MGT/P 293: Pricing
COURSE DESCRIPTION

Course Objectives

One of the most important decisions that a manager has to make concerns the price that should be charged for the firm's goods and/or services. Pricing decisions influence the quantity that can be sold and therefore have an impact on the firm's revenues, costs, and profits. This course is designed to deepen your understanding of pricing issues faced by organizations having some degree of market power and to suggest pricing strategies that can be used to increase profitability. Some of the basic principles from economics, marketing and other business disciplines will be developed and implications for managerial pricing decision-making will be presented. There will be an opportunity to apply these concepts to address the problems facing real organizations through specific examples and cases. The expectation is that you will develop an understanding of the types of information that are useful in making pricing decisions and how to use that information when developing pricing policies.

Prerequisites

You should be comfortable with the fundamentals of microeconomics as presented in an introductory course. Further, an introductory marketing course will be useful to provide an understanding of the overall marketing environment in which pricing decisions are made. A basic understanding of statistics and differential calculus will be very helpful.

Teaching Methods

Course materials will be presented through lectures, cases and class discussions. The lectures will be used to present the basic theories and concepts that are important for making pricing decisions. Lecture notes will be provided on a regular basis to assist in note taking and reduce the need for you to draw graphs. Your questions and comments are welcomed on lecture days and are expected when we are discussing cases. The cases in this course are based on the pricing problems facing real organizations. They serve two basic purposes: (1) they introduce some of the major pricing issues facing real organizations, and (2) they provide real world settings for the application of the pricing principles presented in lectures. An analysis of the cases should provide practice in recognizing how the real pricing differs from the "ideal" assumed in the models and how the "optimal" pricing policies must be modified to accommodate these differences.

In addition to the lectures and cases there will be periodic exercises, a midterm, and a final project. The midterm will cover the core concepts of costs, customer behavior and demand, and pricing with competition. The final project will require the systematic analysis of a pricing decision facing a real company or making pricing recommendations for a hypothetical company which would require the development of a pricing simulator incorporating a number of the pricing principles introduced in the course.
Course Organization

The course will be divided into four sections. The first section concerns the producer's costs and the demand for its product when it has substantial market power. We will begin by reviewing the classical economic models of price and output selection. Then we will look more closely at the producer's costs and determine how costs can and do have an impact on the firm's pricing decision. Next, we will turn our attention to the demand (willingness to pay) for the producer's output and the factors influencing it. We will consider methods for estimating the demand for a good or service and the resulting implications of demand on the revenues that can be obtained by charging different prices. We will see that prices normally have a lower bound given by the producer's variable costs and an upper bound given by consumer demand.

The second section concerns the problems of pricing in competitive environments. In competitive industries, the firms are mutually interdependent implying that a firm's optimal price depends on the prices charged by its competitors. We will see that it is important for a firm to forecast how competitors will respond to its pricing policies and assess the impact of those responses on its demand. Several models will be developed to illustrate approaches the firm can take to operate profitably in the face of competition, including: capacity limitations, product differentiation, and signaling to competitors through its responses to competitive activity. We will also consider the challenges of pricing with multiple objectives in an uncertain environment.

The third section of the course addresses the issues of pricing in a market in which consumers vary in their demands for products and product features. We will discuss several approaches that allow a firm to legally increase profits by charging different prices to different customers. In particular, we will examine techniques that will allow the firm to profitably take advantage of differences in purchase timing, desired purchase quantities, and patience through the establishment of an effective pricing policy.

The final section of the course deals with the issue of developing a pricing policy that is consistent with the rest of the firm's marketing mix. We will begin by considering how a firm's pricing policy can influence the demand for multiple products in the product mix and the implications for the development of product lines and the prices of the products within and between lines. We will also consider how the pricing tactics for a product may evolve over the product life cycle. The impacts of advertising and various types of promotions on a product's demand and the structure of markets will then be discussed to provide a basis for developing integrated marketing policies. We will conclude with an analysis of the issues that arise when a supplier uses intermediaries to sell its product to consumers. We will discuss the pricing and product adoption decisions of intermediaries (in particular, retailers) and how this behavior may influence the pricing and promotional policies of a supplier.

Textbook and Readings

The required text for this course is *The Strategies and Tactics of Pricing* – Fourth Edition, by Thomas Nagle and John Hogan (Prentice-Hall, 2006). We will be jumping around in the text a bit since the organization of the book doesn't correspond to the organization of the course closely. This fact should not be a concern since the assigned sections can be read on their own and do not depend on preceding sections. In addition, there will be the collection of readings enclosed in a packet. The readings have been selected to provide a more complete background for some of the topics than I will be able to present in lecture. You may find a few of the articles to be somewhat technical. From those readings you should only try to glean the key issues that are raised and their general conclusions. Don't get bogged down in the mathematical or statistical analysis unless it really interests you.
Grading

The course requirements will be weighted as follows:

- Class/Group Participation: 40%
- Midterm Examination: 40%
- Final Project: 40%

In order to provide greater flexibility for the students, the lowest 20% will be dropped from the grade. However, excessive absences for case discussions or poor contributions to the group assignments will result in a grade penalty regardless of the grading option. More detailed information about these requirements is given below.

Class Participation

Your grade for class participation will be determined by your attendance, your contributions to the class discussions, your group's case analyses, and your efforts on periodic problem sets. With regard to your contributions to the class discussions, both quantity and quality are important because much of the value of a class discussion comes from hearing other people's opinions and insights. Absence from class for case discussions will therefore be penalized. As for the quality of participation, prior preparation is obviously important. I will assume that you have done the assigned readings and/or analyzed the assigned case before you come to class. Time is generally limited when we discuss cases and we will not have much time to spend regurgitating the facts of the cases we will discuss. You should be prepared to present your recommendations and analyses if called on to do so since I will randomly select class members or study groups to contribute to the class discussion.

Each student will be expected to actively take part in a study group that should meet to analyze the assigned cases. Each group will be expected to prepare several short written assignments requiring a specific analysis of a case to be discussed in class. These assignments will be due at the end of the class session in which the case is to be discussed. There will be severe penalties for late case assignments. Groups should analyze the cases completely even if they are not required to submit a written write-up since I may randomly “cold call” on groups to contribute to the case discussions. Experience suggests that the optimal group size is three to four persons. Groups larger or smaller than that will be allowed only under extenuating circumstances and will require my permission.

When preparing case analyses you should only consider information provided in the case. You should not devote your time to obtaining outside data sources since you will not be given credit for points based on outside data and doing so will distract you from effectively analyzing the facts in the presented in the case. When preparing your analyses, you may only consult other students currently enrolled in the class or the instructor. Under no circumstances will you be allowed to consult other individuals who have analyzed the case or use notes that relate to the case analyses.

Midterm Examination

There will be a midterm examination given in this course that is tentatively scheduled to be held Friday November 14th. It will be designed to take no more than an hour and a half although you will be given two hours to complete it. It will consist of several true/false questions requiring explanations and several problems and short essays. If necessary, one alternative midterm exam time will be provided. The exam will only offered at the exam times agreed to by the class. No other make-ups will be offered for any reason. If a student is unable to take the exam at the assigned time, an alternate assignment will be given that will count as twenty percent of the grade.
Final Project
There will be a final project (prepared individually) will be to conduct a pricing analysis and recommend a pricing policy for a real world company. At the end of the day of the sixth class session a proposal will be required summarizing the problem to be addressed and the approach (including a brief summary of available data). You are encouraged to contact me prior to this time if you have questions about the feasibility and appropriateness of the project. See the Outline of Class Assignments for more details concerning the requirements.

Optional Problem Sets
Throughout the course there will be periodic optional problem sets. They are designed to help you apply the concepts discussed in the course to simplified problems. While they are not required, you are strongly encouraged to give a serious attempt at completing them. Doing so will enhance your understanding of the course material and the first several problem sets will generally greatly improve your performance on the midterm. Turning in problem sets will also allow you to earn credit that can help offset weaknesses in the required components of the grade (such as absences or a poor midterm score). Problem sets will not be accepted for credit after solutions are distributed.