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| PRICING STRATEGIESSPRING 2016 MBA**B8649** | White |

**Location:** WJW: 209 T/R, 10:45 AM to 12:15 PM

 Uris: 303: T/R, 2:15 PM to 3:45 PM

**Professor:**  Asim Ansari

**Contact info:** Email: maa48@columbia.edu

 Phone: 212-854-3476 (office)

### Introduction

Pricing is one of the most powerful levers that a firm can use to maximize profits. However, this opportunity to impact profits often remains untapped as many managers do not know how to improve upon historical pricing practices within their companies and industries. This course prepares students to address both strategic and tactical pricing issues and to identify profit-boosting changes in pricing practices across a range of professional contexts – as management consultants, product managers, entrepreneurs, business-unit managers and M&A advisors.

The course is structured around three modules. These are

1. **Pricing Analysis**: In this first module, you will use a variety of data and statistical models to analyze demand and assess willingness to pay. You will also learn how to measure price sensitivity and how to compute price elasticities for new products and for more established ones.
2. **Price Structures and Metrics**: In this module, which forms the heart of the course, you will learn when to use different price structures and how to design them optimally. These price structures take the form of product-line pricing, segmented pricing, price bundling, non-linear price schedules, subscription pricing and other forms of targeting. You will also learn how to use appropriate pricing metrics to monetize value.
3. **Price Management:** In this final module you will study how to manage prices via pricing policy, price delegation, markdown pricing, revenue management and price promotions.

The course uses a mix of lectures, case discussions, mini-cases, analytical exercises, and guest speakers and covers pricing across a broad spectrum of industries involving both B2C and B2B and from both economic and psychological perspectives.

**Reading Materials**

The course uses both *required* and *optional* reading assignments in the form of articles and cases. I will assume that you have done the required reading for each class, have analyzed assigned case materials, and are prepared to discuss them. The optional readings in the class-by-class plan aim to give you additional depth on topics of interest – I might present key points from these in the class, but you are not required to have reviewed the optional reading.

The cases and articles listed in the Class Schedule are included in the course reading packet. A few additional materials will be distributed in class or placed on Canvas in advance of class.

The textbook for the course is:

* *The Strategy and Tactics of Pricing*, by T. Nagle, J. Hogan, and J. Zale, 5th Edition, Prentice Hall, 2010. (NHZ)

The following books are mentioned solely as supplemental reading:

* *Nonlinear Pricing*, Robert B. Wilson, Oxford University Press, 1993.
* *Pricing and Revenue Optimization*, Robert Phillips, Stanford Business Books, 2005.
* *Pricing: Making Profitable Decisions*, Kent B. Monroe, 2nd Edition, Amazon, NY 1990.

**Student Teams**

You will work in **teams of 5** on the group case analysis and final project. Please form your groups as quickly as possible. If you need help in forming a team, let me know in a timely manner so I can facilitate communication with others.

# Grading

1. Class participation: 25%

2. Three individual short assignments (SA): 5% each, total = 15%

3. One individual case write-up (IW): 15% each, total = 15%

4. One group case write-ups (GW): 15% each, total = 15%

5. Course Project (team): 30%

####  Total 100%

Each of these components is described in detail below.

**Class Participation**

You are invited to highlight insightful linkages between class material and your past experience as a professional and as a consumer, and to participate actively in discussion of problems and cases. As you cannot participate without attending, class attendance will be required and will be monitored. You are also expected to contribute positively to the class environment.

**Short Assignments**

There are three short assignments in the course. You need to do them individually. They may involve questions relating to a case or other readings. These assignments will be made available later on Canvas.

**Case Write-Ups**

The due dates for the cases and assignments are given in the Class Schedule section of this document. You will complete one case as part of your group (GW) and the other individually (IW). Both cases are due at the beginning of the class where that case will be discussed. The following cases will be due:

* *Springfield Nor’easters* (IW)
* *Fortis Industries* (GW)

Each full case write-up must not exceed **three** pages (12-point Times New Roman, single-spaced, one-inch margins). This limit does not include exhibits such as tables or graphs. If you need more than three pages, then you are probably including too much information in your solution. Assume the reader is familiar with the case; do not summarize or restate more of the case than necessary.

**Guidelines for Course Project**

Your team will complete a course project. The goal of the project is to apply the concepts from the course to a real pricing problem, either one created by the team or an opportunity faced by a real organization (potentially your own). I include a set of suggested project ideas after this section, but you are free to choose your own topic. If you do, please discuss it with me well in advance.

**Timeline and Deliverables**

The final deliverables are due at the beginning of the last class. The final deliverables are in the form of **PowerPoint slides and an in-class presentation**. There is no formal project write-up. That is, all your motivation, analysis, and recommendations must be contained within the presentation. The presentation should be 15 to 20 minutes long and we will allocate an additional 4 to 6 minutes for questions and comments from the class. I **strongly** encourage you to include additional supporting charts, data, or analysis in an Appendix. The Appendix should contain details that are unnecessary to discuss in the presentation but which are important for me to consider in evaluating the project.

# Topic Ideas for the Final Project

1. **Product lifecycles have shrunk in recent years due to rapidly shifting customer preferences, product proliferation and technological advancements.**

Pricing is a particularly important and complex issue for short-lifecycle products – i.e., products that become obsolete within 6 months to 2 years of introduction. Profile the pricing practices at a company that operates in a short-lifecycle environment – e.g., technology, fashion, entertainment or information contexts. How does the company adjust prices as the product evolves from one stage to the next, as the demand/supply balance changes, or as customers’ value for the product changes? Where within the organization are markdown/promotion vs. introductory price decisions made? What role do channel partners play in managing price across the lifecycle? How are customer expectations managed vis-à-vis price changes? What practical issues does the company face in implementing advanced pricing practices? What opportunities do you see for further improving pricing practices?

1. **Some industries are experiencing major forces of change that are leading to the adoption of new pricing practices.**

Examples of such forces include deregulation, entry of low-cost competition, technological innovation, and transition from one stage to the next of the industry/product lifecycle. Identify an industry that is witnessing such changes in pricing caused by environmental forces. Profile the changes in pricing that are being driven in the industry and the strategies being adopted by different players. Who is being successful at capturing additional value – across competitors, and across the value chain? Is the industry converging to a stable new pricing regime or is it moving into relatively anarchic conditions? What factors are causing the industry to evolve in this fashion? What efforts are industry players making to enhance their organizational effectiveness to price in the new environment?

1. **Identify a company that has a reputation in its industry for being smart at pricing.** Profile its pricing practices – strategy, organization and implementation.

Why has its competition not been able to mimic its success? How much value is smart pricing adding? What insights can other businesses (beyond this industry) draw from this company?

1. **Identify a situation where a company or an industry moved from a “one-size-fits-all” approach to pricing to a segmented pricing approach.**

What triggered the shift? How successful has it been? What practical challenges came up in making the transition and how were these addressed? How much value has been created by the shift to segmented pricing? What integrated strategies across the 4P’s were needed to implement the change? What other improvements can you suggest in how the company/industry should approach pricing?

1. **Describe the pricing strategy for a recently launched product.**

What is the pricing structure and the logic behind it? What did the organization do to implement its pricing successfully in the marketplace? What was the analysis / decision making process that the company went through in arriving at the launch price? What role did competitive pricing behavior play in influencing the success/failure of the product? What improvements could you suggest on how the company approached pricing and the actual pricing strategy?

1. **Pricing optimization systems are gaining steam in the retail sector.**

Demand-Tech, Khi-Metrics, ProfitLogic and Manugistics (all acquired by major players) have developed systems that help retailers optimize pricing for countless product categories. Pick a retail segment and analyze the impact pricing optimization has – and will – have on the industry. How much value is being created? What are the risks, and how could these be mitigated? How could you tell if this is the right time to invest in this capability or not for a player in this segment? What aspects of pricing will pricing optimization automate, and where is managerial involvement still critical? What do you foresee the scope and impact of pricing optimization to be in 5 to 10 years within this segment?

1. **Managing pricing coherently across channels is a particularly tough challenge for brands that are distributed via multiple channels**

Common problems include gray markets, and the conflict between a direct channel, such as the web, with indirect channel partners. Identify a company that has actively worked on addressing pricing challenges across channels. What factors were behind these challenges (e.g., self-interested behavior of channel partners)? How did the company address these issues? How successful has its approach been? Are there other actions it could have taken that you would recommend? What insights can this offer to other businesses in the same or other industries?

Note that the questions in each topic are meant to be suggestive, not exhaustive. Feel free to add additional analyses – the key is to unearth insightful findings and conclusions

Connections with the Core

This course builds upon what you have learned in the marketing and economics core regarding pricing fundamentals. The course also relies on your knowledge of statistics and business analytics. In particular, your knowledge of regression and optimization, and the skills that you acquired in using Excel will be valuable in dealing with data and deriving optimal price structures.

**Conduct**

Out of respect for the other students in your class, it is important for you to focus your full attention on the class for the entire class period. Most students observe proper decorum, but it takes only one person’s behavior to distract the entire class. Class will be conducted using the same rules of decorum that would apply in a business meeting. These rules include the following:

* Arrive to class on time
* Once you have arrived, you should leave the classroom only if absolutely necessary. Leaving to make or take phone calls, to meet with classmates, or to go to an interview, is not considered appropriate behavior.
* If for some reason you must be late for class or leave early, please let me know.
* Unless otherwise directed, use of laptops, cell phones, PDAs, or any other wireless devices is prohibited.

**Honor Code**

You are expected to conform to the norms of behavior outlined in the Columbia Business School Integrity Code (printed at the beginning of the reading packet). Use of case or lecture notes from previous sections of the course is not allowed. Any allegation of academic dishonesty will be forwarded to the Dean’s office for investigation. Any case of proven academic dishonesty will result in failure in the course.

### SCHEDULE

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| --- | --- | --- | --- |
| **Sessions** | **Topic** | **Cases Discussed** | **Due** |
| 1  | Framework for Pricing Strategy |  *Beauregard Textiles* |  |
| 2 | Demand Modeling & Price Optimization |  |  |
| 3 | Value and Relevant Costs |  |  |
| 4  | Assessing Value | *Curled Metals* | SA1: *Curled Metals* |
| 5  | Consumer Psychology and Pricing |  |  |
| 6  | Price Elasticities and Market Structure |  |  |
| 7  | Modeling Bidding Data in B2B  | *B2B Targeting* |  |
| 8 | New Product Pricing via Surveys | *Springfield Nor’easters* |  |
| 9 | New Product Pricing via Multinomial Logit Choice Models |  | SA2: Demand Modeling  |
| 10  | Guest Speaker: Legal Aspects of Pricing  |  |  |
| 11 | Price Structures and Metrics |  |  |
| 12  | Product Lines and Complements | *Keurig at Home* |  |
| 13 | Pricing Optimization for Product Lines and Complements |  |  |
| 14 | Segmented Pricing and Price Targeting | *Springfield Nor’easters* | IW: Springfield Nor’easters |
| 15 | Nonlinear Pricing |  |  |
| 16 | Guest Speaker |  |  |
| 17 | Revenue Management |  |  |
| 18 | Price Management and Negotiation | *Fabtek (B)**The case of the pricing predicament* | SA3: The case of the pricing predicament |
| 19 | Markdowns and Price Promotions |  |  |
| 20 | Price Promotions | *Culinarian Cookware* |  |
| 21 | Integrative Case | *Fortis Industries* | GW: Fortis Industries |
| 22 | Course Wrap-up |  |  |
| 23 | Project Presentations |  |  |
| 24 | Project Presentations |  |  |

SA: Short Individual Assignment, IW: Individual Level Case Writeup, GW: Group Case Writeup

**Session 1 Framework for Pricing**

We will begin with a discussion of Beauregard Textiles, which is a simple case that highlights factors critical for pricing decisions. We will then focus on the role of pricing in value creation and discuss the increasing importance of pricing in today’s markets. We will conclude with a framework for pricing decisions

**Case: Beauregard Textiles [HBS 9-191-058]**

Required Reading

* “Executives Zero in on Price,” WSJ, Sept. 27, 2010.
* “The Price is Really Right,” Business Week, March 2003.

Optional Reading: “The Price is Wrong”, Economist, May 23, 2002.

**Session 2 Demand Modeling and Price Optimization**

We will discuss the basic economic principles that underlie pricing and study the relationship between willingness to pay and demand schedules.

**Session 3 Customer Value and Relevant Costs**

We will review the concepts of Economic value to the consumer and will discuss which costs are relevant for pricing decisions.

Required Reading: “Setting Value, not Price,” Leszinski and Marn, McKinsey Quarterly 1997, #1.

Optional Reading

* NHZ, Chapter 1, Chapters 2 and 9.
* “Pricing, Profits, and Customer Value,” Cespedes, Shapiro, & Ross, 2011 (HBS 9-811-016).
* “Business Marketing: Understand What Customers Value,” James Anderson & James Narus, HBR, Nov-Dec 1998.

**Session 4** **Assessing Value and New Product Pricing Strategies**

We will discuss the Curled Metals case. The case will highlight the importance of choosing a pricing strategy that is consistent with the firm’s overall marketing strategy.

**Case: Curled Metal Inc. [HBS 9-709-434]**

Optional Reading

* NHZ, Chapters 2 and 6
* “Bearings that Pack a Punch (and Their Own Controls),” NYT, Jan. 2, 2010.

**Session 5 Psychology for Pricing**

In this session, we will explore the psychology of pricing. Consumers are boundedly rational in their perceptions and reactions to prices. We will study the concept of loss aversion and discuss reference prices, pricing cues, framing and context effects, and mental accounting. Finally, we will discuss how marketers can influence price perceptions and customer actions.

Required Reading

* “Note on Behavioral Pricing” Gourville, HBS 9-599-114.
* “Mind Your Pricing Cues,” HBR, Sept 2003.
* “Taxi Supply and Demand, Priced by the Mile,” NYT, Jan. 8, 2012.

Optional Reading

* NHZ, Chapters 4 and 5.
* “Many Discounts, Few Deals,” WSJ, Dec. 15, 2010.

**Session 6 Price Elasticity and Market Structure**

We will study how to compute own and cross price elasticities using historical data and linear regression and semi-log regression. We will also discuss how to use these elasticities to assess competitive market structure and the clout and vulnerability of competitors.

Required Reading: NHZ, Chapter 12

 **Session 7 Modeling Bidding and Order Data in B2B Contexts**

We will use a mini-case about pricing decisions for a B2B metals retailer. We will study how transactional data from past bids can be used to decipher the likelihood of purchase on a given order and how an analysis of such data can be used for targeting prices.

Required Reading: None

**Session 8 New Product Pricing Using Surveys**

We will study how surveys and experiments can be used to assess the price sensitivity in new product situations where data are not available. We will discuss how surveys can be designed and executed to obtain reliable information about prices

Required Reading: **Case: Springfield Nor’easters**

**Session 9 New Product Pricing Using Experiments**

We will study how choice based conjoint analysis and other experiments can be used to assess the willingness to pay for new products.

Optional Reading: Online Controlled Experiments and A/B Tests Ron Kohavi and Roger Longbotham

**Session 10 Guest Speaker: Legal Aspects of Pricing**

We will learn about different aspects of the law that influences pricing practices. We will discuss price fixing, resale price maintenance, predatory pricing, dumping and other legal issues of relevance to pricing.

Required Reading: NHZ: Chapter 13

**Session 11 Price Structures and Metrics**

We will discuss why and how companies can benefit from price structures. We will also discuss how pricing metrics can be used to extract value and enhance profits.

Required Reading: NHZ: Chapter 3

Optional Reading

* “The Mystery of the Rude Waiter,” Slate, Jan. 21, 2006.

**Session 12 Product Lines and Complements**

We will discuss how to price product lines and complementary products within the context of the Keurig Case.

**Case: Keurig at Home**

Optional Reading: “Should You Launch a Fighter Brand?” HBR, 2009.

**Session 13 Pricing Optimization for Product Lines and Complements**

We will discuss how to design product lines to enhance profitability. We will also learn how to create optimal product and price bundles for complementary products.

Required Reading: “Why Cable Companies Bundle Their Channels,” The New Yorker, Jan. 25, 2010.

**Session 14 Segmented Pricing and Price Targeting**

We will learn how to implement optimal prices for different segments in the context of the Springfield Nor’easters case

**Case: Springfield Nor’easters**

Required Reading: “Versioning: The Smart Way to Sell Information,” Shapiro & Varian, HBR, Nov-Dec 1998.

**Session 15 Nonlinear Pricing**

We will learn in the different contexts in which nonlinear pricing makes sense. We will also discuss different forms of nonlinear pricing and will construct nonlinear pricing schedules based on data.

**Session 16 Guest Speaker**

**Session 17 Revenue Management**

We will discuss the rationale and meaning of revenue management and study its application in a variety of industries. We will also look at different revenue management mechanisms and how they operate.

**Session 18 Price Management and Negotiation**

We will study how to structure and manage price negotiations, using the cases, Fabtek (B) and “The Case of the Pricing Predicament”.

**Case: Fabtek (B) [HBS 9-592-096]**

**Case: The Case of the Pricing Predicament**

Required Reading

* “How to Master the Art of Negotiating Price,” WSJ, Mar. 22, 2011.
* “Airbus and Boeing Duke it Out to Win Lucrative Iberia Deal,” WSJ, Mar 10, 2003

**Session 19 Markdowns and Price Promotions**

We will discuss how firms can use price promotions and markdowns to manage prices in the short term. We will study the different forms of sales promotions and how these impact category purchasing, brand choices and store choices.

**Session 20 Managing Prices via Sales Promotions**

We will discuss the case Culinarian cookware to establish a framework for analyzing the impact of sales promotions.

**Case: Culinarian Cookware [HBS 4057]**

Required Reading: “Is Groupon Ruining Retail?”, NYT Mar. 16, 2011.

Optional Reading: “Trade Promotion: Essential to Selling through Resellers,” Ailawadi, Farris, and Shames, Sloan Management Review, Fall 1999.

**Session 21 Integrative Case**

We will discuss the integrative case, Fortis Industries, which ties together many of the fundamental concepts we have covered in the course

**Case: Fortis Industries [HBS 9-511-079]**

Required Reading: “Is Groupon Ruining Retail?”, NYT Mar. 16, 2011.

**Session 22 Course Wrap Up**

**Session 23 Project Presentations**

**Session 24 Project Presentations**