

3

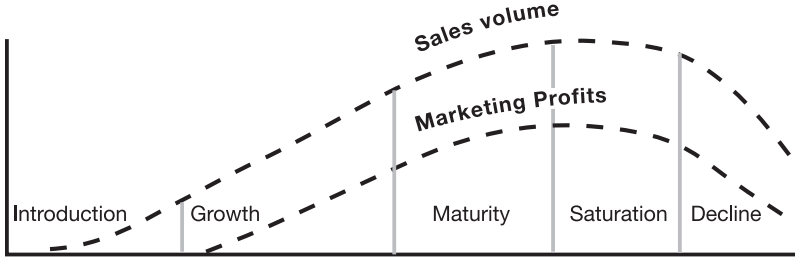
Product and Price

Look at the learning patterns for the chapter before and after studying each set.



A Product planning

C Market segmentation



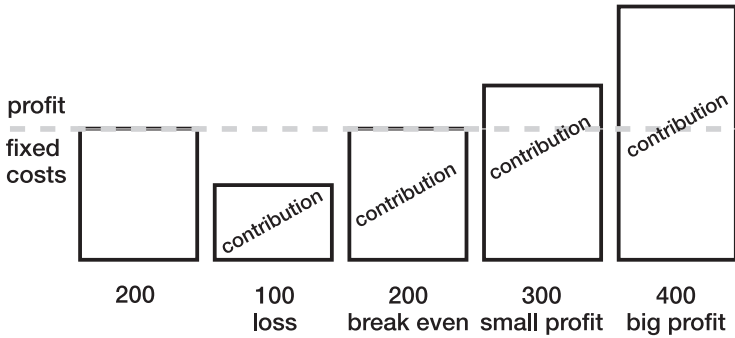
B Product life-cycle



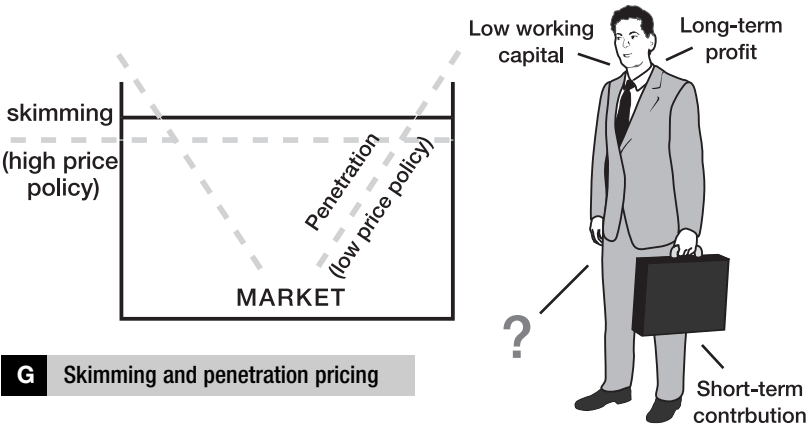
D Product Differentiation



E Product Diversification

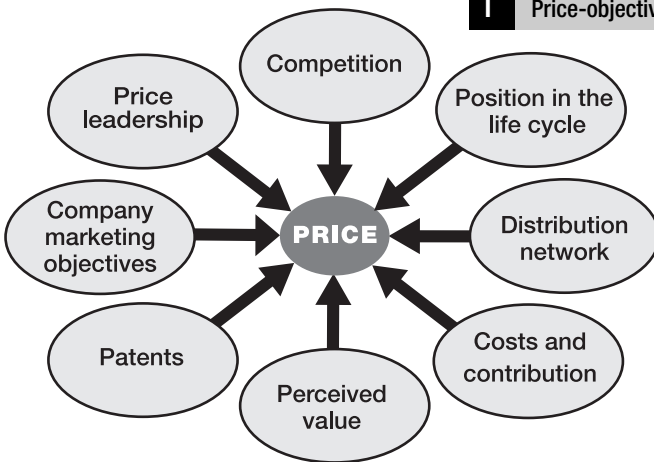


F Contribution towards fixed cost and profit not per unit but total



G Skimming and penetration pricing

I Price-objective conflicts



H Determinants of pricing policy

LU 3.1 Product Management and Policy

Estimated time: 10 minutes

Key Learning Points

A sound product policy is essential to business survival and its growth. It should cover the following: production, personnel, finance, industrial relations, marketing systems, general management as well as the all-important marketing function.

Products are key assets of the business and therefore must be continually improved, developed, and in due course, replaced.

Product planning is a competitive tool, which requires an understanding of consumer needs and market trends in an ever-changing environment.

Product policy must relate to consumer needs and market potential. It must be creative, constantly reappraised, planned and always focused on new developments.

LU 3.1 Detailed Exercises

Correct answers

1. "When an arrow is loosed from the bow it may go straight or it may not, according to what the archer does. How strange, therefore, that but when it goes out of true, it is the arrow which is blamed" (Sufi). This is the same with new products. Sound, bold products and policy are essential to a firm's ... and

SURVIVAL/GROWTH

Correct answers

- | | |
|-----------------------------------------------------------------------------------------------------------------------------------------------------|-----------------|
| 2. A good product policy is concerned not only with the short-term, but also with the-term survival of the firm. | LONG |
| 3. An integrated product policy must be concerned with all the functions of the firm, but most of all with | MARKETING |
| 4. Development of new products demands systematic planning. | PRODUCT |
| 5. Product planning will have considerable influence on the volume of sales and so on the of the firm. | PROFITS |
| 6. Product planning must be constantly adapted to the changing environment, and so calls for up-to-date knowledge of consumer and trends. | NEEDS
MARKET |
| 7. Product planning is an important competitive tool, and the key word in this statement is | COMPETITIVE |
| 8. In the face of competition, a well-planned product policy is essential to ensure a stream of new products to seize opportunities. | MARKET |
| 9. Imaginative product planning calls for a real understanding of consumer motivation, both rational and | EMOTIONAL |
| 10. Sound product policy focuses upon known or forecast consumer | NEEDS |
| 11. Products are part of the assets of a firm, and must be managed boldly, but as carefully as other | ASSETS |

Correct answers

12. Product policy must be consistent with the realities of the market and the research and production of the firm.

POTENTIAL

13. What is really important for sound product policy?
(a) creativity (b) continual appraisal (c) sufficient quantification (d) bold risk-taking (e) advance planning (f) concern with new products (g) all of the above

(g)

14. All products should be (a) improved (b) developed (c) left alone (d) replaced

(b)

LU 3.2 Product Life-cycle

Estimated time: 15 minutes

Key Learning Points

In a continually changing marketing environment, with continually changing consumer needs, our products move through a five-phase cycle:

- a) introduction
- b) growth
- c) maturity
- d) saturation
- e) decline.

Changing consumer needs and product obsolescence require systematic “*forward* planning” and sound product policy. This will involve:

- a) market segmentation

- b) product differentiation
- c) product simplification
- d) product diversification
- e) planned obsolescence.

KEY NOTE:

Study the Key Learning Points and Visual Learning Diagrams at the beginning of the LU, complete the exercise, and then study them again.

**LU 3.2 Detailed Exercises****Correct answers**

- | | |
|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------|
| 1. There will always be a strong market for some products, like saddles, because there will always be horses. (True/False). | TRUE ... but ...? |
| 2. Just like people, products have a life-cycle, and they move through it in natural relation to constantly changing consumer and marketing environment. | NEEDS |
| 3. Introduction, growth, maturity, saturation, and decline are the five phases of a product -cycle. | LIFE |
| 4. If in the <i>introductory</i> phase of the product life-cycle the sales volume is not sufficient to cover development costs, even when there are no competitors, such a product should be (promoted/dropped). | PROMOTED |
| 5. Promoting a new product calls for strong concern to reach the target market through the stimulation of needs of the | CONSUMER |

Correct answers

- | | |
|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------|
| <p>6. In the <i>growth</i> phase of the product life-cycle, sales increase considerably, and the product produces (satisfaction/profits).</p> | <p>PROFITS</p> |
| <p>7. In the <i>growth</i> phase of the life of a product, which of the following will need special attention?
 a) competitors
 b) promotion of the brand name
 c) rising costs
 d) matching of production levels with demand</p> | <p>(a), (b), (d)</p> |
| <p>8. In the <i>maturity</i> phase of a product life-cycle, sales rise more slowly, due to increased</p> | <p>COMPETITION</p> |
| <p>9. Product differentiation tends to decrease as competition increases. Strong competition will lead to (more/less) differentiation between products.</p> | <p>LESS</p> |
| <p>10. In the <i>maturity</i> phase of a product life-cycle, more intensive marketing may reduce profits, but this can be overcome by finding new</p> | <p>MARKETS</p> |
| <p>11. The final phase in the life-cycle of the product is its <i>saturation and decline</i>. At this stage, emphasis is on optimizing returns and controlling</p> | <p>COSTS</p> |
| <p>12. Which of the following identify specifically the saturation-and-decline phase in the life of a product?
 a. negligible product difference between competitors
 b. eventual abandonment of the product
 c. distribution of the product to all possible outlets
 d. matching supply with demand
 e. hardening of the arteries</p> | <p>(a), (b), (c)</p> |

Correct answers	
13. The life-history of a product is called the -cycle. Is this cycle inevitable with all products?	PRODUCT LIFE YES
14. Consumer needs change, and all products become obsolete in time. A firm must therefore have a continuing flow of new	PRODUCTS
15. We must remember that if we invent and make a much better mousetrap, the public will eventually beat a path to our door. (True/False)?	TRUE (but we may be dead)
16. For a new product to be the pattern a structure of the particular market must be known.	TARGET
17. Remember, products don't just happen; preparation for the emergence of a new product involves a series of steps. What is the proper order for these? a) full-scale production and marketing b) consumer research c) soliciting of ideas d) market testing and test-marketing e) development of a feasible product f) expansion of ideas into product specifications	(b), (c), (f), (e), (d), (a)
18. New products often fail because of inadequate planning and inadequate introduction of the product to the market. Failure is inevitable if consumer are ignored and the product is poorly (designed/promoted).	NEEDS / PROMOTED
19. A product can fail if its conception is too (simple/sophisticated).	SOPHISTICATED
20. When products are 'directed' towards special individual markets, there is segmentation.	MARKET

Correct answers

- | | |
|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------|
| <p>21. Market segmentation creates market segments made up of different types of consumer. Here we must differentiate not between products but between</p> | <p>CONSUMER</p> |
| <p>22. Which of the following are market segments expressed in terms of consumer type?
 (a) individuals (b) consumer markets
 (c) families (d) institutions
 (e) psychopaths (f) income groups</p> | <p>c d f</p> |
| <p>23. By contrast, product differentiation emphasizes the difference between our and the similar products of our</p> | <p>PRODUCT
COMPETITION</p> |
| <p>24. When a firm produces many products, it may simplify its range by some products.</p> | <p>ELIMINATING</p> |
| <p>25. A critical appraisal of sales, profits, markets, consumers, production, and competition should lead to the elimination of products.</p> | <p>WEAK</p> |
| <p>26. Product diversification by exploitation of our financial resources can lead to which of the following? (a) satisfaction of new consumer, (b) increase in sales and (c) taking risks to get an advantage.</p> | <p>(a), (b), (c)</p> |
| <p>27. Planned product obsolescence determines the term of usefulness of the product, i.e. when it will be</p> | <p>ELIMINATED</p> |
| <p>28. Eliminating weak products is product simplification. Development of new products is product Determining the end of a product is product Making a product different is product And all of these are part of product policy and relate to a changing market environment.</p> | <p>DEVELOPMENT
OBSOLESCENCE
DIFFERENTIATION</p> |

Correct answers

29. If we expand from foods into machine tools and cosmetics, we are (diversifying/crazy).

DIVERSIFYING

30. Planned obsolescence occurs (during/after) the product life-cycle.

DURING

Now take another look at the summary for this LU before you look at your marks. Less than twenty-four right? Better look at this LU again. If you did better than this, push on to LU 3.3 after another quick look at the VLD for this chapter.

LU 3.3 Major Determinants of Price

Estimated time: 15 minutes

Key Learning Points

Relate price to customer value — received and perceived. Price indicates the company's intended value positioning of its products and brand. Pricing decisions involve consideration of:

- Market segmentation
- Market positioning
- Value propositions
- Other marketing mix elements.

Relate price to the company's marketing objectives because pricing decisions involve market share, competitive reaction, price leadership, market leadership and they influence working capital, required contribution and profit. Costs of production set the minimum selling price of a product, but only relevant costs to the pricing decision.

Pricing is based on product quality strategies such as charging a premium price for a high quality product, charging a medium price for a medium quality product, and charging an economy price for a low quality product. This assumes that there are three types of buyers: high quality conscious buyers, average quality buyers, and price conscious buyers.

You can target each of these three buyers, with different versions of your product such as stripped-down versions for price sensitive customers and thereby charging a lower price.

Costs can be divided into fixed costs and variable costs.

Fixed costs (overheads) include salaries, rent, insurance, maintenance of premises and equipment, taxes, and interest on capital. Total fixed costs are not affected by an increase in production volume (up to the total maximum production capacity the firm can achieve without plant expansion). Unit fixed cost decreases with increase in production volume.

Variable costs include the cost of raw materials and labor directly involved in the manufacturing process. Total variable costs increase with increased volume. Unit variable cost is constant despite changes in production volume.

Profit = selling price – costs (fixed and variable).

Contribution is defined as selling price less variable costs. Since unit selling price and unit variable cost are constant despite changes in production volume, unit contribution is also constant. However, total contribution, which is made up of all the individual unit contributions, will increase with increased volume and decrease with decreased volume.

Contribution is a contribution to fixed costs and profit, so:

profit = contribution less fixed costs.

For profit, unit contribution must be positive (i.e. unit selling price must be greater than unit variable cost), and total contribution must be greater than total fixed costs.

Major Determinants of Price

EXHIBIT 1

		<i>Product A</i>
Unit selling price	2.00	
<i>Less:</i> Unit variable cost	0.68	1.98
Unit fixed cost	1.30	
Profit	0.02	
Contribution	?	

EXHIBIT 2

		<i>Product Z</i>
Selling price		0.50
<i>Less:</i> Variable cost		0.68
Contribution (positive or negative?)		?

EXHIBIT 3

<i>Volume</i>	<i>Unit selling price</i>	<i>Unit variable cost</i>	<i>Unit contribution</i>	<i>Total contribution</i>
100,000	2.00	0.68	?	?
150,000	2.00	0.68	?	?

EXHIBIT 4

Volume	1,000	10,000
Unit selling price	2.00	2.00
Unit variable cost	0.68	?
Unit contribution	?	?
Total contribution	1,320	13,200
Total fixed costs	2,000	2,000
Total profit	?	?

LU 3.3 Detailed Exercises

Correct answers

- | | |
|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------|
| <p>1. How are you doing? Take a deep breath and grit your teeth. Did you study the learning-patterns again? Right. Now we discuss pricing policy. The basic aim of pricing policy is maximum long-term profitability. is dependent on profitability.</p> | <p>SURVIVAL</p> |
| <p>2. Specifically, pricing policy may be directed towards maintaining or improving market share, obtaining a target return on investment, pricing to meet or follow competition, or pricing to discourage entry of potential competition. The basic aim is maximum long-term</p> | <p>PROFITABILITY</p> |
| <p>3. Costs are an important factor in pricing policy, but we must determine which are relevant to decisions.</p> | <p>COSTS/PRICING</p> |
| <p>4. Costs can be divided into fixed costs and costs.</p> | <p>VARIABLE</p> |
| <p>5. Total fixed costs (overheads) do not change with volume of production. But when we consider these total fixed costs spread over all the production units, fixed cost per unit (increases/decreases) ... with increased production volume.</p> | <p>DECREASES</p> |
| <p>6. Total cost does not change with changes in the production volume of a given product, but fixed cost per unit decreases with (increased/decreased) production volume.</p> | <p>INCREASED</p> |
| <p>7. Variable costs are the same for each unit of product. The greater the number of units, the (greater/smaller) the total variable costs, but the share of variable costs per unit remains constant. They are thus always relevant to... ..</p> | <p>GREATER
PRICING POLICY</p> |

Correct answers

- | | |
|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------|
| 8. Contribution = selling price less variable costs. Since selling price per unit and variable costs per unit remain constant despite changes in volume, <i>unit contribution</i> also remains constant with changes in | VOLUME |
| 9. If selling price is greater than variable costs, contribution will be positive. If selling price is less than variable costs, contribution will be | NEGATIVE |
| 10. Contribution = selling price less variable costs. For profit, contribution must be (positive/negative). | POSITIVE |
| 11. Unit contribution remains constant with changes in volume. Total contribution with increase in volume. | INCREASES |
| 12. Unit contribution (changes/does not change) with change in volume. Total contribution (changes/does not change). | DOES NOT CHANGE |
| 13. For profit, contribution must be
Getting on all right? | POSITIVE
(YES !) |
| 14. In pricing policy, we must ensure that unit selling price is greater than unit variable | COST |
| 15. Profit = contribution less fixed costs. Unit fixed cost decreases as production volume
(increases/decreases) | INCREASES |
| 16. For profit, total contribution must be greater than total fixed ... | COSTS |
| 17. For profit, pricing policy must ensure that contribution is (b) total contribution is greater than total fixed | POSITIVE
COSTS |

Correct answers

- | | |
|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------|
| <p>18. However, pricing policy objectives include not only contribution and long-term profit, but also share, competitive reaction, and leadership. Price must balance these conflicting objectives (True/False).</p> | <p>MARKET
PRICE
TRUE</p> |
| <p>19. Marketing objectives determine the marketing mix, which consists of Product, Place, and</p> | <p>PRICE
PROMOTION</p> |
| <p>20. The marketing mix establishes what should be emphasized in marketing strategy. Thus, by specifying the role of price in strategy, marketing objectives exert influence on decisions.</p> | <p>PRICING</p> |
| <p>21. Price communicates to the market the company's intended ... positioning.</p> | <p>VALUE</p> |
| <p>22. Price must be in conjunction with the marketing</p> | <p>MIX</p> |
| <p>23. is the easiest marketing mix variable to adjust.</p> | <p>PRICE</p> |
| <p>24. A firm must determine its position based on quality and</p> | <p>PRICE</p> |
| <p>25. A company must set its price based on value ...</p> | <p>RECEIVED</p> |

But it is commonly a little price sensitive! Now read the summary again for this LU, and let's look at your marks. If you got twenty-one or more right, you're doing fine. Review the learning-patterns quickly before tackling LU 3.4 with vigor and enthusiasm. You're more than half-way through now. If you didn't answer twenty-one questions correctly, don't be despondent. This was a tough section. Take a coffeekbreak and then try it again.

LU 3.4 Pricing Policy

Estimated time: 20 minutes

Key Learning Points

Pricing depends mainly on what the market will pay, but it also depends upon:

- a) leadership
- b) competition
- c) the position in the product life-cycle
- d) the length of the life-cycle
- e) the distribution network
- f) costs and contribution
- g) the patent position
- h) company marketing objectives.

Important determinants of price are costs, the state of the market, the contribution concept, marketing objectives, geographical conditions, and government and legal regulations.

In effective pricing, we seek primarily contribution rather than profit. Total contribution depends upon volume, selling price, and variable costs. A high contribution is possible at different volumes.

Skimming pricing is a high-price policy for introduction of a new product to get the largest possible recovery of new-product investment.

Penetration pricing is a low-price strategy designed to gain as much of the potential market as possible within a short time after the introduction of a new product.

LU 3.4 Detailed Exercises

Correct answers	
1. Knowledge has worth, but it is bestowed only upon those who can gather it to themselves, retain it, and use it appropriately (Sufi). (True/False).	TRUE
2. The <i>ultimate</i> aim of a pricing policy is to achieve high (satisfaction/profit).	PROFIT
3. A key factor in pricing is what the (retailer/market) will pay.	MARKET
4. The position of a product in its life-cycle and the length of this life-cycle are also determinants of policy.	PRICING
5. Who has market leadership and what competition we face (are/are not) very important for pricing.	ARE
6. Pricing policy must be consistent with the firm's marketing objectives (True/False).	TRUE
7. The <i>key factor</i> in pricing policy is (a) what the market will pay? or (b) the cost of the product?	(a)
8. Leadership, competition, product life-cycle, consumer image, and the distribution network are all influences on the	PRICING POLICY
9. One product has a major market share and strongly influences the market. This usually implies leadership.	PRICE (market)
10. If we have price leadership, then generally competitors (a) make the pricing decisions or (b) follow our pricing.	(b)

Correct answers

- | | |
|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------|
| 11. During the life-cycle we may, in the introductory phase, be able to use <i>skimming</i> or <i>penetration</i> pricing. Skimming is the high-price position used to maximize the cost-recovery rate of a new | PRODUCT |
| 12. A high-price policy for a new product to get the largest <i>cost recovery</i> rate is called ... | SKIMMING |
| 13. By contrast, penetration pricing is used to get as much of the potential market as possible, and generally means (high/low) pricing. | LOW |
| 14. Penetration is used in the introductory phase (when there are no patent considerations) in order to the market. | SATURATE |
| 15. During the growth phase, if the previous strategy was skimming, the price must be lower. If it was penetration, the position in the market must now be consolidated at the (lowest/highest) price level. | HIGHEST |
| 16. If a product has patent protection, can we set a higher price? (Yes/No). | YES |
| 17. This is because (a) the product is safe from competition (b) the product has a longer life (c) a patent is a necessary evil. | (a) |
| 18. Maturity-phase pricing should be at the minimum in order to be (profitable/competitive). | COMPETITIVE |
| 19. In the maturity phase, profitability begins to (rise/decline). | DECLINE |
| 20. In the saturation and decline phases, there is a fall in sales and therefore in | PROFIT |

Correct answers

- | | |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------|
| 21. Before the last phase, the possibility of introducing products must be investigated and explored. | NEW |
| 22. If the life-cycle is <i>long</i> , prices should be high in the (introductory/decline) phase. | INTRODUCTORY |
| 23. In a <i>short</i> cycle there is rapid obsolescence, so the price should generally be (high/low). | HIGH |
| 24. When the customer is willing and able to pay whatever price the seller fixes, then the cost becomes (irrelevant/important). | IRRELEVANT |
| 25. Price control is another factor to be considered. When government regulations insist on retail-price maintenance, then the price is | CONTROLLED |
| 26. Cost fixes the lower limit of the price range, but is not the only important factor. It is important therefore to determine which elements of the cost pattern are relevant to the decision. | PRICING |
| 27. Costs that are relevant to the pricing decision should be (predicted/accurately assessed). | ACCURATELY ASSESSED |
| 28. Fixed costs are allocated and (do/do not) vary in total with volume. | DO NOT |
| 29. Costs that vary directly with the sales volume are costs. | VARIABLE |
| 30. Total contribution depends upon volume, selling price, and variable costs. The greater the volume, the (higher/lower) the contribution. | HIGHER |

Correct answers

31. Since total profits = total contribution less total fixed costs, and total fixed costs do not increase with increased volume, total profits will increase with (increased/decreased) volume, provided contribution is positive.
- INCREASED
32. Pricing policy is also influenced by the geographical area when transportation charges have an impact upon
- PRICE
33. Match the following:
- a) f.o.b. pricing
 - b) delivered pricing
 - c) postage-stamp pricing
 - d) base-point pricing
 - e) zone or grid pricing
- with :
- 1) buyer pays charges from fixed base point
 - 2) each zone has a different price
 - 3) price includes transportation costs
 - 4) buyer pays actual freight costs
 - 5) uniform delivered price to all
- (a) 4, (b) 3,
(c) 5, (d) 1,
(e) 2
34. Another factor in pricing policy is “concessions” given to special customers. Discounts can be non-cumulative or cumulative. Non-cumulative discounts are based on the size of the individual order. If this is small it can be (costly/cheap).
- COSTLY
35. Cumulative discounts are based on the total amount purchased over a period. Assuming continued patronage, the purchaser is not penalized for a(small/large) shipment
- SMALL
36. Trade discounts are discounts to the distributor on the (list/wholesale) price.
- LIST

Correct answers

37. Discounts which encourage immediate payment and avoid credit costs are discounts.

CASH

38. Finally, we must note the importance of overall marketing objectives in determining the level of relative to sales.

PRICES

Now look at the summary for this LU again. With thirty-one correct, move on to Chapter 4, after a quick review of the KLPs and VLD.