<th>(2) × (3)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Material savings</td>
<td>35</td>
<td>0.2</td>
<td>7.0</td>
</tr>
<tr>
<td>Output/hour</td>
<td>10</td>
<td>0.2</td>
<td>2.0</td>
</tr>
<tr>
<td>Adaptability</td>
<td>5</td>
<td>0.2</td>
<td>1.0</td>
</tr>
<tr>
<td>Quality of applications</td>
<td>10</td>
<td>0.2</td>
<td>2.0</td>
</tr>
<tr>
<td>Less maintenance</td>
<td>10</td>
<td>0.2</td>
<td>2.0</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>1.00</strong></td>
<td></td>
<td><strong>14.0</strong></td>
</tr>
</tbody>
</table>

### Brand (Firm) B

<table>
<thead>
<tr>
<th>Incremental Benefit</th>
<th>Improvement Factor, %</th>
<th>Benefit weight</th>
<th>(2) × (3)</th>
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</thead>
<tbody>
<tr>
<td>Material savings</td>
<td>50</td>
<td>0.5</td>
<td>25.0</td>
</tr>
<tr>
<td>Output/hour</td>
<td>10</td>
<td>0.1</td>
<td>1.0</td>
</tr>
<tr>
<td>Adaptability</td>
<td>5</td>
<td>0.1</td>
<td>0.5</td>
</tr>
<tr>
<td>Quality of applications</td>
<td>10</td>
<td>0.2</td>
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<tr>
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<td>0.1</td>
<td>1.0</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>1.00</strong></td>
<td></td>
<td><strong>29.5</strong></td>
</tr>
</tbody>
</table>
Aligning Price with Value

Price

<table>
<thead>
<tr>
<th>High</th>
<th>Medium</th>
<th>Low</th>
</tr>
</thead>
<tbody>
<tr>
<td>Missed Opportunities</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Value Received

Price = Value

Un-harvested Value
Step 4: Communicate Value to Customers

The Communication Principles (1)

1. Keep price structures understandable, flexible, and relatively easy to administer.
2. Consistently and clearly communicate price structure. Discounts, allowances, rebates, and rewards for loyalty should be aboveboard and clearly defined.
3. Provide complete and accurate information about each offer.
4. Provide appropriate reference price and actual selling price.
5. Avoid vague phrasing (e.g., “save up to 50 percent”)
Step 4 : Communicate Value to Customers
the Communication Principles (2)

6. Minimize the amount of work and effort required for customers to take advantage of an offer.

7. Refrain from using “suggested list price” or similar phrases; buyers may distrust these phrases, and they may be considered deceptive.

8. Communicate the total savings in an offer; minimize the need for buyers to make calculations to determine savings.

9. Place a reference value on any “free” aspect of an offer.
Step 5: Continuously Develop Ways to Capture Customer Value

- Being “value-oriented” involves not just satisfying customers, but creating perceived value by framing the context of customer judgments and preference formation.
- Pricing depends not only on careful measurement of customer perceptions, but also on developing effective strategies and tactics to manage those perceptions toward the true value of a firm’s products and services.
Reacting to Price Competition

Accommodate or Ignore

Is your position in other markets threatened if competitor gains share?

Yes

Does the value of the markets at risk justify the cost of a response?

No

Respond

Yes

Competitive Price Cut or New Product Entry

Is there a response that would cost less than the preventable sales loss?

No

If you respond, is competitor willing and able to cut price again to reestablish the price difference?

Yes

Will the multiple responses required to match a competitor still cost less than the avoidable sales loss?

Yes

Respond

No
## Options for Reacting to Price Competition

<table>
<thead>
<tr>
<th>Competitor is Strategically</th>
<th>Weaker</th>
<th>Neutral or Stronger</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Price Reaction is</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Too Costly</td>
<td>IGNORE</td>
<td>ACCOMMODATE</td>
</tr>
<tr>
<td>Cost-Justified</td>
<td>ATTACK</td>
<td>DEFEND</td>
</tr>
</tbody>
</table>
The Value-Based Marketing (5Cs)

- **Comprehend** what drives sustainable value for customers
- **Create** value for customers
- **Communicate** the value that you create
  - Tangible features
  - Intangible features
- **Convince** customers that they must pay for value received
- **Capture** value with appropriate price metrics and fences