Chapter 11

Pricing Issues in

Channel Management

The Importance of Pricing

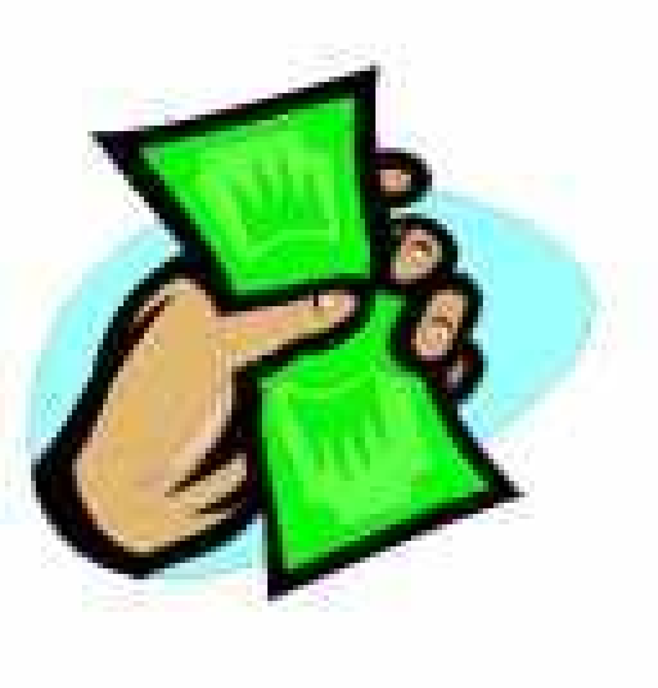
Pricing decisions cause top-level marketing executives more concern than any other strategic marketing decision area.

Pricing is viewed as having a more direct link to the firm's bottom line.

Objective 2:

Anatomy of Channel Pricing Structure

Channel participants each want a part of the total price sufficient to cover their costs and provide a desired level of profit.



The "Golden Rule" of Channel Pricing

It is not enough to base pricing decisions solely on the market, internal cost considerations, and competitive factors. Rather, for those firms using independent channel members, explicit consideration of how pricing decisions affect channel member behavior is an important part of pricing strategy.

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Pricing decisions can have a substantial impact on channel member performance.

Objective 3:

Influencing Pricing Strategy

The major challenge for the channel manager:

To help foster pricing strategies that promote channel member cooperation and minimize conflict

Channel Manager's Role

Major areas of consideration in a manufacturer's pricing decision

- Internal cost considerations
- Target market considerations
- Competitive considerations
- Channel considerations

Channel manager must focus on the channel considerations and work to incorporate them into the firm's pricing decisions

Channel Manager's Role

To find out about channel member views and to appraise their effects on channel member performance

Channel Manager's Role

Have channel members' viewpoints on pricing issues included as an integral part of the manufacturer's price-making process

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Such action anticipates and hopefully avoids problems that may arise after pricing decisions have taken effect

Channel Pricing Guidelines

Why?

1. To help those involved in pricing decisions to focus more clearly on the channel implications of their pricing decisions

2. To provide general prescriptions on how to formulate pricing strategies that will help promote channel member cooperation and minimize conflict

Profit Margins

Guideline #1: Each efficient reseller must obtain unit profit margins in excess of unit operating costs.

OR

Channel members who believe that the manufacturer is not allowing them sufficient margins are likely to seek out other suppliers or establish and promote their own private brands.

Different Classes of Resellers

Guideline #2: Each class of reseller margins should vary in rough proportion to the cost of the functions the reseller performs.

1. Do channel members hold inventories?
2. Do they make purchases in large or small quantities?
3. Do they provide repair services?
4. Do they extend credit to customers?
5. Do they deliver?
6. Do they help train the customers' sales force?

Rival Brands

Guideline #3: At all points in the vertical chain (channel levels), prices charged must be in line with those charged for comparable rival brands.

Channel managers should attempt to weigh any margin differentials between their own and competitive brands in terms of what kind of support their firms offer and what level of support they expect from channel members.

Special Arrangements

Guideline #4: Special distribution arrangements—variations in functions performed or departures from the usual flow of merchandise—should be accompanied by corresponding variations in financial arrangements.

The margin structure should reflect any changes in the usual allocation of distribution tasks between the manufacturer and the channel members.

Conventional Norms in Margins

Guideline #5: Margins allowed to any type of reseller must conform to the conventional percentage norms unless a very strong case can be made for departing from the norms.

Exceptions are possible if they can be justified in the eyes of the channel members. However, it is the job of the channel manager to attempt to explain to the channel members any margin changes that deviate downward from the norm.

Margin Variation on Models

Guideline #6: Variations in margins on individual models and styles of a line are permissible and expected. However, they must vary around the conventional margin for the trade.

Channel members are often amenable to accepting the lower margins associated with promotional products so long as they are convinced of the promotional value of the product in building patronage.

Price Points

Guideline #7: A price structure should contain offerings at the chief price points, where such price points exist.

Price points are specific prices, usually at the retail level, to which consumers have become accustomed. Failure to recognize retail price points can create problems for the manufacturer as well as its channel members if consumers expect to find products at particular price points and such products are not offered.

Product Variations

Guideline #8: A manufacturer's price structure must reflect variations in the attractiveness of individual product offerings.

If the price differences are not closely associated with visible or identified product features, the channel members will have a more difficult selling job.

Guideline Caveat

There is no Guarantee

Particular circumstances and situations exist in which these guidelines will not apply or will be irrelevant.

Objective 6:

Other Channel Pricing Issues

Exercising control in channel pricing

Changing price policies

Passing price increases through the channel

Using price incentives in the channel

Dealing with the *gray market* & with *free riding*

Exercising Control in Pricing

Because channel members typically view pricing as the area over which they have total control. . .

First: Rule out any type of coercive approaches to controlling channel member pricing policies.

Second: The manufacturer should encroach on the domain of channel member pricing policies only if the manufacturer believes that it is in his or her vital long-term strategic interest to do so.

Finally: If the manufacturer believes that it is necessary to exercise some control over member pricing, he or she should do so through "friendly persuasion."

Changing Price Policies

Changes in manufacturer pricing policies or related terms of sale cause reactions among channel members.

Channel members fear such changes because they have become accustomed to the strategy, or their own pricing strategies may be closely tied to those of the manufacturer.

Passing Price Increases Through the Channel

Strategies for channel members to use in order to avoid simply passing along price increases through the channel:

First: Manufacturers should consider the long- and the short-term implications of such increases versus maintaining the current prices.

Second: Manufacturers should do whatever possible if passing on the price increase is unavoidable.

Finally: Manufacturers could change their strategies in other areas of the marketing mix to help offset the effects of such increases.

Using Price Incentives in the Channel

Manufacturers face difficulties gaining strong retailer acceptance and follow-through on pricing promotions.

Possible Solutions:

- Make pricing promotions as simple and straightforward as possible.
- Design price-promotion strategies to be *at least as attractive to retailers as they are to consumers.*

Gray Market & Free Riding

Gray Market
The sale of brand-name products at very low prices by unauthorized distributors or dealers

Free Riding
Describes the behavior of distributors & dealers who offer extremely low prices but little service to customers

Channel design decisions that result in closely controlled channels and selective distribution as well as changing buyer preferences may help limit the growth of the gray market and free riding.