

## Pricing in the Internet Age

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## Pricing Concepts

- ◆ The 3C's of pricing in order of importance are
  - Customer Value
  - Competitor's pricing
  - Your costs
- ◆ Other pricing issues
  - Direct versus indirect payment

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## Customer Value Issues

- ◆ Different consumers value a product differently
  - Price = Value is the objective
  - Sell at different prices, if possible
- ◆ What is the problem one faces in doing the above?
- ◆ Only variable costs matter when determining a price floor

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## Customer Value Issues

- ◆ Product bundling
  - With digital products, bundling makes sense in a majority of cases
  - With physical products, the variable costs of producing the product & customer value determines whether bundling makes sense

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## Customer Value Issues

- ◆ “The Internet leads us towards markets for products & services”
  - Implies?
- ◆ The increased use of auctions as a substitute for managerially determined prices
- ◆ Auctions & reverse auctions
  - Bidding for goods & services
  - Favors which party?

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## Customer Value Issues

- ◆ Types of Auctions
  - English auction -- artwork, etc.
  - Dutch auction -- flowers
  - Offer auction -- sellers make offers
  - Bid auction -- buyers bid
  - Clearinghouse auction -- buyers bid and sellers make offers
  - etc.

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## Customer Value Issues

- ◆ Differentiation across customers -- what do we know about digital products?
  - Free versions can generate demand for "pay" products
  - Multiple versions are a must, even if extra costs are incurred
  - The exponential rule ( $N^2$ )
  - etc.

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## Competitor's Pricing Issues

- ◆ Competitor's prices are constraints on your pricing options -- they greatly restrict what you can do.
- ◆ Differentiation is the answer. How does one differentiate digital products?
  - Features, display, time, etc.
- ◆ Can the Internet be used to help differentiate your products?

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## Your Cost Issues

- ◆ Must understand cost structure of your products & services
  - The ratio of variable to fixed costs is key
  - The magnitude of variable costs also can be important
- ◆ Affected by the type of product
  - Perishable products
  - low or zero variable costs
  - high variable/fixed costs

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## Other Pricing Issues

- ◆ Who is the customer?
  - If you are YAHOO?
  - If you are Priceline?
- ◆ Free stuff on the Internet
- ◆ Earning money on the web (to surf) for example
- ◆ Yield management and other priority capacity pricing systems

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## Other Pricing Issues

- ◆ Direct versus indirect prices
  - Out-of-pocket costs for the customer
  - Indirect costs to the customer
    - targeted advertising
    - queuing delay
    - search costs
    - other indirect costs?
- ◆ Relationship between type of customer and the “Direct versus indirect price” tradeoff

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## Summary

- ◆ We have discussed a number of issues related to pricing in the information age
- ◆ An additional thought
  - Production decisions affect costs and costs affect pricing decisions in the long run (cannot continue variable cost pricing forever). What affect should this have on pricing options that are available?

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