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Strategies to fight low cost rivals

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“By far the single most important thing marketers can do to boost the bottom line is improve the way they price. Interestingly, while firms continue to spend a lot of money trying to reduce costs or bolster revenue, very little attention is paid to optimising price.”

page 14 Marco Bertini

“Using price to awaken consumer thinking... ...and impact buying behaviour. Marco Bertini develops the findings of recent research on the psychological aspects of pricing.

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Rajesh K. Chandy joins London Business School on sabbatical leave from the University of Minnesota, where he holds the James D. Watkins Chair in Marketing, and served until August 2008 as Co-Director of the Institute for Research in Marketing. Chandy served (with the CEOs of 3M, IBM, Microsoft, Medtronic, and UPS) as a member of the US Secretary of Commerce Advisory Committee on Measuring Innovation in the 21st Century Economy. His areas of expertise include innovation, technology management, and marketing strategy. His research and publications on innovation have received several awards, including the Journal of Marketing Harold Maynard Award for contributions to marketing theory and thought, the American Marketing Association Early Career Award for Contributions to Marketing Strategy, the AMA TechSIG Award for the best article on Technology and Innovation, the Marketing Science Institute Alden Clayton Award for the best marketing dissertation proposal, and the Mary Kay Award for the best marketing dissertation. Fortune magazine described his findings on innovation as "an unorthodox and bracing set of management principles." He serves on the editorial boards of Journal of Marketing Research, IEEE Transactions on Engineering Management, Journal of Marketing, International Journal of Research in Marketing, Journal of the Academy of Management Practice in the Entrepreneurship and Technology Management, and Marketing Letters. Chandy has received a number of teaching awards, including the Outstanding Professor of the Year Award, the Award for Excellence in Teaching, and the Outstanding Faculty Recognition Award at the Carlson School of Management, University of Minnesota.

John Mullins is an Associate Professor of Management Practice in Marketing and Entrepreneurship at the London Business School. He earned his MBA at the Stanford Graduate School of Business and his PhD from the University of Minnesota. An award-winning teacher, John brings to his teaching and research 20 years of executive experience in high-growth retailing firms including two ventures he founded and one he took public. Since becoming a business school professor in 1990, John has published three books, numerous cases and more than 40 articles in a variety of outlets, including Harvard Business Review, the MIT Sloan Management Review, and the Journal of Product Innovation Management. His research has won national and international awards from the Marketing Science Institute, the American Marketing Association, and the Richard D. Irwin Foundation. He is a frequent speaker to audiences in entrepreneurship and venture capital.


A company can price discriminate between customers with a high and a low willingness to pay by offering multiple pricing plans. Such plans differ in their monthly fee, their usage price and possibly the number of free units. For example, mobile phone companies offer many different cell phone plans ranging from none to unlimited free minutes. Web hosting companies charge different monthly fees depending on the amount of web space and bandwidth. Insurance companies typically charge a flat fee per month but experiment with pay-as-you-drive insurance. This seminar highlights several strategies that companies can use to price discrimination with options pricing plans and evaluates the probability of such pricing strategies based on results of multiple research projects. We discuss questions such as why customers and companies benefit from a “flat-rate bias”, how customers’ uncertainty about usage contributes to profits, when it may be profitable to switch customers to new tariffs and whether companies should offer so-called rollover minutes.

For full details and to register, please visit www.london.edu/marketing/
Strategies to fight low cost rivals

Nirmalya Kumar

Over the past five years, I’ve studied around 50 incumbents and 25 low-cost businesses. My research shows that ignoring cut-price rivals is a mistake because it eventually forces companies to vacate entire market segments.

The sustainability of low-cost businesses

Successful price warriors stay ahead of market leaders because consumer behaviour works in their favour. If a business gets a customer to buy its products or services on the basis of price, it will lose the customer only if a rival offers a lower price. Since the discounters win all their customers because of the prices they offer, they don’t have to worry about traditional rivals that always charge premiums. Only new entrants with even lower cost structures can compete with the price warriors.

The futility of price wars

The moment a company spots a low-cost competitor, it would do well to ask itself this question: Is our new rival targeting a segment we don’t want to serve or will it eat into our sales? If the new entrant has set its sights on customers no other business serves, incumbents needn’t worry—for the moment. They can observe without engaging the competitor. That wait-and-watch strategy often works for companies that market products for people at the very top of the pyramid, such as wines, perfumes, and cosmetics. Even when market leaders copy the critical elements of low-cost players’ business models, they are unable to match their prices. That’s because the individual elements of the model don’t matter as much as the interactions among them.

Slashing prices usually boosts profits for all incumbents without driving the low-cost entrant out of business. I learned that firsthand while serving as a consultant to a European telecom-equipment provider that was competing against traditional rivals as well as a low-cost Asian competitor for a multimillion-dollar contract in Africa. All the bidders kept cutting prices in order to win, despite the larger equity bases of the latter. That wait-and-watch strategy often works for companies that market products for people at the very top of the pyramid, such as wines, perfumes, and cosmetics. Even when market leaders copy the critical elements of low-cost players’ business models, they are unable to match their prices. That’s because the individual elements of the model don’t matter as much as the interactions among them.

The Sustainability of Low-Cost Businesses

When market leaders do respond, they often set off price wars, hurting themselves more than the challenger. Companies that wake up to that fact usually change course in one of two ways. Some become more defensive and try to differentiate their products—a strategy that works only if they can meet a stringent set of conditions. Others take the offensive by launching low-cost businesses of their own. This so-called dual strategy succeeds only if companies can generate synergies between the existing businesses and the new ventures. If they cannot, companies are better off trying to transform themselves into solution providers or, difficult though it is, into low-cost players. Before I analyse the various strategy options, however, I must dispel some myths about low-cost businesses.
order to best the Asian rival's offer, which proved to be the lowest after every round of bidding. Eventually, the telecom giants discovered that the Asian company had offered a 40% discount on the lowest price the customer could negotiate with rivals. Not surprisingly, the low-cost company won the contract. In addition, although the telecom giants had not made profits on their lowest bids, the Asian contender seemed likely to do so.

When differentiation works

When businesses finally realise they can't win a price war with low-cost players, they try to differentiate their products in a last-ditch attempt at coexistence. Companies, we're told, should adopt the following approaches:

- Design cost products, as, say, Apple and Boeing do
- Continually innovate in the tradition of Gillette and 3M
- Offer a unique product mix, like that of Sharper Image and Whole Foods
- Be a community, la Harley-Davidson and Red Bull
- Sell experiences, as Four Seasons, noodles, and Starbucks do

Three conditions will determine their efficacy. First, smart businesses don't compete tactics in isolation. Second, companies must be able to persuade consumers to pay for benefits and the ability to do so usually depends on the products they sell. And third, companies must bring costs and benefits in line before implementing the differentiation strategy.

Dealing with dual strategies

When companies discover that the low-price customer segment is large, they often set up low-cost ventures themselves. Because of their years of industry experience as well as their abundant resources, incumbents are often seduced into believing that they can easily replicate cut-price operations. Moreover, the business models of such rivals appear to be simpler than their own. In the 1990s, for instance, all the major airlines launched low-fare second carriers—Continental Lite, Delta Express, KLM’s Buzz, SAS’s Snorral, US Airways’ Meridian, Unibet Shuttle—to take on low-cost competition. All these second carriers have since been shut down or sold off, showing how tough it is for companies to use the dual strategy. Although most executives don’t realise it, various companies provide. Over time, the seller develops a deep understanding of the customer’s business processes, so the customer finds it difficult and costly to change suppliers. Furthermore, since low-cost players have limited product ranges and service capabilities, they cannot offer solutions.

Despite the popularity of this strategy, making the changeover is difficult. Many companies, such as Boots, Compaq, Xerox, and Unisys, didn’t succeed because they assumed that selling solutions required modifying their existing business models rather than transforming them.

Switch to low-cost models

In theory, a company can consider switching from a high-cost to a low-cost business model. In practice, such a transformation is unlikely because the incumbent will have a profitable albeit shrinking business to maintain. Moreover, switching to a low-cost business model means acquiring capabilities that are different from the company’s existing competences. It’s hard to imagine many market leaders having the stomach for that.

Low-cost players will continue to mushroom, and some will succeed. However, there will always be two kinds of consumers: those who buy on the basis of price and those who are partial to quality. Therefore, there will always be room for both low-cost players and value-added businesses. How much room each will have depends not only on the industry and customers’ preferences, but also on the strategies traditional businesses deploy. If incumbents don’t take on low-cost rivals quickly and effectively, they can blame no one for their failure but themselves.

Successful price warriors stay ahead of bigger rivals by using several tactics: they focus on just one or a few consumer segments; they deliver the basic product or provide one benefit better than rivals do; and they back everyday low prices with superfine operations to keep costs down.

Purchasing managers in business markets are becoming increasingly sophisticated in their strategies and tactics. Increasingly held accountable for reducing costs, purchasing and other customer, managers don’t have the luxury of simply believing suppliers’ claims of cost savings. A relatively easy and quick way to obtain savings is for purchasing managers to focus on price and obtain price concessions from suppliers. To enhance their negotiating power, purchasing managers attempt to convince suppliers that their offerings are the same as their competitors, so that they could be easily replaced.

In the face of such pressure, suppliers cage in and match competitor prices. It is a rare commodity in business markets to find firms that do business based on demonstrably superior value.

Big idea: Prices are transparent, value is opaque. The book presents a methodology for how to demonstrate the value of your firm’s offering versus the next best alternative in monetary terms. This approach presents below, value merchants

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Betfair is the UK’s biggest online betting company with over 1,800,000 registered customers and over 500,000 active users.

Central to Betfair’s success is its technology which allows it to manage risk perfectly. The result is that punters can bet on an event after it has started. Betfair charges a small house edge. ‘zero lounge’ which means the games have no house edge.

It launched the betting exchange concept with cutting-edge technology in June 2000. Co-founders Andrew Black and Edward Wray were named Ernst and Young Emerging Entrepreneurs of the Year in 2002. The company has since become global and runs from bases in London, Malta, and Tasmania.

Betfair offers betting on over 50 different sports and events from 122 different countries. Horse racing is the dominant sport, then soccer and tennis. Cricket and golf are growth areas. Others include realty TV and financial markets.

The Betfair Games portfolio has expanded to provide its customer streams in what is a highly competitive market. Multiples and Accumulator at Betfair was launched in 2001 for customers to have the chance to win across selections with a range of accumulator betting options. This runs from Malta and has been a significant area of growth and investment. In addition, Betfair Poker was launched in 2004 and is now the exclusive sponsor of the World Series of Poker Europe in London. It’s the result of a three-year partnership with Harrah’s Entertainment to stage the first World Series of Poker event outside of Las Vegas. Betfair Casino was launched in October 2006 after an innovative ‘zero lounge’ which means the games have no house edge.

Betfair launched its own Starting Price (SP) in December 2007 allowing customers to take SP odds set by customer demand instead of being dictated by the bookmaker.

In the UK, Betfair pays tax in exactly the same way as every other bookmaker: a gross profits tax at 15%. This allows all bookmakers to compete on an even footing and ensures a well-regulated and safe environment for all punters. In the 2007 budget, Gordon Brown set the Remotegaming duty at 15% in line with the rate of general betting duty.

Betfair works closely with governments and regulators to provide transparency. It has a 40 strong Integrity Team which monitors betting patterns and records details of every bet and currently has 32 Memoranda of Understanding (MoU) with sports governing bodies to share information about betting patterns and customer behaviour. At the 2007 tennis tournament in Sopot, Poland, Betfair voided £3.4m bets between Martin Vassallo Arguello and Nikolay Davydenko following suspicious betting patterns during the match. The information provided by the Integrity Team to the Association of Tennis Professionals was key to the Gunn and Rees report ‘Environmental Review of Integrity in Professional Tennis’ in May 2008.

Betfair has received two Queen’s Awards for Enterprise: 2003 for Innovation and 2008 for International Trade. In 2004, it won Company of the Year at the Confederation of British Industry Growing Business Awards and in November 2005, it retained its title as Company of the Year at the CBI Growing Business Awards.
Marketing Insight interview:

Anton Bell

Director of Central Marketing, Betfair

Professor Patrick Barwise talked to Anton Bell about the role of marketing and branding at Betfair.

Curriculum Vitae

Betfair 2004-present
Director Central Marketing
Customer Acquisition, CRM, Insight, Planning and Delivery – across sports, casino, poker
Director/Head of Insight
Customer, consumer, competitor and marketing analytics and research

Centrica 2000-2004
Senior Analyst/Project Manager
Marketing, customer relationship management and insight role for Centrica Group – Goldfish, OneTel, The AA, British Gas

Capital One 1999-2000
Senior Analyst/Project Manager
Marketing sub-prime financial credit products and new partnership development

London School of Economics and Political Science
BSc (Econ) Econometrics and Mathematical Economics

What brought you to Betfair?

After Centrica sold Goldfish.com to LloydsTSB, I began looking for a new and fresh online environment that would continue my move away from financial services. When the Betfair opportunity came along, the company was a relatively new and successful enterprise with huge scope for global growth. I'd grown up around betting and gambling - my mum's partner worked as an in-course bookmaker and I'd done a stint with William Hill when I was at university - so I was excited by the chance to be part of something that was revolutionising the gambling industry.

Tell me about the Insight function at Betfair

Building the Insight capability at Betfair was my first challenge. I started with a couple of data analysts querying the new data warehouse and then grew to a strong team of Insight specialists responsible for customer understanding, behavioural analysis and modelling, consumer and market research, competitor and market intelligence. The aim was to bring these areas together to inform and drive business decisions.

What would be a typical Insight project?

One of the first research projects we undertook was simple to understand what our customers thought about us. Our customer base consisted mostly of sophisticated early adopters who were very passionate about their betting and with it, the opportunity that we provided them versus the traditional bookmaker. We were looking to grow our product portfolio and needed to prioritise this against customers’ perceptions of the values we stood for – being innovative, offering value, being fair and on the side of the punter and obviously, person to person (P2P). Talking to our customers provided some fascinating insights into their motivations and we were able to model their responses to the range of new product concepts. Further quantitative understanding revealed that our savvy sports betting customers were still playing more recreational products with our competitors, whilst exhibiting sophisticated behaviour on the Exchange, so it gave us confidence in our plans for future growth.

How has marketing evolved at Betfair?

In the early days of the Exchange, customer acquisition was heavily driven by word of mouth but as our product portfolio has grown over the last four years, so has our marketing investment. Understanding the effectiveness of our marketing spend is critical as the product and channel mix evolves and we look to prioritise new opportunities. Our Finance and Insight teams work very closely with Marketing to stay on top of this.

As we grow, there is an increasing challenge to communicate effectively with our customer base. Targeting relevant and valuable communications to our customers, into an increasingly crowded email inbox, is something that we strive to improve. A solid understanding of the customer life stage, value and risk is central to this activity.

How has the brand developed over time?

We have always been keen to differentiate ourselves from the traditional bookmakers and our early strap line, ‘Sharp minds Betfair’ was intended to be aspirational and inclusive. We found this approach excluded the more recreational segments of the marketplace and some bettors believed that we weren’t relevant to them. Currently, our aim is to promote both the relevance of our gambling proposition - through scale, value and choice - whilst reinforcing the key P2P differentiator of our sports betting offering, which is betting against other people. In summary it’s a superior offering and hence, ‘Betting as it should be’.

So does the brand now have to stretch across different categories?

Betfair historically was purely a sports betting exchange, but we also have Poker and Casino as part of our portfolio. Tradefair was launched in 2007 for those segments attracted to financial and spreads products and, more recently, Tradefair, where you can set up your own tournaments and play against your friends for money or just for fun. Growing our brand from our primary Exchange heritage and moving from niche to mainstream has been our biggest challenge.

What’s the most exciting marketing innovation that you’ve undertaken while you’ve been there?

Betfair continues to innovate by developing new products and businesses and expanding into new markets, so the Central Marketing Team are constantly faced with new challenges. In the past 12 months we’ve embarked on two new partnerships, the main one being with Harrah’s Entertainment sponsoring the World Series of Poker Europe. In October we went live with our first TV campaign and launched the Betfair Starting Price (SP) in November, which kicked off a 5 month multi-channel campaign delivering a series of new innovations from ‘the Betfair Stable’. This culminated in the Grand National actually which delivered a record number of new customers.

And this really helped building awareness of the Betfair brand?

Brand investment has been central to the past 12 month’s marketing success with increased exposure on television extending our reach and driving growth in the UK and Europe. We have a very strong value proposition but the benefits of the P2P concept can be difficult message to get across in a press ad, a poster or even online. TV has provided a richer medium to communicate with different segments of the gambling population and show that we are relevant to everyone who wants to place a bet or gamble online. This is important when some of our competitors have decades of high street presence benefiting their online proposition.

What was the message from the TV?

The TV campaign ran from October and used animation to represent the Betfair world – the scale of our community, betting against others online, providing value to the customer. Over three waves we have seen significant growth in spontaneous awareness, improved understanding of our portfolio and, importantly, a 20% increase in consideration.

What do you think are the mistakes people are making in marketing?

Aligning creativity with empiricism, and achieving clear measurable objectives, is fundamental to marketing effectiveness. Marketers are often focused on developing the big idea or getting the campaign out of the door and lose sight of the original objectives and the target audience. Constantly evolving and learning from successes and mistakes is critical to improving effectiveness and in a fast moving environment it can be difficult to stop and take stock of where these improvements can be realised.

Why are you supporting the Centre for Marketing at London Business School?

London Business School is a great place for staying in touch with new thinking about business and marketing. Operating in new territory, it is vital to look at exemplars in other categories and apply learnings and best practice to our relatively unique model.
Introducing Marco Bertini

Assistant Professor of Marketing, Marco Bertini discusses the effect that price can have on people’s judgments and preferences and suggests how it can be used to solve some of the issues facing marketers today.

What do you see as the main challenge for the marketing function today?

One of the main challenges still faced by the discipline of marketing is accountability. For a number of years now there has been pressure on marketers to demonstrate the return generated by their investments. A lot of work has been done in that area. I can think of a number of important research papers and books that have provided useful insights. At the same time, I think there is still a considerable amount of work to do. More important, I am concerned about some of the reactive measures that marketers seem to be taking. Pressured to quantify their decisions, some marketers are reverting to actions that have little to do with customers. One example is segmentation. Segmentation is getting a lot more attention nowadays; however, marketers seem to favour more and more schemes that rely on easy-to-justify variables such as demographics and geography in consumer markets and account size or industry type in business markets – none of which really identify what customer needs exist in the marketplace. A second example is in pricing, the area I conduct most of my research and teaching in. Harder economic times are putting pricing under the microscope. Unfortunately, marketers continue to base their pricing decisions on the costs of the products they sell. Again, this move is easy to quantify and justify, but neglects the key criterion: what is the customer actually willing to pay?

What is the single most important thing that marketing can do to boost the bottom line?

By far the single most important thing marketers can do to boost the bottom line is improve the way they price. Interestingly, while firms continue to spend a lot of money trying to reduce costs or bolster revenue, very little attention is paid to optimising pricing. First of all, prices should not be set based on costs. This does not mean costs are irrelevant – far from it. Costs are important to understand the implications of pricing decisions. Beyond that, pricing policy needs to start from two key pieces of information: (1) the objective worth of the product we are selling, and (2) the perceived value of that same product to our customers. It is the job of marketing to quantify the benefits in a firm’s offering, measure the gap between objective and perceived value, and work hard to bridge that gap by communicating value in a way that customers understand.

An additional way to improve the quality of pricing is to make sure price policy is well integrated with the other marketing decisions. For instance, a deep understanding of customer needs through segmentation gives marketers the basic information for price discrimination – charging different prices to different segments. Unless firms understand where value is created, and how that value differs across groups of people, the prices that are subsequently set are never going to be optimal. Also, price needs to be calculated in conjunction with the other three “Ps” of the marketing mix. The marketing mix is just that: a mix. Better pricing decisions keep these other factors in mind: How should we structure our product line such that we can charge different prices for different models? What channels of distribution should be used to reach different customer segments with different prices? What promotional material do we need to develop to communicate the value we are selling and therefore justify the price we charge? And so on.

What is unique about the contribution of London Business School’s Centre for Marketing to the discipline of marketing?

The way in which it integrates rigorous academic research with practical relevance. All of the marketing faculty at the school have a strong interest in addressing problems that are important to practice. We definitely pride ourselves in doing things that we think managers find both interesting and useful. This is evident in the research questions we tackle and in the way we teach our programmes and courses. As much as possible, we bring the insight generated by our research to the classroom. The feedback we then receive from the students is crucial to ensure we continue to study relevant phenomena.

What are some of the more interesting findings with practical implications of your research over the years?

As I mentioned earlier, my main area of research is pricing. My work to date has looked at instances where price changes people’s perceptions of the products and services they buy. I find this topic very interesting because such an effect is not really supposed to exist. Price has nothing to do with the quality of a good. It all is supposed to do is index the terms of trade; that is, price “tells” consumers how much money they need to give up in order to make a purchase. My own research and that of other academics in marketing, psychology, and economics show that price can actually have a very strong effect on people’s judgments and preferences.

My article on page 16 demonstrates that price (the amount firms charge, the way firms present price, etc.) can influence how we perceive everyday goods. I have documented cases when the effect is driven by the amount of thinking we do or the attention we pay. The research of other academics has identified other explanations.

What are the main research areas you currently working on?

I am currently working on a number of interesting projects in the area of pricing and promotions. One project I am particularly keen on studies the relationship between assortment size and consumers’ willingness to pay. My co-authors and I have conducted four different experiments to date. The data tells us that consumers are willing to pay less for low quality products and more for high quality products when assortments are large. This polarisation of willingness to pay is puzzling because the evaluation of any product is supposed to be based solely on the merits of that good, not on the number of alternatives available. My co-authors and I believe this effect exists when consumers are uncertain about the value of an offering – a fairly common situation. When this is the case, we believe that consumers infer how important quality
Using price to awaken consumer thinking and impact buying behaviour

Are you aware just how much the price of a product or even the way that the price is presented to the consumer can affect buying behaviour? Recent research on the psychological aspects of pricing suggests that the relationship between price and choice might be more complex than originally thought. Marco Bertini and Luc Wathieu explore this further. Firstly they look at the way that price information is presented and how this can influence consumers’ perceptions of value. Secondly they consider how overpricing can motivate consumers to think about the personal value of a new benefit, in turn affecting their likelihood to buy. The practice of price partitioning has become increasingly common. Instead of charging a simple, all-inclusive price, firms regularly post sets of mandatory charges attached to various attributes of an offer. This phenomenon is not limited to predictable settings such as Internet sites and catalogues. Today, one can also find furniture stores breaking out the cost of sofa pillows and footstools as separate fees. There are differing views on the effects of price partitioning on consumer behaviour. Some believe that price partitioning could increase demand because buyers tend to underestimate the total cost associated with multiple charges. Others, however, argue that price partitioning will decrease demand because multiple losses are generally more painful than a single loss of equal monetary value and that advertising a partitioned price often triggers negative effect, which could consequent into boycotting of the brand and damaging word-of-mouth.

Price partitioning will not only impact on the perception of expenses, but also the perception of nonprice attributes; i.e. the benefits of the purchase. Consumers that are presented with an all-inclusive price are likely to concentrate their evaluation on the focal attribute of the transaction (DOM, groceries, etc.). A partitioned price, on the other hand, increases the amount of attention paid to secondary attributes (shipping and handling, advance booking, etc.), which in turn affects preference and choice. It can sensitize consumers to features they might otherwise overlook. An emphasis on perceived benefits (rather than the negative trade-offs) in which price partitioning increases demand as well as situations in which price partitioning harms demand. For instance, shipping and handling is a requisite in most online transactions, and the cost associated with this service typically varies little across vendors. A secondary attribute is neglected if price is all-inclusive but overemphasised if price is partitioned. This could be an explanation for the “abandoned basket effect” that causes many online transactions to fail through once shipping charges are levied. Secondary features that are relatively easy (difficult) to evaluate receive exaggerated (minimal) consideration under price partitioning. Spelling out what consumers “get” for their money through price partitioning might or might not be good business. If a product offering is mediocre in terms of secondary attributes, for example, firms might benefit by using all-inclusive prices to focus attention to the focal attribute. On the other hand, firms that offer commoditised products might use price partitioning to capitalise on the attractiveness of secondary features and distinct attention from any weakness, in the main value proposition. It is not only the way in which a price is broken down that will awaken consumer thinking. Pricing a product at a level higher than may be initially expected can also motivate consumers to think for longer about a purchase and the personal value of its benefit. What if a firm introduces a new benefit of any kind, consumers are often unsure whether or not they need it or what the benefit is worth to them. Accounting for this uncertainty, firms normally offer an introductory discount or target a small group of more affluent or enthusiastic consumers. Alternatively companies can influence people to think by overpricing—i.e., reduce what they initially want to pay, but not too high. Encouraging the consumer to make a more definite judgment about the personal benefit of a purchase will intensify desire and willingness to pay, justifying the posted price premium.

Consumers’ motivation to think is determined by market prices in combination with other factors such as magnitude of the potential benefit, initial degree of uncertainty, and cost of thinking. If the price associated with a unique additional benefit is low enough, consumers will buy without further questioning their prior impressions. An excessively high price, on the other hand, will discourage a quick purchase because the additional advertisement could reveal nothing to compensate for the extra cost. However, there does exist between these two extremes, a range of prices that should encourage consumers to think and gain clarity regarding the personal relevance of the offered benefit. A sophisticated firm will acknowledge this phenomenon by adjusting its marketing strategy to better manage consumer deliberation. The firm should first consider pricing away from consumers’ initial willingness to pay and evaluate whether regressive pricing (closer to the market’s mean price) or transgressive pricing (farther from the market’s mean price) is optimal. Moderate overpricing is more likely to be optimal when production cost is higher and consumers’ cost of thinking and initial lack of prejudice. The effect of a higher price is not to select less-price-sensitive or higher income consumers but to trigger a ‘polarisation of demand that induces a split between enthusiasts and the in-between’. Potentially useful concepts arising from this work by Bertini and Wathieu include transgressive pricing, regressive pricing, and projective advertising or retailing, all of which derive from the view that one function of price and marketing communication is to stimulate consumers’ thinking and deliberation. Information processing theories and behavioural decision research can be brought together to study these effects, suggesting an interesting avenue for developing our understanding of consumer decision making.

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“Consumers’ motivation to think is determined by market prices in combination with other factors such as magnitude of the potential benefit, initial degree of uncertainty, and cost of thinking.”

This article is taken from the following two papers:•  Price as a stimulus to think: the case for wilful attention arousal through price partitioning•  Price as a stimulus to think: the case for wilful attention arousal through price partitioning

Both written by Marco Bertini, London Business School, and Luc Wathieu (EFM, Cambridge School of Management and Technology)
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