



Pricing beyond the 'homo oeconomicus'

Expensive mistakes and profitable opportunities in pricing research



Dansk Markedsanalyse Dag

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Vocatus is the leading research and consultancy company in pricing psychology...

- **Vocatus:** a full service market research and consultancy company with around 60 employees that is based in Munich
- **Focus:** price and decision research in various sectors including IT / telecommunications, consumer goods, financial services, automotive and investment products in a B2C as well as in a B2B context

- **Awards** for our approach to pricing and decision research:

- 2005 German Market Research Award „Best Study“
- 2006 ESOMAR Nomination „Fernanda Monti Award“
- 2007 ESOMAR Nomination „Excellence Award“
- 2008 Nomination German Market Research Award „Best Study“
- 2010 German Market Research Award „Best Study“
- 2010 ESOMAR award „Best Methodological Paper“ Congress



- **Besonderheit („USP“):** we're the only institute to consistently implement approaches to pricing that are based upon pricing psychology – we develop pricing strategies for real-life consumers, thus exploiting the hidden potential of stable pricing psychology effects

...where we can rely upon wide-ranging experience from a huge variety of sectors

Some of our clients in the area of price and decision research



In their current version, classic pricing tools destroy more value than they generate since they miss a large part of the story

Starting point

- **Core pricing problem:** the greatest warrior on the battlefield of major price wars is not the real-life consumer, but a tenacious spectre that is unfortunately found in every textbook: the '*homo oeconomicus*'
- **Classic research tools:** all the classic pricing research tools build upon this inappropriate model of human choice, and further support the development of suboptimal pricing strategies
- **Psychological framework:** a more appropriate pricing research framework can reveal hidden margin potentials, and more profitable pricing strategies can be developed without losing the advantages of classic tools

...so you're invited to join the journey that leads to a new pricing toolbox!

Price motivation can be more diverse than a belief in the 'homo oeconomicus' allows

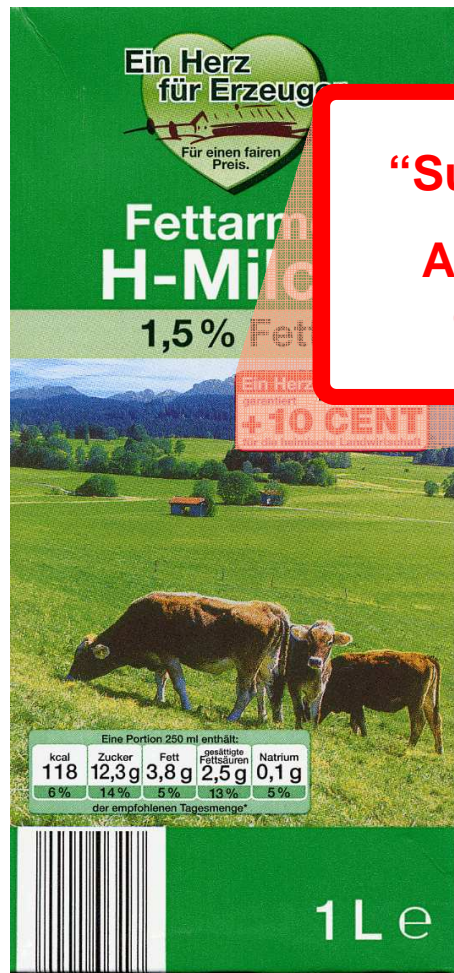


Why it's important to be aware of actual price motivation – example:

- 'Homo oeconomicus' versus 'fairness' - how you can even use price increases as a form of advertising:

Example: commodity goods from different sectors

Price motivation can be diverse – if it's a known quantity, it can sometimes even make sense to use price increases to advertise...



**“Support local producers!
An extra 10 cents go to
German agriculture”**

...but not for every provider!

e.on

E.ON Mitte Vertrieb GmbH · Postfach 10 11 25 · 34211 Kassel

Frau
Maria Mustermann
Musterweg 10
12345 Musterhausen

Support local producers!
An extra 10 cents go to
German energy providers

Jahresrechnung für Strom
August 2007 bis Juli 2008
Für: Hauptstraße 15
34567 Musterstadt
Sehr geehrte Frau Mustermann,

für unsere Lieferungen und Leistungen berechnen wir Ihnen die folgenden Beträge.
Die Einzelheiten können Sie den beigefügten Aufstellungen entnehmen.

	Brutobetrag:
Betrag für Strom	411,09 €
= Rechnungsbetrag	411,09 €
- erhaltene Zahlungen	-280,00 €
= Restbetrag	131,09 €
+ 1 Teilbetrag (für Aug.)	37,00 €
Zahlungsbetrag, fällig am 31.08.2008	168,09 €

Den Zahlungsbetrag sowie die Teilbeträge werden wir auf Grund Ihrer Einzugsmächtigung zu den nachstehenden Fälligkeitsterminen von Ihrem Konto abbuchen:
Konto-Nr. 123456789 (Bankleitzahl 52090000).

Zahlungstermine:

Zahlungsbetrag			Teilbetrag für Feb.		
fällig am:	Betrag:		fällig am:	Betrag:	
31.08.2008	168,09 €		28.02.2009	37,00 €	
Teilbetrag für Sep.	30.09.2008	37,00 €	Teilbetrag für März	31.03.2009	37,00 €
Teilbetrag für Okt.	31.10.2008	37,00 €	Teilbetrag für Apr.	30.04.2009	37,00 €
Teilbetrag für Nov.	30.11.2008	37,00 €	Teilbetrag für Mai	31.05.2009	37,00 €
Teilbetrag für Dez.	31.12.2008	37,00 €	Teilbetrag für Juni	30.06.2009	37,00 €
Teilbetrag für Jan.	31.01.2009	37,00 €	Teilbetrag für Juli	31.07.2009	37,00 €

– illustrative example –

Rechnungsnummer: 1000140084

Geschäftsbereich
Ulrich Fischer
Ulrich Fischerberg

E.ON Mitte Vertrieb GmbH
Mühlentwiete 2
34131 Kassel
Internet: www.eon-mitte-vertrieb.com

Stz der Gesellschaft: Kassel
9408 14400, Ansgarstraße Kassel
Steuernummer 028 022 30749

Landesbank Hessen-Thüringen
Konto-Nr. 12 345 678
BLZ 250 200 100

Price sensitivity can only be validly estimated by looking beyond price assessment and integrating price interest and knowledge too



Why it's important to measure price assessment in the context of all cognitive constructs - an example:

- **Price assessment *versus* price interest and knowledge:** only asking about “willingness to pay” produces systematically biased results. If price interest and price knowledge are not factored in, wrong (and expensive) pricing decisions are bound to be made:

*Self-experiment:
mobile telecommunications*

To find the optimal price, one has to gain a better understanding of customers and their decision processes – let's just give it a try:

Pricing psychology – a self-experiment

- **Who has a mobile phone?**
- **Who thinks that mobile telecommunication is inexpensive?**
(→ price assessment)
- **Who thought that the tariffs were one of the most important decision criteria when choosing a mobile telecoms provider?**
(→ price interest)
- **Who knows the price of a peak-rate call lasting 3.5 minutes to a different provider's mobile telecoms network?**
(→ price knowledge)
- **Who's certain they're with the cheapest mobile telecoms provider?**
(→ purchase behaviour)

The results may surprise some people – but that’s simply the way real-life consumers behave

Case study: telecoms

- **Price assessment, price knowledge, purchase behaviour, and price interest:**

around 1/3 of respondents think mobile telecoms are expensive, are unaware of the tariffs, and are certain they’re not with the cheapest provider, even though the tariff was one of the most important decision criteria for them!



- **Price knowledge and purchase behaviour:**

43% are unaware of their tariffs, even though the tariff was one of the most important decision criteria for them!

- **Price assessment and price knowledge:**

52% think mobile telecoms are expensive without being aware of the tariffs!

- **Purchase behaviour and price interest:**

57% are certain they’re not with the cheapest provider, even though the tariff was one of the most important decision criteria for them!

Something that seems incomprehensible from a theoretical perspective actually conceals vast margin potential...

Pricing psychology – a self-experiment

Let's summarise:

even though you're unaware of the tariffs, you think mobile telecoms are expensive.

And although you considered the tariffs to be a very important decision criterion, most of you are certain you're not with the cheapest provider!

From the perspective of...

... classic price management, these findings are incomprehensible

... pricing psychology, these findings are a typical result

... the company, these findings are 'grounds for celebration'

Understanding the real decision process highlights opportunities to capture new margin potentials



Why it's important to be aware of the actual decision process - example:

- Understanding budgetary concerns might help to explain why discounts are futile:

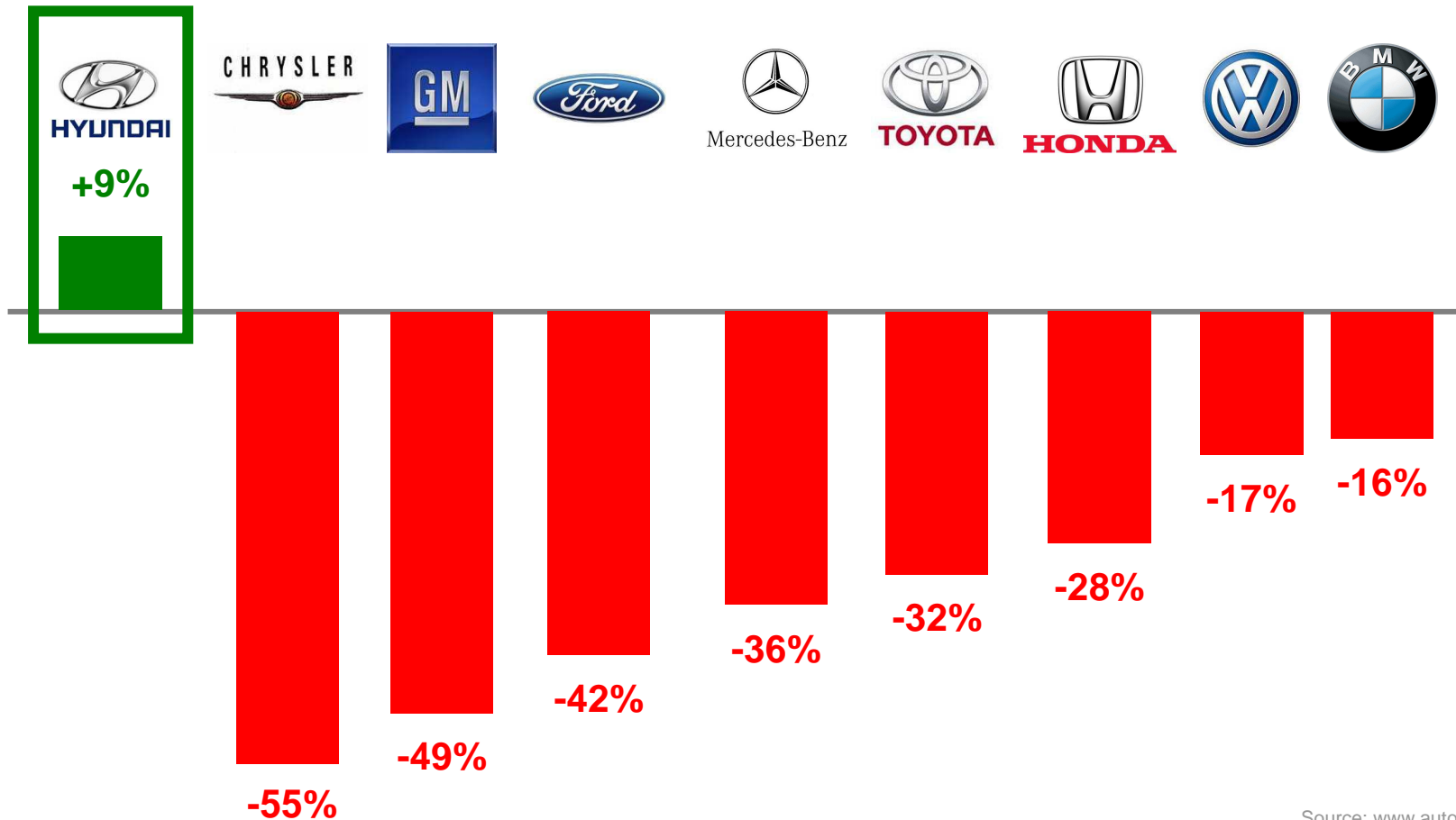
Case study: the US automotive industry in times of economic turbulence

Sometimes there are other options besides discounts in times of economic crisis

Automotive case study: understanding the decision process

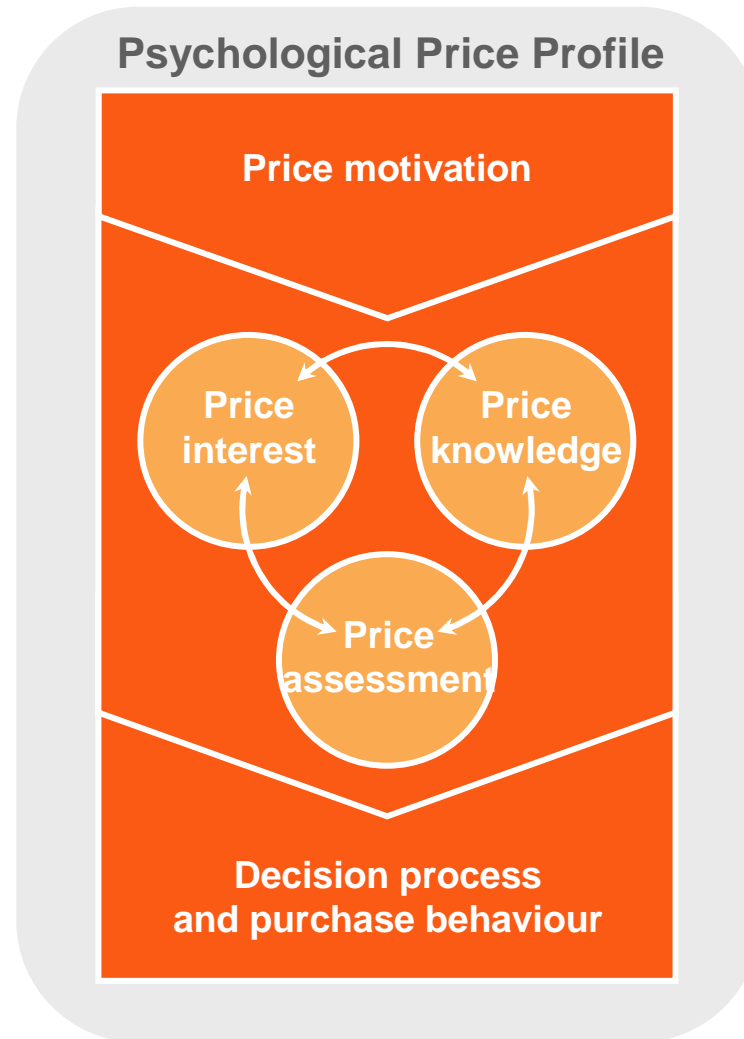
Thinking beyond the 'homo oeconomicus' will help to increase sales volume, sustain profits, and maintain the perception of value

Automotive case study: Hyundai sales (1/2008 vs. 1/2009)

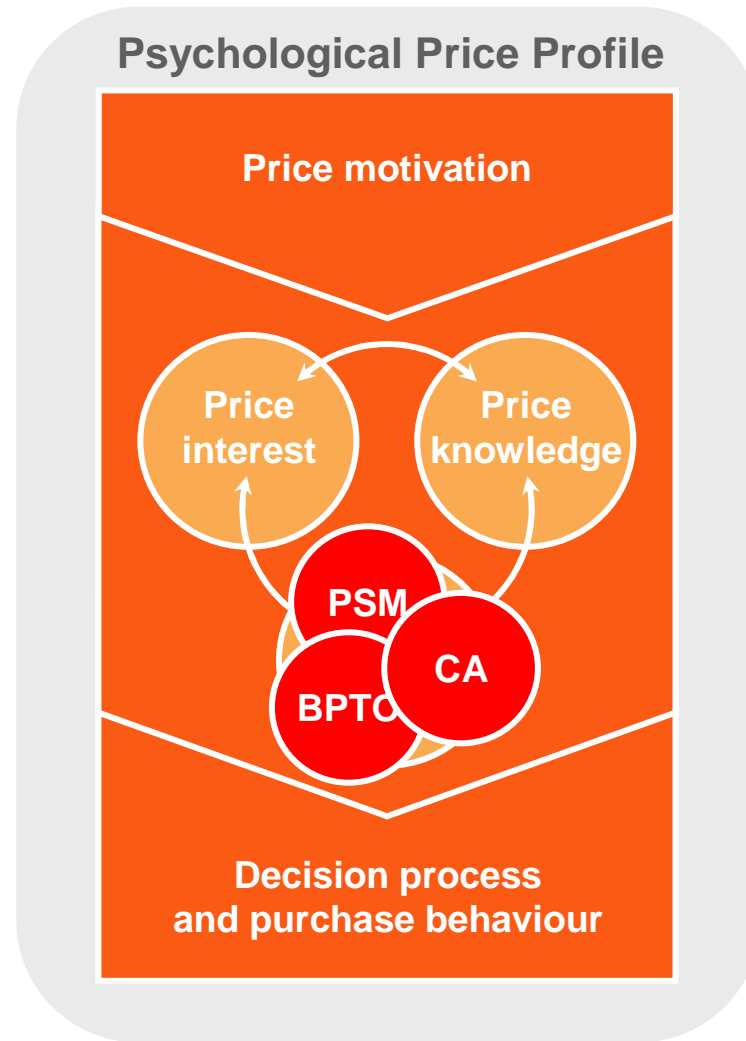


Source: www.autoincar.com

First conclusion: when it comes to optimal pricing strategies, one has to understand the entire 'Psychological Price Profile' ('PPP') ...



... but classic pricing tools neglect these dimensions and only focus on price assessment



... whereas relative price sensitivity is prevalent, and suitable points of comparison can dramatically influence decision behaviour

Case study: media

- Economist e-paper subscription \$ 59
- Economist print subscription \$ 125
- Economist e-paper and print subscription \$ 125

Choice (%)

16%
0%
84%

You might think that options nobody buys are actually dispensable, but...

- Economist e-paper subscription \$ 59
- Economist e-paper and print subscription \$ 125

68%
32%

‘GRIPS’* was intended to condense the ‘PPP’ into a price-related typology and build the basis for more successful pricing strategies

GRIPS* – objectives

- **Comprehensive:** the ‘Grand International Pricing Study’ (‘GRIPS’) was planned to comprehensively understand people’s price-dependent purchase behaviour across all dimensions of the ‘PPP’
- **Universal:** ‘GRIPS’ should deliver results that are universal in terms of being internationally stable and valid across sectors
 - GRIPS was carried out in parallel in 16 countries across four continents
 - GRIPS recruited recent buyers of one out of ten different products in six sectors Automotive Airlines Banking Insurance FMCG Telecoms
- **Practical:** if at all possible, it should provide a price-related consumer typology that builds the basis for:
 - improved understanding and prediction of purchase behaviour
 - improvements to existing pricing research tools
 - the development of better pricing strategies

Second conclusion: one can essentially observe five different consumer types when it comes to prices – and not just one!

The Vocatus pricing typology ('GRIPS')

- **Discount Hunters**

Selectively interested in discounts; lose sight of the total price; buy because of (and not in spite of) the price



Discount Hunters want to be smarter than others – but in their quest for a good deal they sometimes lose track of the broader perspective

Startseite Artikel bezahlen Anmelden Einloggen Service Übersicht

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zurück zur Startseite Kategorie: Möbel & Wohnen > Komplett-Einrichtungen > Schlafzimmer
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- **Loss Avoiders**


Disappointed or cautious consumers; are more afraid of losing something rather than deriving any fun from shopping; they see the latter as unrealistic



If one recognises people's particular motivation, it can be directly addressed by using appropriate pricing strategies

Case study – mobile telecoms market in Switzerland

Orange initially analysed the motivation behind consumers' price sensitivity instead of rushing ahead and asking how low they had to go to attract new customers and keep current ones.



	Optima 30	Optima 100	Optima 200	Optima 400	Optima 600	Optima 1200
Incl. Minutes	30	100	200	400	600	1200
Monthly Fee	22.-	39.-	75.-	125.-	170.-	330.-

Source: www.orange.ch

By doing this, they were able to develop an extremely successful price plan that not only fulfils basic consumer needs (fair and easy to understand), but also makes future price comparisons difficult.

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- **Dynamic Price Accepters**

Open to innovations and options; typically spend more than originally planned

- **Comparison Avoiding Loyals**

Brand-loyal; don't want to invest any time in making comparisons; considerable degree of trust in product promises


























- **Price Indifferents**

Not interested in prices or price comparisons, and unaware of prices too – the topic leaves them cold



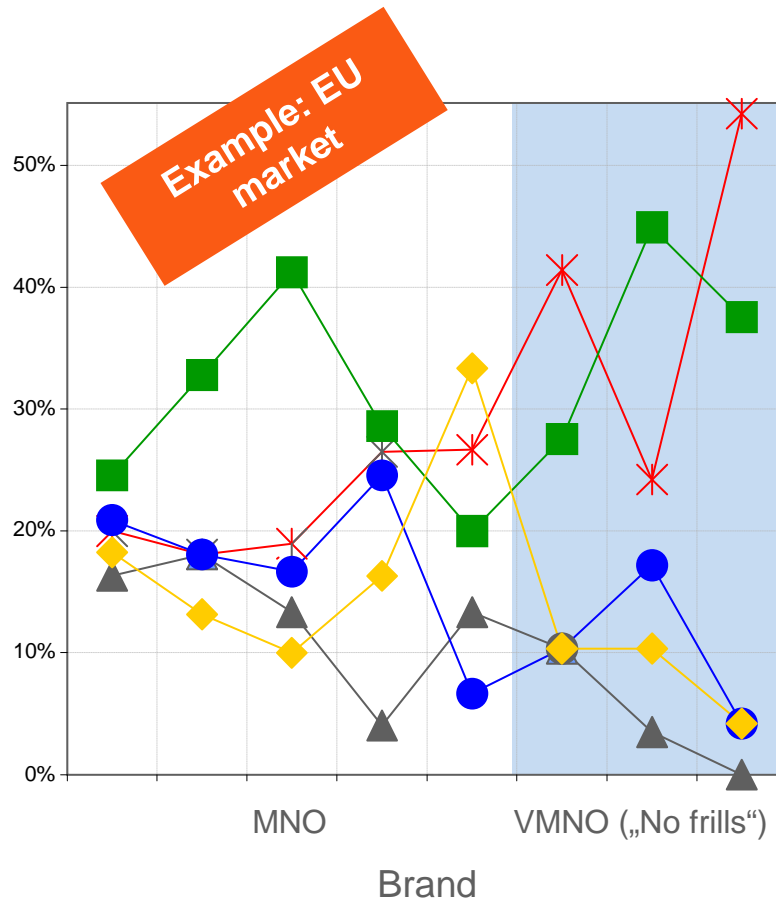
The distribution of GRIPS types differs greatly, depending on the sector

GRIPS at sector level

	 DH	 DPA	 LA	 CAL	 PI
in %	Discount Hunter	Dynamic Price Acceptor	Loss Avoider	Comparison Avoiding Loyal	Price Indifferent
Automotive	 51.5	 20.0	 13.8	 10.8	 3.9
Mobile telecoms	 22.5	 7.3	 36.3	 26.3	 7.6
Magazines	 10.8	 37.4	 2.3	 14.9	 34.2
Financial services	 34.9	 10.1	 30.2	 21.7	 3.1

Within a given sector, GRIPS sensitively reflects market conditions and the distinctive pricing and product strategies of different providers

GRIPS at brand level



A fundamental change in pricing perspective...

- Different providers have (and attract) different customers on the basis of their individual product and pricing strategy
- Different marketing levers are decisive for different brands: different customers are more or less easy to acquire, and competitors must be differentiated with respect to their competitive proximity
- The 'pricing fingerprint' differentiates beyond price levels; this widens the marketing perspective to encompass more than just price wars



Third conclusion: the ‘PPP’ and ‘GRIPS’ help to develop more profitable pricing strategies – three case studies...



Application



- 
- 1. How the ‘PPP’ can help find hidden margins where classic tools are blind**



→ *Case study: newspapers*

- 2. How ‘GRIPS’ can enhance and correct existing tools**

→ *Case study: mobile telecommunications*

- 3. How ‘GRIPS’ can help find pricing strategies beyond the ‘*homo oeconomicus*’**

→ *Case study: last-minute travel*

Pricing is too important to be left to inappropriate tools, but their advantages can still be leveraged with the new research framework

Three takeaways

- 1. Classic pricing assumptions kill profits...:** the assumption of a '*homo oeconomicus*' consistently undermines margins. This phantom destroys value on a conceptual, methodological, and operational level (this is true for B2C as well as for B2B, although most examples here have focussed on B2C)
- 2. ...but a psychological framework and typology ('PPP' and 'GRIPS')** enables more valid recommendations and a better exploitation of potential margins:
 - Unnecessary price wars can be avoided and more margins can be captured, because behaviourally relevant price sensitivity can be measured (e.g. newspapers)
 - Even seemingly paradoxical pricing strategies can be developed as they become conceivable (e.g. last-minute travel)
- 3. This broadens the scope of pricing:** 'PPP' and 'GRIPS' show that:
 - Pricing research entails more than simply measuring price acceptance
 - A pricing strategy involves much more than simply defining price points
 - On the methodological level, the best of both worlds can be seamlessly combined

Thank you for your kind attention!



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