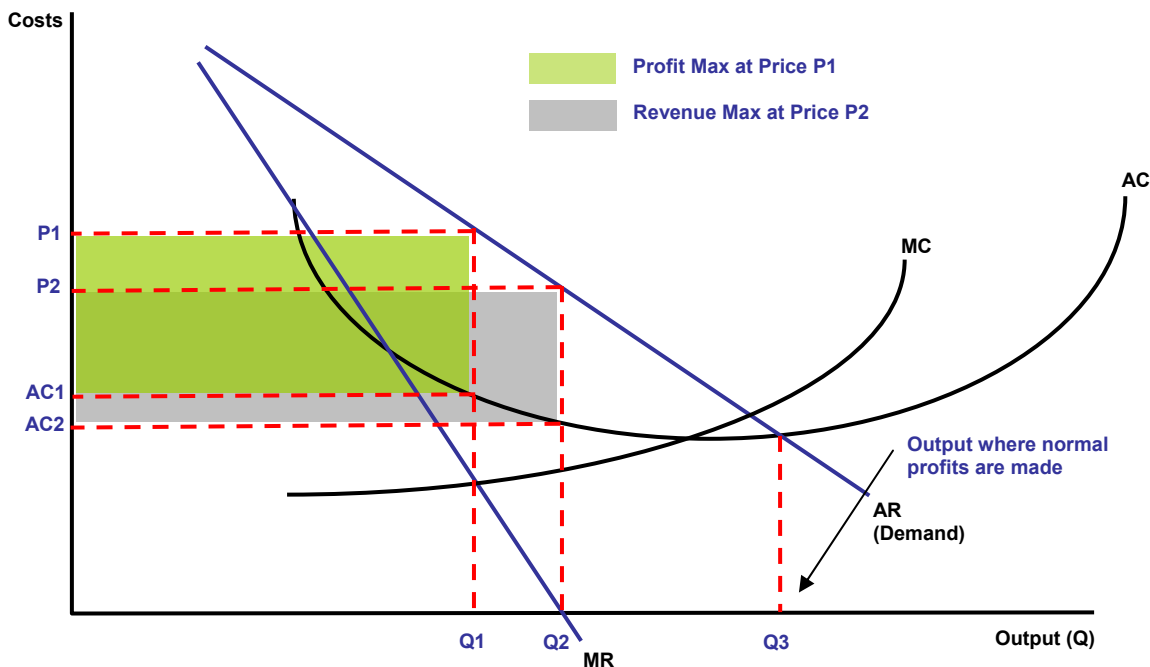


Revision on Business Pricing Strategies

Possible business objective	Price and output point
1. Profit maximization	Output where $MR=MC$
2. Revenue maximization	Output where $MR = \text{zero}$
3. Achieve normal profits only	Output where $P=AC$ (or $AR=AC$)
4. Price discrimination (price targeting)	A range of prices – charging different prices to different consumers for reasons not associated with costs of supply



The traditional "textbook" model is based on the following assumptions:

Profit maximization – profit seeking businesses looking to achieve a profit maximizing "equilibrium"

Businesses have full information about cost and revenue conditions in all of their markets

Linear demand / revenue curves – i.e. straight line AR and MR schedules

Pricing power based on market power – monopoly pricing compared to firms operating in perfect competition

Changing theories of pricing	Real examples to use
1. Much greater use of dynamic pricing especially with the use of the Internet (as opposed to fixed pricing)	Auctions, reverse auctions (where buyers set the price they are willing to pay and then sellers bid for their business), trading exchanges, price matching schemes. e.g. EBay, PriceLine Product bundling (e.g. with holidays (free travel insurance) software, games consoles)
2. Segmentation of markets	Extensive use of price discrimination / price targeting in home and overseas markets
3. Different business objectives	Many businesses are not pure profit maximisers, they may have varying objectives and may opt to engage in satisficing behaviour
4. Globalization of markets	The law of one price cannot hold in a world of globalization where businesses are frequently selling standardized products e.g. drugs, cereals, iPods in markets where consumer preferences, incomes, et al are markedly different. (e.g. price differentials within the EU)
5. Interdependence between firms especially in an oligopoly	Standard textbook theory suggests that firms are independent in their pricing behaviour – patently this is not the case . Many markets tend towards oligopoly in the long run and here we find a high level of interdependence between firms – how will rivals respond to a price change or a change in non-price competition? Potential for different forms of price collusion (overt and tacit) including price leadership behaviour
6. Many markets still affected by industry regulators	Few markets in the UK are completely free from the oversight of competition authorities and other regulatory agencies – in many cases businesses have their prices “controlled” or influenced by the activities of the regulatory authorities e.g. Postal services (PostComm); OFCOM (Telecoms)

Evaluation points:

- Technology is giving most businesses much greater scope for price discrimination / dynamic pricing as a means of raising revenue from a given level of sales
- On the other hand, pricing power is being diminished by greater price transparency
- All firms have some pricing power! Perfect competition does not exist in any market
- But pricing power depends on many variables
 - The extent and nature of competition from domestic and international competitors
 - The limits of industry regulation
 - Ultimately the willingness and ability of consumer to pay for a product is a key constraint on any business

Test your understanding:

Alternatives to profit maximization: <http://vle.tutor2u.net/mod/quiz/view.php?id=1489>

Price discrimination: <http://vle.tutor2u.net/mod/quiz/view.php?id=1494>