Strategic Services Marketing

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Week – 08

Lecture - 36

Pricing Strategies for Services and Value-based Pricing

Hello everyone. As you know along with physical processes, people and physical evidence, price is also one of the most important factor or element of marketing mix when it comes to services. So, in this session let's explore pricing strategies for services and the importance of a value based pricing strategy. Before that what is pricing? Pricing refers to the process of determining the monetary value assigned to a product or service that a business offers to customers in exchange for goods or services. It involves setting a specific amount or range of prices that customers are willing to pay based on various factors such as production cost, competition, market demand, pursued value and profit objectives. Pricing involves more than just assigning a number to a product or service.

It is a strategic decision that can have significant implications for business success. The pricing strategy chosen by a company or service provider can influence it's revenue, profitability, market positioning, customer perceptions and overall competitiveness. There are various pricing strategies that businesses can utilize including cost based pricing, competition based pricing, value based pricing, dynamic pricing, skimming pricing, penetration pricing and psychological pricing. Each strategy has its own advantages, disadvantages and suitability depending on factors such as the nature of the product or service, target market and business objectives.

Ultimately, pricing is about finding the right balance between generating revenue and delivering value to your customers while also ensuring profitability and maintaining competitiveness in the market. It requires careful analysis, market research and strategic decision making to determine the optimal pricing approach for a business or service provider's offering. So what is services pricing then? Services pricing refers to the process of determining the monetary value assigned to the services provided by a business or individual. Unlike pricing tangible goods, pricing services can be more complex due to their intangible nature and the unique characteristics of service delivery.

So what are the factors that one should consider while pricing services? So let's discuss some service pricing that involves different factors that affect this particular decision.

The first factor here is of course costs. This includes direct costs associated with providing the service, for example labour, material, overhead as well as indirect costs, for example administrative expenses, marketing and so on. Second factor is market demand. Here it is important to understand the demand for the services within the target market and how customers perceive it's value relative to competitors' offerings. The third important factor is value preposition.

Value proposition means identifying the unique value proposition of the service and determining how much customers are willing to pay for it based on the benefits received. Another factor is competitive landscape. This involves analyzing pricing strategies of your competitors, offering similar services and positioning the service appropriately within the market. Another factor that influence services prices is customer segmentation. This means tailoring pricing to different customer segments based on their preferences, willingness to pay and even perceived value.

Another factor is brand reputation. Leveraging the reputation and brand image of the service provider to justify premium pricing or even differentiate from lower price competitors. So this brand reputation also influences prices of services. Then comes pricing models. This involves choosing the appropriate pricing model, for example hourly rates, project based fees or even subscription based pricing that aligns with the nature of the services and customer preferences.

And the last factor that influence services pricing is regulatory considerations. This means ensuring compliance and all those regulatory requirements to be fulfilled as a industry standards that are given by the regulators or government sometimes. So this also influences services pricing decisions. So why it is important? Why this particular pricing of strategies for services is important decision for an organization? The first reason is of course it influences revenue generation. Pricing directly impacts a service provider's revenue generation.

A well-designed pricing strategy can maximize revenue by ensuring that the price charge reflects the value delivered to the customers. Next important thing is with respect to profitability. Effective pricing strategies contribute to the profitability of the service business. By accurately assessing cost and aligning prices with perceived value, companies or service providers can maintain healthy profit margins. Third factor of influence is because of competitive positioning it offers.

Pricing strategies play a crucial role in positioning a service provider within the competitive landscape. As shown in this particular diagram, we can say the fast foods can be mapped across different dimensions, for example cost versus experience they offer. And all those service providers are placed appropriately in their respective quarters or kind of you know metrics positions. Strategy pricing can help differentiate offerings from competitors and attract target customers. Next importance is with respect to customer perceptions.

Pricing communicates value to customers and influences their perceptions of the service. By employing right pricing strategy, businesses can convey quality, exclusivity or even affordability depending on their positioning in the market. Another benefit is with respect to customer retention. Pricing strategies can impact customer retention and loyalty. Fair and transparent pricing builds trust with customers, encouraging repeat business and reducing churn rates.

Next benefit is with respect to market penetration. Pricing can be used as a tool to penetrate new markets or segments. Strategic pricing adjustment such as discounts or promotional pricing can attract new customers and stimulate demand. Another benefit is with respect to adaptation to market dynamics. Pricing strategies need to be flexible to adapt to changing market conditions, customer preferences and competitive pressures.

Regular evaluation and adjustment of pricing strategies are essential for long term success. Then what are the objectives of pricing in general? So in general objectives of pricing may be of four types. First survival of course then expansion of current profits, ruling the market and then a market for an innovative idea. Survival, the objective of pricing for any company or service provider is to fix a price that is reasonable for the consumers and also for the producer to survive in the market. Therefore, while determining the cost of product or services all the variables and fixed costs should be taken into consideration.

Once the survival phase is over the company can strive for extra profits. Second objective is with respect to expansion of current profits. Companies tries to enlarge their profit margins by evaluating the demand and supply of services and goods. So the pricing is fixed according to the services demand and the substitute for the particular product or service. Third objective is ruling the market.

Firms impose low figure for the goods and services to get hold of large market size. The technique helps to increase the sale by increasing the demand and leading to low production cost. And a final objective can be to get a market for an innovative idea. The company charges high prices for their product and services that are highly innovative and use cutting edge technology. The price is high because of high production cost.

Mobile phone, electronic gadgets are a few examples of this type of objective pricing. So what are the objectives for services pricing? There are mainly three objectives. First gain profits and cover cost, build demand and develop a user base and third support positioning strategy. Let's discuss these one by one.

First is gaining profit. It's important to make the largest possible long term contribution or profit or the objective can be to achieve a specific target level but do not seek to maximise profit. Also it may be possible to go for maximising revenue from a fixed capacity by varying prices and target customers over time. Second part of this is covering costs. The objective can be to cover fully allocated cost including corporate overhead etc. Secondly cover cost of providing one particular service excluding overheads or cover incremental cost of selling one extra unit or serving one extra customer.

Any of these can be applicable. Second objective deals with building demand and developing a user base. With respect to building demand, objective can be to maximise demand when capacity is not restriction provided a certain minimum level of revenue is achieved or achieve full capacity utilisation especially when high capacity utilisation add to the value created for all customers. For example, houseful shows.

Then developing a user base. Encourage trial or adoption of a service. For example, for new services with high infrastructure cost and for membership type services, this is a go to objective. Second objective can be to build market share and or even large user base. What does Facebook and LinkedIn were doing is to achieve this market share first. Third objective for services pricing includes supporting positioning strategy.

The objective can be to help and support the firm's overall positioning and differentiation strategy. For example, as a price leader or as a premium quality provider which can be reflected through the prices attached to those services. Moreover, some firms can also go for promoting themselves as we will not be under sold positioning whereby a firm promises the best possible service at the best possible price. Moreover, services pricing also supports some competitive strategy decisions as well. For example, they discourage existing competitors from expanding their capacity whereas sometimes pricing can also discourage potential new competitors from entering into the market.

With that, now let's discuss some key criteria that should be considered while going for services pricing. Firm needs to answer some of the questions that can guide them in terms of deciding pricing for their services. The first question falls under the larger umbrella of how much should be charged for the services. This includes many questions under it. For example, what cost is the organization attempting to recover? Is the organization trying to achieve a specific profit margin or return on investment by selling this service? Second question can be how sensitive are customers to various prices? Third, what prices are charged by competitors? Fourth, what discount or discount should be offered from basic prices? Then are psychological pricing points, for example, 4.

95 versus 5, customarily used in this particular industry and market? And should auctions and dynamic pricing be used? Then the second set of questions a service firm should try to address is with respect to what should be the basis of pricing. This includes answers to the questions or information like execution of a specific task, is it going to form the base of pricing or admission to a service facility or units of time, for example, hours, week, month or year, for how long the service is available and based on that pricing will be decided. Physical resources consumed during the particular service or geographic distance covered or weight or size of the object service, for example, in terms of transportation and logistic industry or should each service element be built independently or should a single price be charged for a bundle package. So, all these questions are also important to arrive at a pricing for particular services. Then third set of questions address how should prices be communicated to the target market, for example, whether we are going to do this through which communication platform or medium, for example, advertising, signage, electronic, display, salespeople or even our own customer service personnel or what message or content should be placed in those media or medium and can the psychology of pricing presentation and communication be used in this context.

So, multiple factors are important while understanding what kind of pricing will work in which context based on type of services served, the market practices and even competitors. With this, let's move on to the next important concept like what are the different pricing strategies available for service firms. There are basically a lot of them, but let's discuss nine of these which are prominently present across service industries. These are competition based pricing, cost plus pricing, dynamic pricing, high low pricing, penetration pricing, skimming pricing, value based pricing, psychological pricing and geographic pricing.

Let's discuss these one by one. First here is competition based pricing. In competition based pricing wherein it is pricing strategy that uses the competitors prices as a benchmark. In such a situation, firm with lower per unit of services enjoys an enviable market advantage and often assume price leadership. For example, as shown in this particular image that shows the rates across Uber and Lyft that how much do they cost for a particular customer.

Second type is cost plus pricing. A cost plus pricing strategy focuses solely on the cost of producing your product or services or your cost of goods sold which is known as COGS. It's also known as markup pricing since businesses who use this strategy markup their products based on how much they would like to profit. For example, Costco, a retail chain have different club memberships, Gold, Goldstar, Business or even Business Exitives and you can notice the differences in terms of prices. Then comes dynamic pricing. Dynamic pricing is also known as surge pricing or demand pricing or even time based pricing.

It’s a flexible pricing strategy where price fluctuates based on market and customer demand. This image showcase how airline practices dynamic prices. You can notice that some prices are different across two different times. For example, New Year's weekend and exactly one week after that particular New Year.

Then comes high low pricing. A high low pricing strategy is when a company initially sells a product at a high price but lowers that price when the product drops in novelty or relevance. For example, discounts, clearance sections and year end sells are examples of this kind of pricing. Then comes penetration pricing. When companies enter the market with an extremely low price effectively drawing attention and revenue away from higher end price competitors as exactly captured in this image where Netflix adopted this penetration pricing. So, they started with a lower prices and slowly they go on increasing the prices over a period of time.

Then comes skimming pricing. A skimming pricing strategy is when companies charge the highest possible price for a new product and then lower the prices over time as the product becomes less and less popular. This is exactly opposite of penetration pricing. So, we start with charging higher prices initially right and then just move on to the right side lowering the prices to gain more market in the particular market industry. Then comes value based pricing. In value based pricing, it is a balancing act between quality and price.

High end resorts and hotels usually sell their buffet, lunch and dinner items using this value based pricing method. Then comes psychological pricing. A psychological pricing is what it sounds like it targets human psychology to boost yourselves. Another way to use psychological pricing would be to place a more expensive item directly next to the one you are most focused on selling. For example, what does is instead of pricing it at $10, let us price it for $9.

99. So, this again a psychology at place then, as captured with this particular screenshot, Amazon Prime membership based on 30-day free trial and then monthly, 3-month subscription and yearly subscription and you notice the price changes across these particular offerings. So, this is again something is an example of psychological pricing at place. And finally, we have geographic pricing. A geographic pricing is when products or services are priced differently depending on geographical location or market. For example, East versus West states in US different pricing adopted by particular service firm.

So, there are lot of pricing strategies, but again there are lot of pricing models as well. For example, just to discuss few of them there might be premium model, premium pricing model, hourly pricing, bundle pricing, project based pricing and subscription pricing. In premium pricing, it's a combination of the words free and premium. Premium pricing is when companies offer a basic version of their product hoping that users will eventually pay to upgrade to or even access more features of the same product.

So, that is a free plus premium. Then comes premium pricing also known as prestige pricing or even luxury pricing. A premium pricing model is when companies price their products high to present the image that their product are high value, luxury or even premium. Then comes hourly pricing also known as rate based pricing which is commonly used by consultants, freelancers, contractors and other service providing individuals or labourers who provide business services. Then comes bundle pricing is when you offer two or more complementary products or services together and sell them for a single price. So, you may choose to sell your bundle product or service only as a part of a bundle or sell them as both components of bundles and individual products as well.

Then comes project based pricing is the opposite of hourly pricing. This approach charges a flat fee per project instead of a direct exchange of money for time. It is also used by consultants, freelancers, contractors and other individuals or labourers who provide business services. And then comes subscription pricing. Subscription pricing is a common pricing model at SaaS companies, online retailers and even agencies who offer subscription packages for their services.

For example, Amazon Prime, Netflix and so on. Whether you offer flat rate subscriptions or tiered subscriptions the benefits of this models are endless. Now let's discuss how to design pricing strategy. So, it is a five stage process. So, the first stage here is evaluating pricing potential. This is to make a strategy that is optimal for your unique business.

It's important to evaluate your pricing potential. There are many factors that affect pricing potential which includes geographical market specifics, operating costs, inventories, demand, fluctuations, competitive advantages and even concerns and demographic data. Then comes second stage determining your buyer persona. Price your service on the type of buyer persona that is looking for it. When you look at ideal customer you will have to look at their customer lifetime value, willingness to pay and pain points.

Third stage deals with analyzing historical data. Look at your previous strategies specific to pricing. Calculate the difference in close deals, churn data or even sold product on different pricing strategies that your business has worked with before and look at which were the most successful price points. Next stage is strike a balance between value and business goals. Make sure the price is good to your bottom line and your buyer personas. This compromise will better help your business and customer pool with the intentions of increasing profitability, improving cash flow, market penetration, expanding market share and increasing lead conversion.

And finally, look at your competitors, what the pricing they are using. You can't make a pricing strategy without conducting research on your competitors offering. Decide between two main choices when you see the price difference for your same product or service. First do you want to beat your competitors price? If a competitor is charging more for the same offering as your brand then make the price more affordable. Second option for you is to go for beating your competitors in terms of value.

For example price you are offering higher than your competitors if the value provided to the customer is greater. Now let's move on to the next set of concept which is value based pricing strategy. One of the pricing strategies that we have looked at. Value based pricing strategy also known as value added pricing or value pricing is a method of setting the prices based on your customers and how they perceive the value of your product. To show it in a chart we can see here is the cost of providing those services.

This is the markup that you want to contain or achieve just to be profitable and then this is the zone where customers are actually perceiving the value of your product or services. So, this is nothing, but your value based pricing. So, it allows you an extra margin above and beyond your cost plus kind of you know pricing. So, for example, a famous painting or a meal at fine dining restaurant might come with a higher price tag. Why? Isn't because the materials used to create the art or food were costly.

It's because consumers believe the final product and experience attached to it to be worth a lot and that is why value based pricing is most important. To understand this particular term in better that how to price a product and how value based pricing can be applied have a look at this particular video that explains more about this particular concept. Pricing is a sacred act of capitalism. There's a math part to pricing, but the judgment part is much more interesting.

You might have been taught that price is your cost plus a margin. Now, it's really tempting to think that way, but I think it's better if you consider price as the value to your customer minus an incentive to buy. Let me explain. Robert Dolan teaches marketing at the Harvard Business School. I think the very best thing he ever did was to describe a value based approach to pricing. Dolan ask's us to imagine a world where the cost to produce our product is somewhere greater than zero.

It seems perfectly reasonable. Price should be set somewhere above cost. Also not a crazy idea. Now, that gap matters a lot. It's the gross margin or the incentive to sell. You don't actually have a business without it.

For Dolan, a different gap matters much more. It's the gap between price and perceived value. He called that gap the incentive to buy, and it entirely explains why a customer decides to buy or not to buy our product. In Dolan's model, perceived value comes from a lot of the same intuitive and rational considerations that Kahneman and Tversky described in their work. Marketing's job is to make the gap between perceived value and price as large as possible. If you're selling a product like crazy, your customer must perceive a huge gap between value and price.

Not selling anything. That's an incentive to buy problem. And you don't fix that by lowering price. That's a cop-out and a one-way ticket to reducing value for your customer. Try raising perceived value instead.

Add features to your product. Create tiered assortments. Good, better, best. And improve the product marketing. Perceived value, after all, is a stew of intuition, rational analytics, and aversion to loss. Thank you, Robert Dolan. You really saved us from… So value-based pricing in services is a pricing strategy where the price of service is determined by the perceived value it provides to the customer, rather than cost of production or the prices of competitors. This approach is grounded in the idea that customers are willing to pay based on the perceived benefits and outcomes they are receiving from that particular service.

Then there are some advantages of going for value-based pricing strategy. This involves increased profits, attracting and retaining better clients, differentiation from competitors, and improved customer relationship. Increased profits. Value-based pricing can significantly boost profits for services in several ways. By pricing their services based on the perceived value to the client or customer, rather than just the cost, consulting firms can often command higher rates. This shift in pricing strategy can lead to increased revenue streams and ultimately higher profits.

Second advantage is with respect to attracting and retaining better clients. Value-based pricing in consulting services, for that matter, can be instrumental in attracting and keeping higher quality and higher value clients. By pricing services based on the specific value-based deliverables, consulting firms can more clearly demonstrate the direct link between the benefits and outcomes clients are expecting. Third benefit or advantage is with respect to differentiation from competitors. Value-based pricing provides a powerful means of differentiation from competitors in the professional services industry, for example consulting a game. By placing emphasis on the unique needs and requirements of each individual customer, businesses can position themselves as providers of customized, high-value solutions, etc.

Clients are increasingly seeking personalized, tailored solutions and value-based pricing demonstrates a commitment to meeting those individualized needs. Another benefit is improved customer relationship. Value-based pricing forms the cornerstone of improved customer relationships in the professional services. When businesses align their pricing with the unique value they offer, it creates a foundation of trust and transparency. This in turn leads to stronger, more enduring client and even partnerships with those particular customers.

At the same time, there are some disadvantages of opting for value-based pricing strategy. These are difficulty in perceived value, vulnerability to competition and potential customer alienation. difficulty in determining perceived value. Estimating the perceived value of product or service can be challenging as it involves understanding customer preferences and perceptions, which may vary across different customer segments.

The second disadvantage is with respect to vulnerability to competition. If a competitor offers a similar product or service at a lower price, customers may perceive the competitor's offering as a better value and potentially leading to lost sales and market share for you. Third disadvantage is with respect to potential customer alienation. If customers feel that the price is too high relative to the value they perceive, they may become dissatisfied and switch to a competitor. It’s essential to strike the right balance between price and perceived value to avoid alienating customers.

With that, let’s understand the stages or steps to implement value-based pricing strategy. There are four stages for this.

Step 1. Identify your target customers. Step 2. Understand their needs and pain points. Step 3. Quantify the value of your services. And finally, Step 4. Communicate the value of your services to your customers. Let’s discuss one by one. First step is identifying your target customers and their needs. Identifying your target customers is a fundamental yet crucial step in implementing value-based pricing for professional services. This involves utilizing market research, conducting surveys, or even engaging in direct conversation to discern the true value your services can provide to them.

Step 2. Deals with understanding their needs and pain points. It’s imperative to have a deep understanding of your customers' needs and pain points. Start by asking yourself crucial questions like, what specific challenges do my customers experience? What solutions are they actually seeking and what outcomes do they hope to achieve? By delving into these inquiries, you gain valuable insights that allow you to tailor your services to offer the most impactful solutions. Step 3. Quantifying the value of your services. Here, it involves assigning a tangible, measurable value to the outcomes and benefits your service delivers to the clients or customers.

Begin by considering the specific improvements or advantages that your expertise bring to the particular business or client. This could encompass factors like increased revenue, cost savings, enhanced efficiency, or even strategic insights for your clients. And the fourth step involves communicating the value of your service to your customers. Here it is essential to clearly articulate how your expertise will directly benefit your customers or clients. One powerful way to achieve this is through the use of case studies, which provide concrete examples of the positive impact your services have had on past clients.

So to conclude, in this session, we try to understand pricing, services pricing, and different pricing strategies, including value-based pricing strategy that can be used for pricing services. Thank you.