Global Marketing Management

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Lecture-24
Global pricing part-1

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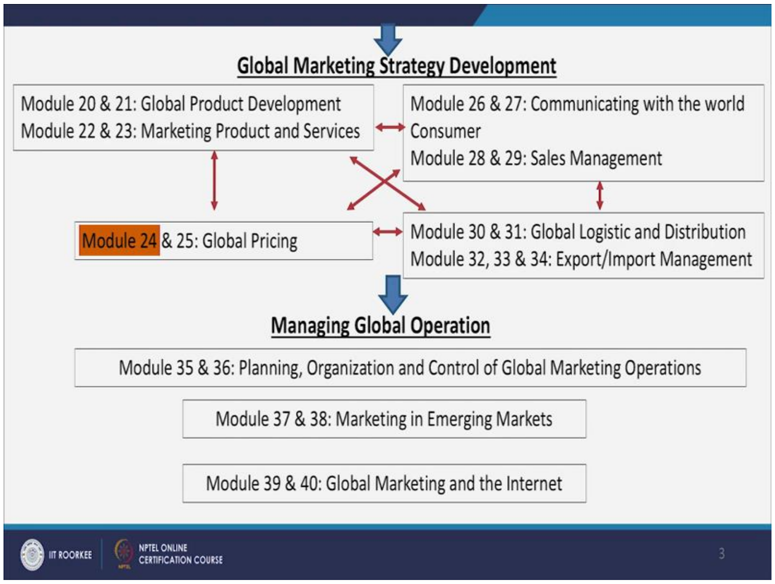

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Welcome to this course on, Global Marketing Management and now we will talk about Global pricing which is spread over module 24 and 25. So we will start with module 24 and let us see what are the things that will be talking about this module? First is the driver of foreign market pricing. Now, the problem is that the same product exactly, exactly similar looking product, of same looking product, they are priced differently in different countries. Why it is so, so what are the drivers for that, it and it is not only government regulation that are like that. So we will understand, what makes the price of our same product different in different countries. Then we will talk about, managing price escalations. So when the prices of the product goes up, start going up, then what the company should do, and then, what should be done in inflationary environment, where the prices keep in because of inflation the pricing, the prices keeps on increasing then how to go about doing pricing in that.

So today the inflation is different, tomorrow it increases and day after tomorrow again get, again it increases, so how we go about doing pricing in that kind of environment .So this is the most critical and complex issue in international marketing and that is the pricing. Price is the only marketing mix that creates revenues, all other elements of the marketing mix that create cost.

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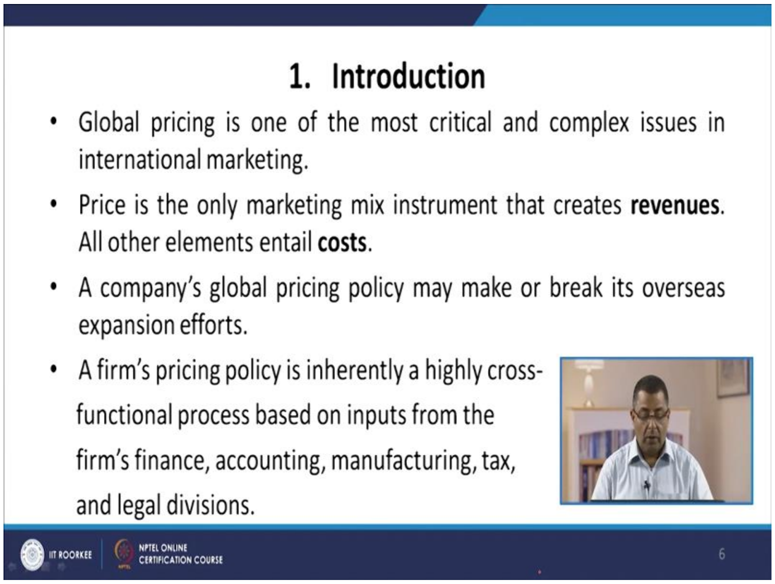

A global pricing policy may make or break its overseas expansion efforts, so if the pricing is not sufficient enough to cover the cost and add to profits, then the companies, obviously the survival will be at Stake. And a firm's pricing policy in is inherently a highly cross functional process based on input from the firm's finance, accounting, manufacturing, tax and legal divisions. So the company maybe raising finances at a different rate in one country and they may be raising finance at a different rate, rate in another country.

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So multinational also face the challenge of how to co-ordinate their pricing across different countries because if the price differential is huge then smuggling will start. The people will start smuggling product and from there, in countries from where they are priced low, to countries where they are priced high. So it is not piracy. The lack of coordination will create a parallel trade or gray market situation. With parallel imports, middlemen make a profit by shipping products from low priced countries to higher priced countries, and thereby, that will lead to loss to the company, but they will create profit for the measurement.

These imports will compete with high price different product offered by legitimate distributors. so two, both this products they are original but one has come as lesser price, while the original, original while, while the other product that is being sold by, by the company's middlemen it is priced higher. So thereby that it creates a parallel trade, that is called as a gray market.

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So what are the factors that affect foreign market pricing the main drivers are first is the company's goal. Goals are different in different countries, company's cost are different in different countries, customer demand again varies from country to country, competition will also be different in different countries, distribution channels used by the company to sell their products will be different and government policies obviously will be different in different countries.

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Now let us look at each one of them in detail. So when developing pricing in strategy the firm need to decide what it want to accomplish with its strategy. The Goals might include maximizing current profits, penetrating the market, projecting a premium image. So depending upon what kind of goals a company wants to pursue in the market, the pricing will be, will be that will affect how the pricing is termed. The company objective will vary from market to market and especially multinational with the large degree of local autonomy. So when the degree of local autonomy is there with a multinational subsidiary then they will price depending upon their objectives while another subsidiary will price their product according to their objectives.

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For example, New Balance, US based market, maker of hi-tech running shoes, sells its shoes in France as haute couture, expensive and fashionable items rather than simple athletic shoes as it does in United States for instance. So in France they have expensive and fashionable while in United States they are not so. They are placed simple athletic shoes. To beef up the premium image, the price in France is almost twice the US price, because objectives of this company in France are different from objectives in US. Therefore the price differential is huge.

Another driver of foreign market pricing is the company's cost. So the company cost trigger prominently in the pricing decisions, because it, because the cost set the floor for pricing, that is the minimum that the company will have to charge. The company wants to set at least a price that will cover all the cost needed to make and sell its product; otherwise obviously they will be at a loss from day one.

So the company's cost consists of two parts, the first is a variable part, the which is called as a variable cost which change with sales volume. So the, as the sale volume changes, the variable cost, that is the cost per head of the item will change, cost of input per head of the item will change.

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And then there are fixed cost overheads that do not vary, whether you make one product or you make one thousand or you don't make any product, any unit. Export pricing policies differ depending upon the way costs are treated. Therefore there are 3 basic options that exist for export pricing. One is the Rigid cost plus pricing. So as the name suggest there the company has a certain amount to the profit on top of the cost.

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So the export price is said by adding all cost incurred in selling the product to the international market and a gross margin. The second option is flexible cost plus pricing, flexible cost plus here it was rigid cost plus, now we are talking of flexible cost plus pricing. It is still in both the cases it is still cost plus pricing. So it closely resembles the first method, but adjust prices to market condition in the host market, that is the level of competition. So this gross margin may be different depending upon the competition. So when the competition is huge then maybe the gross margin comes down, when it is not huge, then the gross margin goes up.

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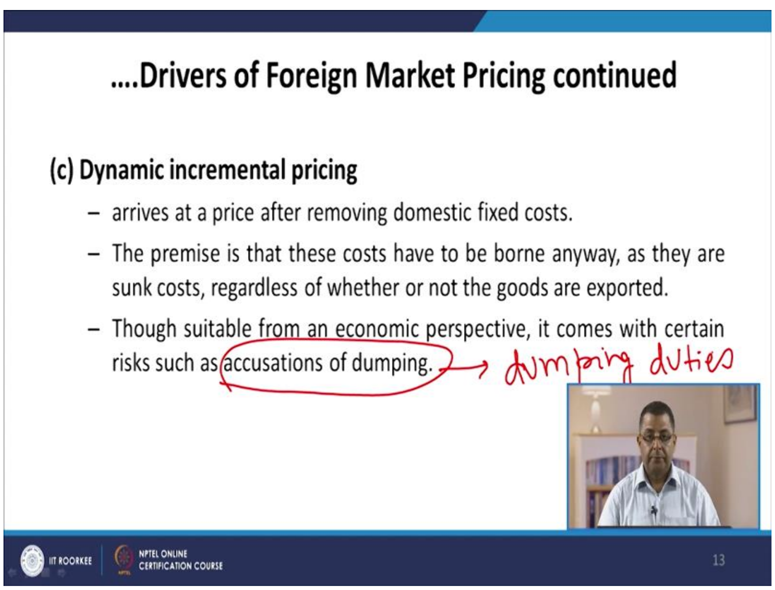

And the third option is dynamic incremental pricing, arrives at a price after removing domestic fixed costs, the premises that these cost have to be borne anyways, as they are sunk costs, regardless of whether or not the goods are exported. Though suitable from an economic perspective, it comes with certain risks such as accusation of dumping. Now the fixed cost are taken care by the domestic, domestic operations while only the variable cost is being covered by the exports so that reduces the price to a large extent and that in that situation that the problem is that the company may attract accusation of dumping and that will lead to attraction of dumping duties.

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The third driver of foreign market pricing is customer demand. What is the demand for that product in that country. So, customer demand is the function of buying power, taste, habits and substitutes. So that is that buying power of the customers their tastes and habits and what are the substitute for that product that are available domestic in that market. Consumers in low per capita income are far more price sensitive. In that case there are four options that can be exercised, to tackle this issue.

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First option is foreign companies targeting the masses in emerging markets such as China or India offer cheaper products with lower costs by changing the product formula, packaging or size. For example how P&G manages these issues, In China it changed the formulation and packaging of Crest Toothpaste, to emphasize cavity prevention, to target middle class, whereas it emphasize the whiting benefits for premium crest products.

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What are the risks associated with this option, the first is brand dilution. A premium brand loses its prestige when a large number of consumers start using it, because it was not supposed to be used by large number of consumers, so that leads to brand dilution. And the second disadvantage is disadvantage or risk is cannibalization. It occurs when high income customers switch to cheaper products in the firm's product portfolio. So people who were buying premium products now they start buying lesser, lesser price products, so that leads to cannibalization.

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To be a, the next option is to be a niche player, for example Starbuck charges by and large the same price worldwide, whether its coffee is, coffee is sold in wealthy Western markets or poorer countries such as Thailand or China. The third option is to have portfolio products that cater to different income tiers. For example, Hindustan Liver, Liver's, Unilever's India subsidiary, dominates many consumer goods categories by following this route. So they have a brand and a product for all price points.

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The fourth option is to sell older versions of the product at low price in market with low buying power. So that is why toyota did not gave it newer versions for their, of their automobiles but rather they came with older versions that they were not sending in other markets. So Daimler also sold older Mercedes models in India; United Distillers sold out of fashion brand such as Vat. The disadvantages such a pricing strategy can backfire, if it manifests a certain amount of arrogance towards the local population and the same thing happened with Mercedes.

So this is the problem here that the pay, local passengers feel that they are being there they are being cheated and they are not being offered with newer version newer model, therefore they do not buy the company's product. Another driver of foreign market pricing is cultural symbolism. It can also; it can also affect pricing decisions.

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In Chinese culture, the number "8" has an auspicious meaning as the word 8 ba, sounds similar to the Chinese word for wealth fa. Special price offers in Chinese cultures often end with at least one eight digit. For instance, Bank Of China, the world's large world third largest bank, set a mortgage arrangement fee of L888 when it started offering mortgages to British houses by, buyers. However, it switched to the more recognizable figure of L995.

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So these are the price promotions from Chinese cultures with price ending 8. So they are all 8. Just for plain simple reason that it is considered to be more auspicious.

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Another driver of foreign market pricing is competition. The competitive situation may vary for a variety of reasons. One is the number of competitors. In some countries, the firm faces very few competitors or even enjoys a monopoly, whereas in other countries the company may have to combat numerous competing brands. Therefore they have to reduce the prices.

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Then the nature of competition can be different, Global vs Local. So in some countries they may be facing global competitors, in some companies, countries, they may be facing local players, private firms versus state owned firms. Some countries they are, they have a competition for from private companies while in other countries they have competition from state owned companies. Even local companies are viewed as national champions and treated accordingly by their local governments.

Such treatment can be in form of subsidies or other goodies, for example cheap loans can be given to the local companies and they are treated as national champions. So, instead of government instead of directly getting into competition with this, they get into competition with multinational because of these small firms, by giving them some kind of goodies or subsidies. A company's competitive position, it will vary across countries, companies will be price leaders, in some countries and price takers, in other countries.

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Some where they, they set the price and some where they take the price highest policies to cut price in the market where it is not the leading brand. Then there are certain non price competition for example advertising channel coverage may be preferable in some countries elsewhere price combats are a way of life. So in some countries you have to reduce price, while in other countries, depending upon the type of competition, there can be, non price competition. For example, advertising and channel coverage.

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So in western countries a prize war is to be avoided at all cost. In contrast, Chinese companies often see a price war as a strategic weapon to grab market dominance. So that is why they keep on reducing price and then they have got into that country of origin effect like price and quality relationship, lower price and lower quality. In many markets, legitimate distribution distributors of global brands need to compete with smugglers. Smuggling operations put downward pressure on the price of the affected product.

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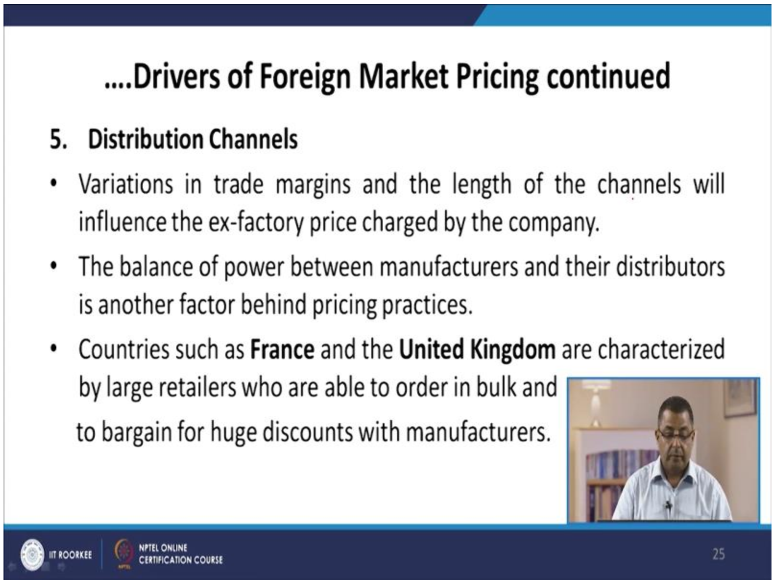

Another driver of foreign, foreign market pricing is are the distribution channels. Variation in trade margins and the length of the channels will influence the ex-factory price charged by the company. For example the number of different middleman that comes from as soon as the product is taken out of the factory and it and it reaches the consumer. The more number of middleman there are there if if the number of middlemen between these two points are more, then obviously the prices will increase, because everyone will keep on adding their percentage, to the cost.

So therefore the variation in trade margins, so somewhere that the retailer may be taking 10% of MRP another at another place, they may be charging 20% for one brand, they may be charging 5% for another brand they may be charging 15% so the balance of power between manufacturers and distributors is another factor behind pricing policy.

So when a company for when a company sells to through large distributors, now this distributors they have large bargaining power huge bargaining power, therefore they may, they may be charging more, more profit of the MRP as compared to when the company sells through, through smaller distributors, retailers. So in countries such as France and United kingdom's are characterized by large retailers, who are able to order in bulk, and to bargain for huge discounts with manufacturers.

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Large Cross Country price gaps open up arbitrage opportunities that lead to parallel imports, that is a gray market we have talked about some time ago from lower price countries to high price ones. These parallel imports are commonly handled by unauthorized distributors at the expense of legitimate channels. To curtail parallel trade, firms can consider narrowing cross-border price disparities. So let us say at one place the product of the price is X and the transportation prices is T, now if that is equal to the price Y, in another country A, this is country B, so then this parallel trade will not happen.

While if the prices in country B, plus transportation cost they are lower than the prices in country A, then obviously there is a chance that, people will, unauthorized distributor will, start parallel trade, in sending products from this country to this country.

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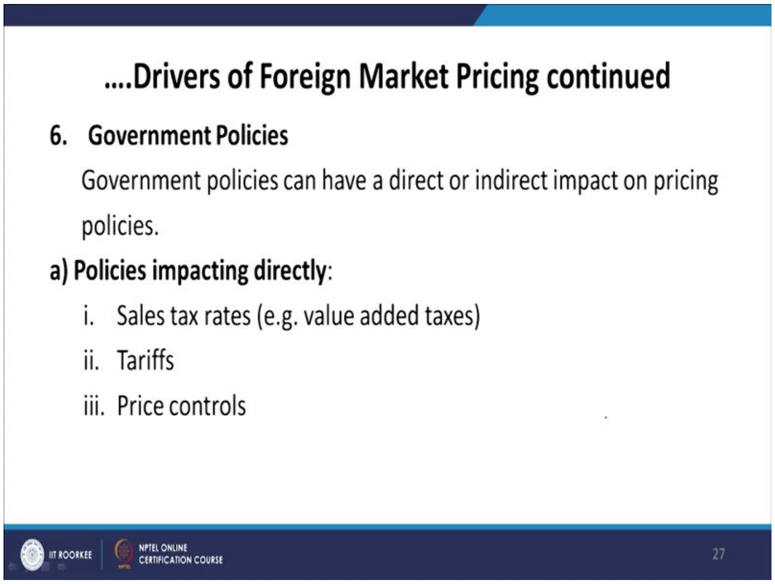

The government policies can also have a direct or indirect impact on pricing. So government several times dictate, for example in India they dictate the price for minimum support price for rice and wheat and various kind of medicines also. So when they when this when there are government policies related to the prices at a company can charge, so that that has to be reflected in the pricing.

So there are policies that impact directly, for example the sales tax rate or the value tax or the GST, then there are tariffs and then governments they control prices for many, many different kind of products. So, as to protect their domestic industry one, to promote their domestic industry two and to protect their consumers within the country that is a third. And increasing in the sales tax rate will usually lower overall demand. In some cases taxes may selectively affect imports.

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For instance in the 19 late 1980, US government introduced a 10% luxury tax on the parts of a car price that exceeds Dollar 30,000. This luxury tax primarily affected the price of luxury import cars since few US made luxury cars sell for more than the dollar 30,000 threshold. So that was primarily for imports.

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Tariffs will inflate the retail price of imports and the third is the price controls. They affect either the whole economy for instance in high inflation countries or selective industries. In many countries, a substantial part of healthcare costs are borne by the government. Prices for reimbursable drugs are negotiated between the government authorities and the pharmaceutical companies because the price has to be reimbursed by the government.

So, it is not only the pharmaceutical companies that can set the price but they have to consult the government also before setting the price for those kind of products. Then there are government policies that affect indirectly, huge government deficit is per interest rate that is the cost of the capital, price volatility and inflation.

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The interplay of these factors will affect the product cost, inflation might also impact labour cost in those countries, for example in Belgium and Brazil that have a wage indexation system. Wages are indexed to the inflation. Such, a system adjust wages for increase in the cost of living.

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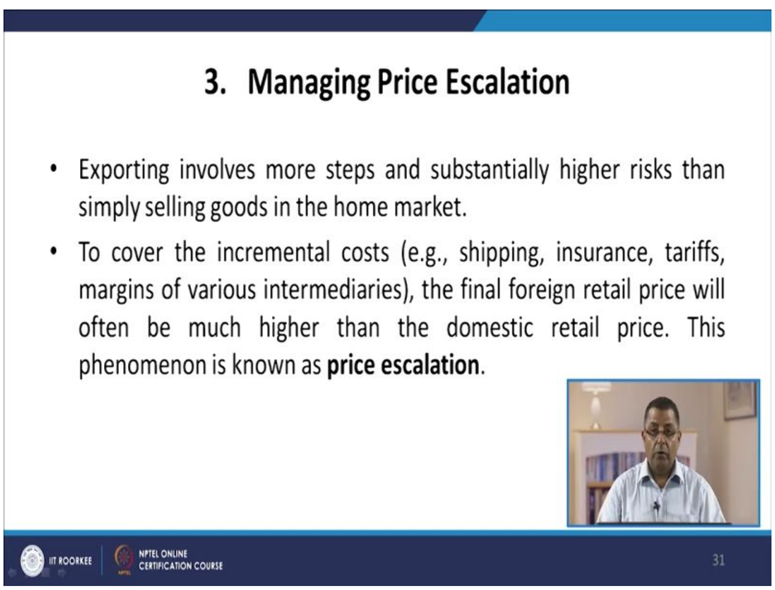

How to manage price escalations? Now export involves more steps and substantially higher risk. Than simply selling goods in the home market, to cover the incremental cost that is the cost of shipping and insurance and tariffs margins of various and margins of various intermediaries, the final foreign retail price will often be much higher than the domestic retail price, because we are adding cost, insurance and freight etc. This phenomena is known as price escalation.

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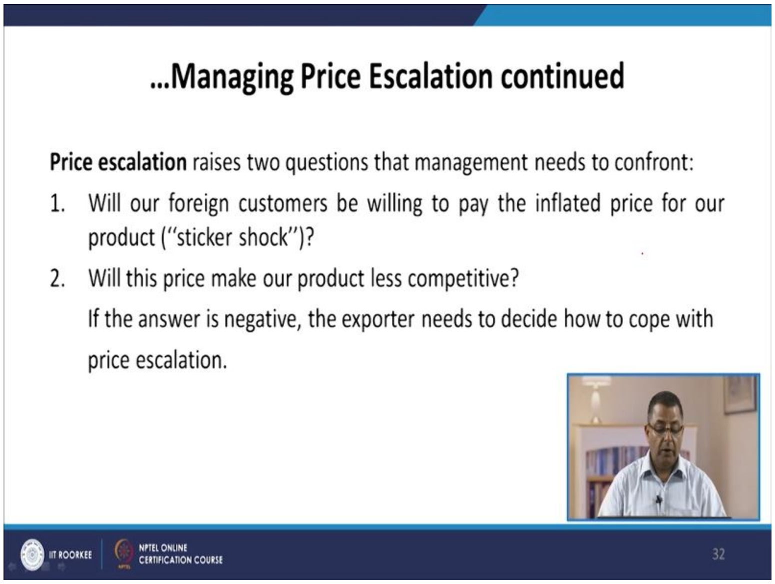

Now this price escalation raises two questions which the management needs to confront. Will our foreign customers be willing to pay the inflated price for our product? So as the prices increases, because of shipping and insurance, so the question is will foreign customers be willing to pay that price? Will this price make our product less competitive? If the prices go up then if the product become less competitive and if the answer is negative, the exporter need to decide how to cope with price escalations, because insurance and tariff are added now, how to reduce the cost, there are two broad approaches to deal with price escalation.

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The first is to find ways to cut export price, so you reduce the reduce the cause of the price of ex factory price and you and Even and even if you add the insurance and freight, then also the total price will be will be lower. Or position the product as a premium or super premium brand, so then it becomes lesser price sensitive; to several options exist to lower the export price. One is to rearrange the distribution channel.

Reduce the number of intermediaries in the distribution channel and therefore the final price will be reduced. Eliminate costly features of the product or make them optional and just sell the core, the core product therefore that will reduce the price. Downsize the product, that is you reduce the size of the product it contains, earlier it used to contain 12 biscuits, now it contains 10 biscuits. Assemble or manufacturer or manufacture the product in the foreign markets, so instead of manufacturing it in your home country, you go and start manufacturing in some other country.

Or adopt the product to escape tariffs or tax levies. So as you have seen in an earlier example of US, US made car price came for less than 30,000 dollars, while they imposed a luxury tax on all kind of cars that came for more than 30000 dollars. So, the hide, so here what they say, is that you reduce the size of the product so that, now it comes in the bracket of less than dollar 30,000. So it will not attract the luxury tax anymore.

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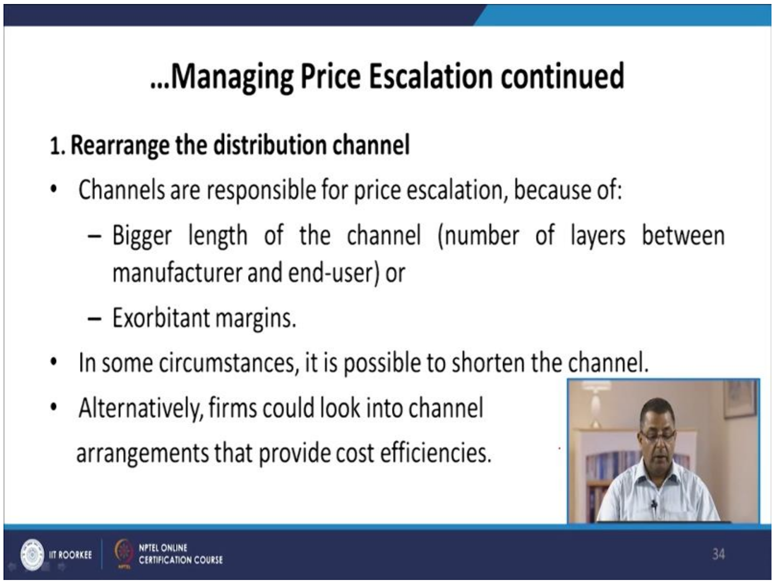

Now we will look at each of these options more in in greater detail. Channels are responsible for price escalation because of, the Bigger length of the channel, the number of layers between manufacturer and end user or exorbitant margins. In some, some circumstances it is possible to shorten the channel. Alternatively, firms could look into channel arrangements that provide cost efficiencies.

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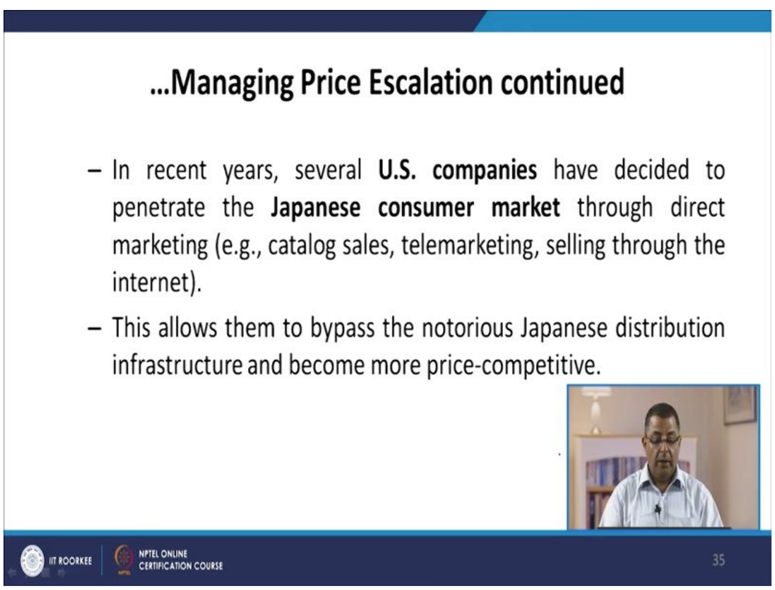

In recent year several US companies have decided to penetrate the Japanese consumer market through direct marketing that is catalog sales, telemarketing, selling through internet. This allows them to bypass the notorious Japanese distribution infrastructure and become more price competitive, viz-a-viz the Japanese product.

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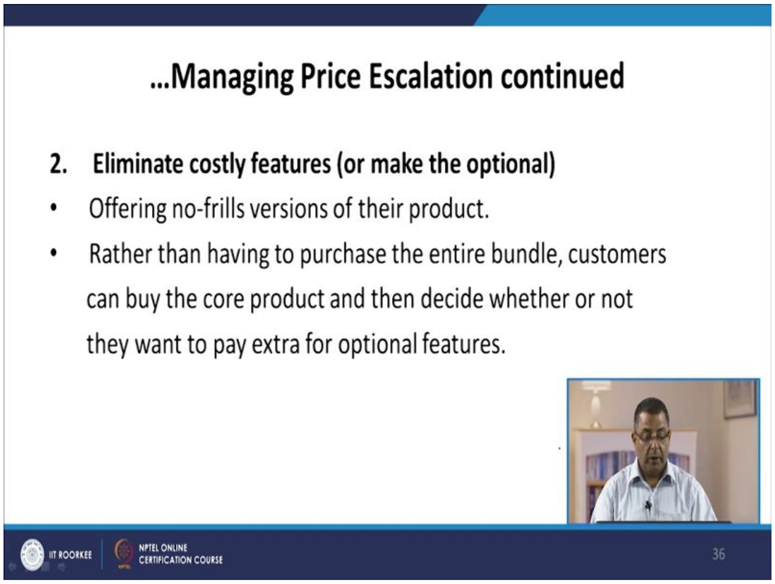

What does eliminate costly features or make them optional means, offering no-frills versions of the product basic the core product. Rather than having to purchase the entire bundle, customers can buy the core product and then decide whether or not they want to pay extra for the optional features.

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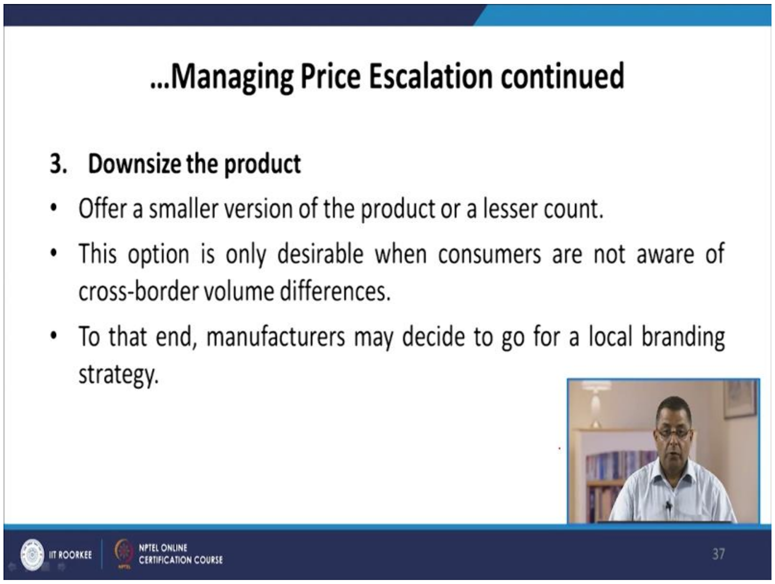

You may downsize the product, downsize the product, offer a smaller version of the product or a lesser count. This option is only desirable when consumers are not aware of cross-border border, boundary differences. So once they get to know what is the total volume, that is being sold at a particular price and this price is not the same kind of ratio is not there in their country then that can become a problem. To that end manufacturers may decide to go for a local branding strategy. So in that case local brands come into play. Assemble of manufacture the product in the foreign markets, foreign markets may not necessarily be the export market. It can be some other country other than the home country.

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Closer proximity to the export market will lower transportation cost and to lessen import duties for goods sold within European Union markets, numerous firms have also decided to set up assembly operations in the EU member States.

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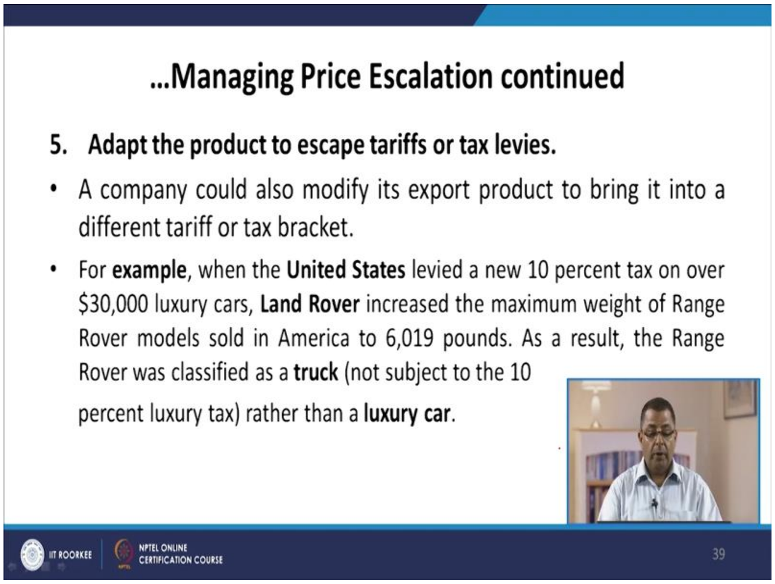

Adapt the product to escape tariff or tax levies. The company could also modify its product export product to bring it into a different tariff or tax bracket. For example, when the United States levied a new 10% tax on over dollar 30,000 luxury cars, Land Rover increased the maximum weight of Range Rover models sold in America to 6,019 pounds. As a result, the Range Rover was classified as truck and not subject to the 10% luxury tax rather than a luxury car.

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Alternatively an exporter can exploit the price escalation situation and go for a premium positioning strategy. For example LEGO, that is a Danish toy maker, sells building block sets in India that are priced between dollar 6 and dollar 223, far more than most other toys that Indian parents can purchase. To justify the premium price, LEGO uses a marketing strategy that targets middle class parents and stresses the educational level of LEGO.

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Now what to do to Price in Inflationary Environments, Inflationary environment where prices are not stable and they keep on changing, so when McDonald's opened doors its door in January 1990 a Big Mac meal, including fries and a soft drink, in Moscow, cost 6 rubles. 3 years later, the same meal cost 1,100 rubles. Rampant inflation is a major obstacle to doing business in many countries. Moreover high inflation rates are usually coupled with highly volatile exchange rate movements, because as inflation increases, the currency that affect the currency, the value of the currency, of that country. So, that that becomes a double edged problem.

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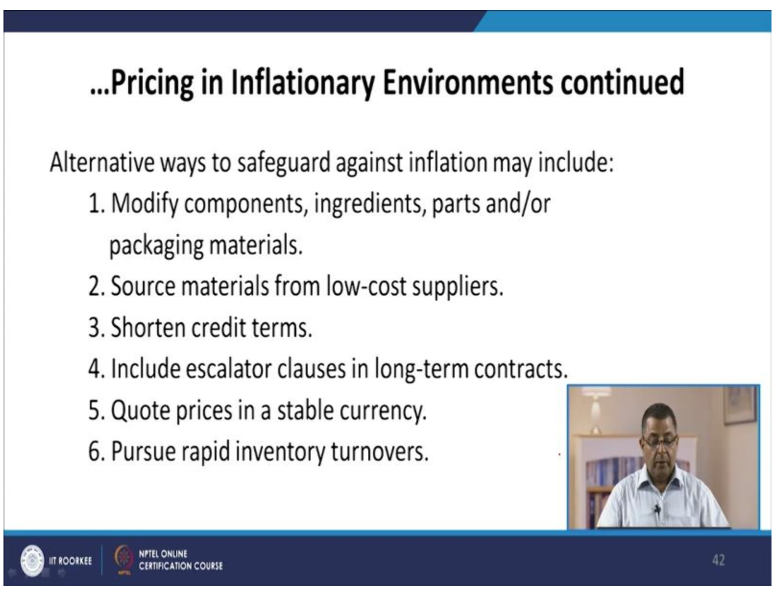

Now what are the ways to safeguard against inflation, the first is to modify components, ingredients, parts and or packaging materials. So you can have a different kind of ingredients and packaging material, source material from a low cost supplier. So therefore your cost remains low. Shorten the credit terms of the whole of the supply chain, it may, it was 45 days earlier and now you can reduce it 30 or 15 days. Including include escalator clause in long term contracts. So you may include increasing price when you are signing long term contracts. Quote prices in a stable currency so don't use that country's currency, but use a stable currency in which you will quote your prices and Pursue Rapid inventory turnovers so that reduces the inventory carrying cost.

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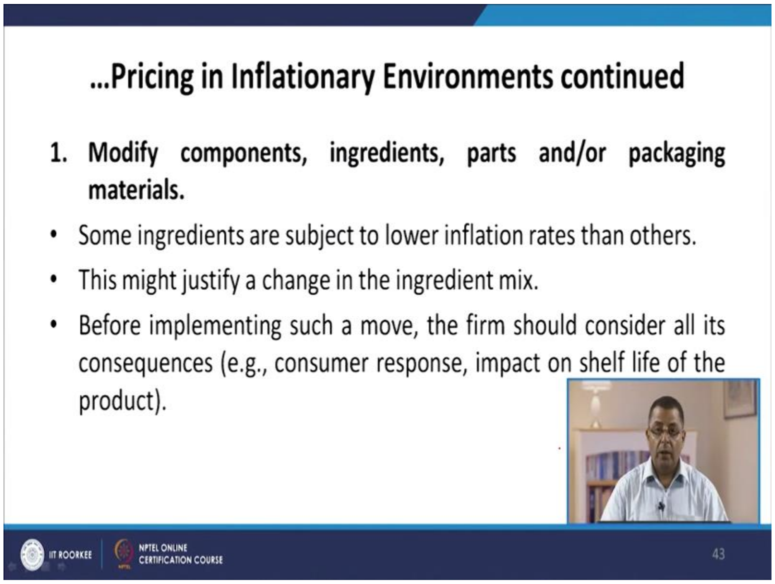

So let us look at each one of them. Modify components, ingredients, part and of packaging material. Some ingredients are subject to lower inflation rates than others. This might justify a change in the ingredients mix. Before implementing such a move, the firm should consider all its consequences, that is, the consumer responses, impact on shelf life of the product.

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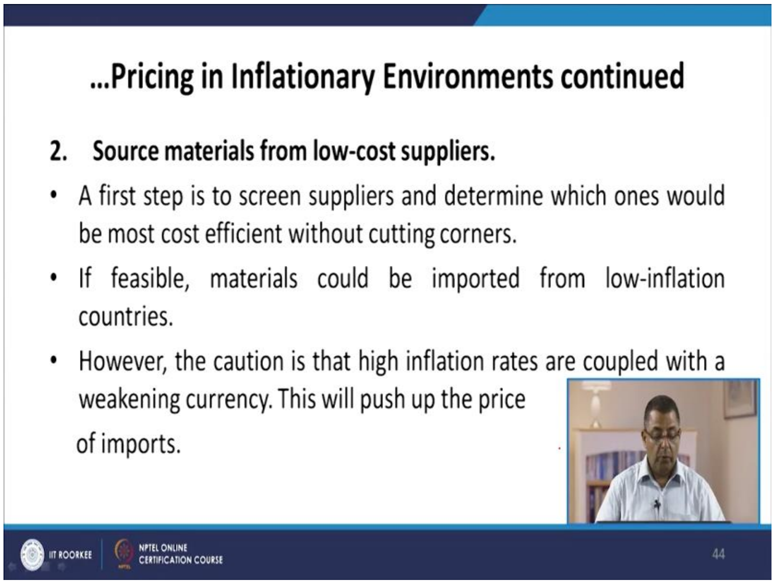

The next is the source material from low cost suppliers of first step is to screen suppliers and determine which ones would be most cost-efficient without cutting corners. If feasible, materials could be imported from low inflation countries. However, the caution is that high inflation rates are coupled with the weakling currency. This will push up the price of imports.

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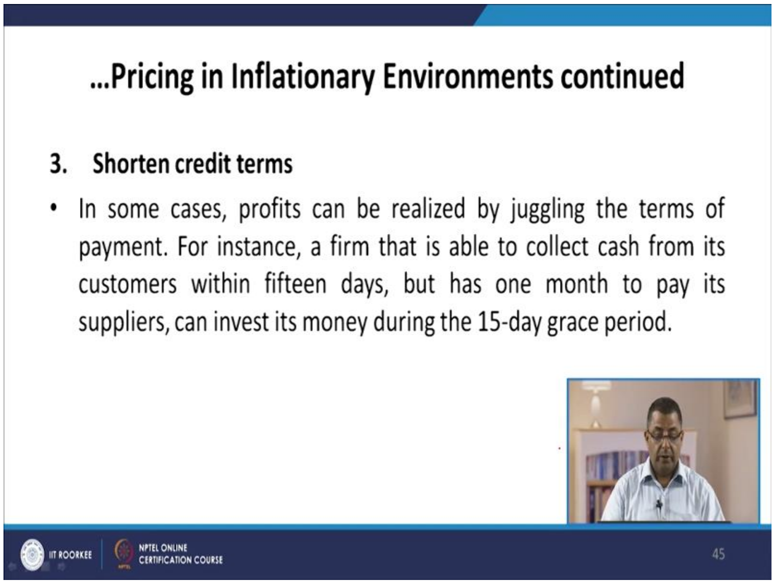

Shorten the credit terms. In some cases profits can be realized by juggling the terms of payment. For instance, a firm will be able to collect cash from its customers within 15 days but has one month to pay its suppliers, it can invest the money during this 15 days grace period.

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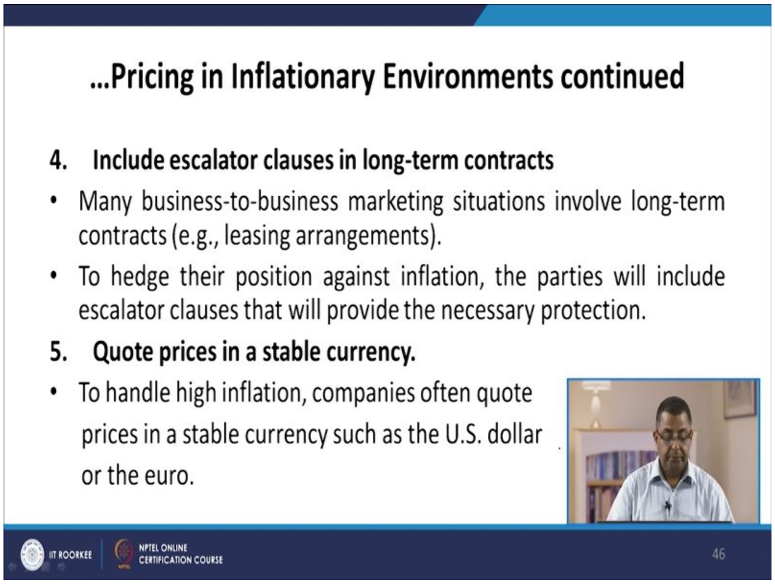

Including the escalator clause then there the company signs long term contracts. Many business to business marketing situations involved long term contracts that are leasing arrangements. To hedge their position against inflation, the parties will include escalator clauses that will provide the necessary protection. Another strategy is to quote prices in stable currencies. To handle high inflation, companies often quote prices in a stable currency such as the US dollar or the euro.

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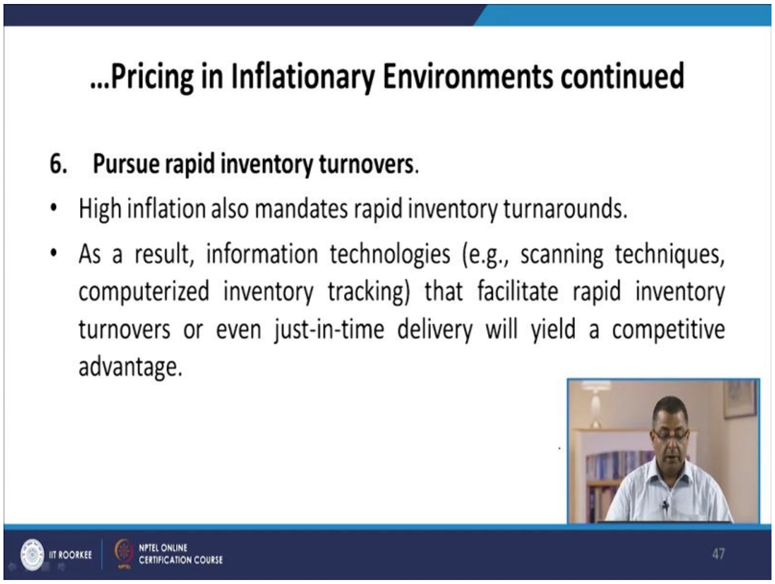

And then to pursue rapid inventory turnovers high inflation also mandates rapid inventory turnovers. The more the bigger that period is the more will be the cost. As a result, information technologies, that is, scanning technology techniques, computerized inventory tracking that facilitate rapid inventory turnover or even just in time delivery will yield a competitive advantage.

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And the last one is to draw lessons from other countries. Operations in other country with a long history of inflation offer valuable lessons for ventures in other high inflation countries. Some companies like McDonald's and Otis Elevator International have relied on expatriate managers from Latin America to cope with inflation in the former, in the former Soviet Union, because earlier the same kind of situation prevailed in Latin America and those managers they were, they had the knowledge of dealing inflation. So therefore they were, they were transferred to Soviet Union, so that they can take care of this problem.

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Now when there are price controls and to combat hyperinflation, governments occasionally impose price controls, for example, Brazil went through 5 price freezes over a 6 year interval. Such temporary price caps could be selective, targeting certain products, but, in extreme circumstances, they will apply across the board to all consumer goods. One consequence of the price control is that goods are diverted to the black market or smuggled overseas, leading to a shortages in the regular market. So when the when the when the when the distributor they are not getting enough profit so they go into hoarding and then they do not release product for the domestic market rather than they can they sell it overseas, smuggled to different countries.

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Now what are the alternative in this kind of situation, one is to adapt a product line, shift target market segments or markets, launch new product of variants of existing products, negotiate with the, with the governments and predict incidence of price controls. So what is meant by adapt a product line?

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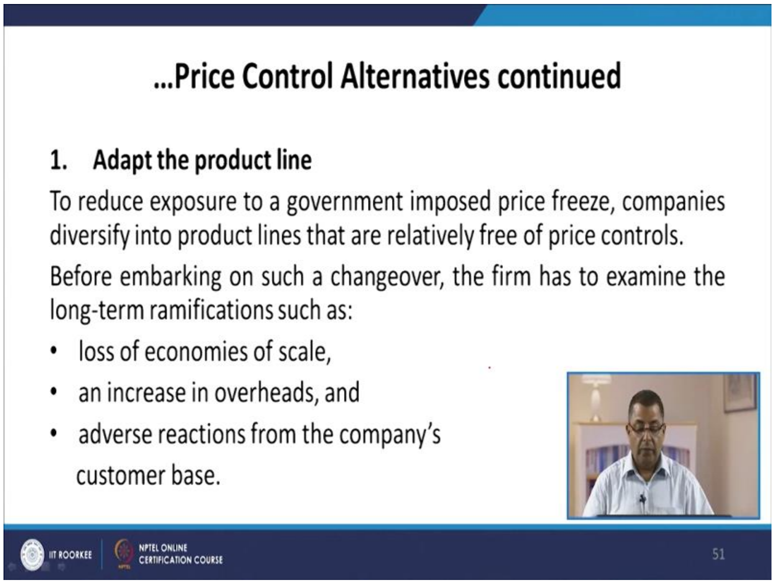

To reduce exposure to a government imposed price freeze, companies diversify into product lines that are relatively free of price controls. So they can be two different kind of soaps, one that comes under the price control order and the other that does not. So before embarking on change over the firm has to examine long-term ramifications such as, it will lead to loss of economies of scale, it will increase overheads and adverse reactions from the countries customer base.

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Another option available is to shift target segments or markets. For instance, price controls often apply to consumer food products but not to animal related products. So, a maker of corn based consumer products might consider a shift from bhaskare, breakfast cereals to chicken feed products.

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The third is to launch new products or variants of existing products. If price controls are selective, that is they do not apply across the board, a company can navigate around them, by systematically launching new products or modifying existing ones. So faced with this price controls in Zimbabwe, baker's added raisins to their dough and called it Raisin Bread, thereby at least momentarily, escaping the price control for bread.

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Yet another option available is to negotiate with the government. Firms can negotiate for permission to adjust their prices. Lobbying can be done individually, but is more likely to be successful on an industry wide basis. So they have Industry associations that can lobby with the government for that. The next is to predict incidence of price control. Some countries have a history of price freeze programs. Given historical information on the occurrence of price controls and other economic variables, econometric models can be constructed to forecast the likelihood of price controls.

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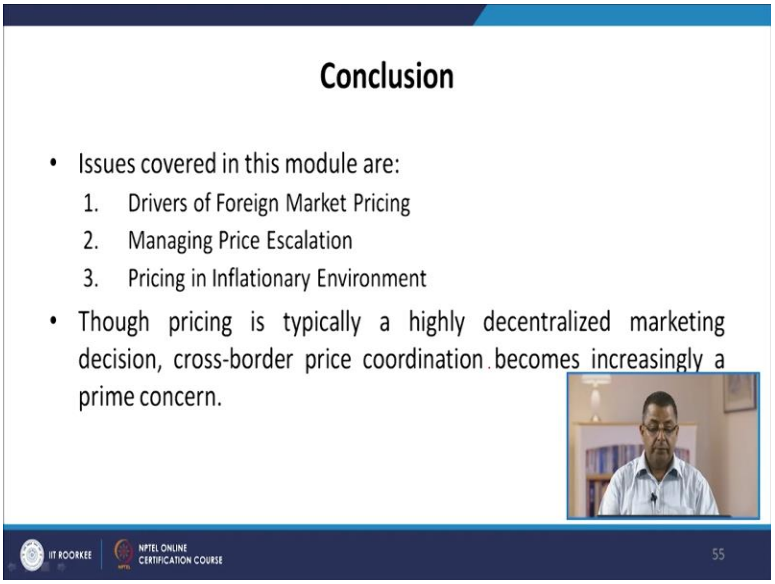

So to conclude, today we have talked about one is are the drivers of foreign market pricing, what are the factors that affect the pricing in different countries and therefore you will find that the MRP for the same product is different in different countries. How to manage price escalation so when a company exports, so because of the longer supply chain, more number of people coming into the process of making the product available to the customer. So therefore the price increases so how to go about managing them.

And the third is pricing in inflationary environment, in those environment, where prices keeps on changing very frequently, or the prices are prices keeps on increasing very frequently, therefore how to price in those kind of environment. Though pricing is typically a decentralized marketing decision, cross-border price coordination becomes increasingly a prime concern. So the prices have to be coordinated across borders, because if it is not and the difference is huge between the prices of the same product across borders, then obviously, parallel trade that is the gray market will come in.

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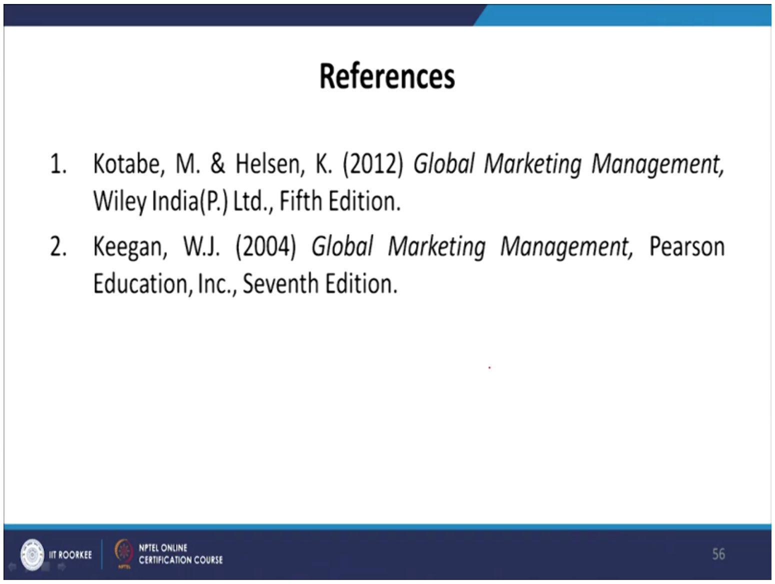

So these are the 2 books that can be used for further understanding of the concepts that are there in this module. Thank you.