

Pricing beyond the *homo oeconomicus*

Expensive mistakes and profitable opportunities in pricing research.

Classic pricing research methods are designed to measure the maximum “willingness to pay” (WTP) of a rationally-deciding *homo oeconomicus*. However, when it comes to real people, it’s often not only the absolute price level that determines purchase; buying behaviour is influenced by many more aspects, such as the underlying price motivation, price knowledge, price interest and the role that price as a whole plays throughout their decision-making process. Vocatus has used a multi-national and multi-industry baseline study to investigate consumers’ actual decision behaviour, and in doing so has defined five different consumer types with regard to price.

A ghoulish spectre is still haunting pricing research: the so-called *homo oeconomicus*. His knowledge of the market is flawless; he’s aware of the prices of his preferred products together with those of comparable alternatives; and he’s always looking for the best value for money. Classic pricing research methods such as conjoint analysis assume the existence of this perfect consumer – the consequence being that the resulting pricing strategies are based on a rational model which is ideal but might not be real.

EMOTION, COGNITION AND BEHAVIOUR

If one takes a closer look at the actual purchase processes of real-life consumers, it quickly becomes obvious that people very rarely make perfectly rational decisions. Consumers may, for example, normally buy their potato crisps from a supermarket where they actively compare offers. Price is then frequently the crucial factor within the purchase decision. On the other hand, if it’s late at night and they’re overcome by a sudden desire for crisps, they’re willing to go to the nearest petrol station and pay two or three times as much – maybe without having even looked at the price.

This example demonstrates that people by no means always act consistently with regard to price. Instead, they are influenced by many different factors. Classic pricing research

methods tend to ignore the fact that consumers make serious ‘errors’ when dealing with prices. For example, they often ignore the fact that price assessment is ‘framing-sensitive’: depending on how one frames the questions about individual WTP, totally different results will be obtained.

Let us assume, for example, that a face cream costs €40 today. When asked about their absolute price acceptance, customers may be willing to pay €50 for it, i.e. €10 more, since it is only when this amount is reached that a noteworthy price threshold becomes apparent. However, companies should treat this response with caution. If one had instead asked the same consumers what absolute price increase they’d accept, the consensus increase may well be only around €2. By contrast, they would probably accept a 10% (i.e. €4) increase if they had instead been asked what relative price increase they would accept. This demonstrates how contradictory consumers’ responses can be, depending on how a question is asked. Pricing researchers must understand this variety of perspectives and not rely upon indications of the absolute price that people would be willing to pay.

As long as our pricing tools employ a “rationalistic” consumer model that is divorced from reality, the potential for price increases will often remain hidden. If we are to detect additional margin potentials, pricing tools must become more sensitive to all psychologically relevant pricing dimensions and to the predictable errors customers make with regard to price. Yet how can one measure consumers’ seemingly unpredictable purchase behaviour?

Even though people may not always act rationally, the decision process is in no way arbitrary; instead, they make consistent and predictable errors. In order to recognize, understand and leverage them, companies must first understand the so-called ‘Psychological Price Profile’. This not only examines how consumers assess a given price, but also looks at the other price dimensions, such as price motivation, knowledge, interest, and the role of price in the decision-making process.

FIVE CONSUMER PRICE TYPES

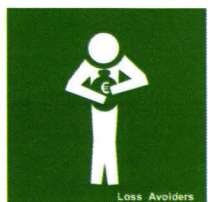
Based upon this Psychological Price Profile, Vocatus used an international study to examine the behaviour of more than 7500 consumers in 16 countries and 10 sectors. The objective was to understand how consumers actually deal with the topic of price within the context of a purchase decision. We discovered five consumer types that differ fundamentally with regard to price knowledge, price relevance, and the emotions that are associated with the purchase process (see illustration). And that's not all: these five consumer segments can be found in every country and sector – although their distribution naturally differs in each case.



Discount Hunter

The first type is colloquially known as the 'Discount Hunter'. Their primary objective is to get the biggest discounts and the best bargains. In order to be 'smarter' than other consumers, they enjoy making in-depth comparisons of prices and products. However, they even tend to buy 'because of' and not 'in spite of' the price.

Thus, for example, they fly to cities they never wanted to go to simply because the €19.90 flight seemed like a bargain. They're often in for a nasty surprise when the final price including fees and fuel surcharges amounts to €79.90.



Loss Avoiders

'Loss Avoiders' manifest a similarly high interest in prices, although not because they enjoy the purchase process per se. Instead, they're afraid of being ripped off. They expend considerable effort on looking for attractive offers even though they actually hate in-depth comparisons. 'Attractive' in this context is much likelier

to mean a fair price or a simple pricing structure, rather than the supposedly 'best' deal. This type is often encountered in markets with complex pricing, like the mobile telecoms sector.



Comparison Avoiding Loyal

The third consumer type is the 'Comparison Avoiding Loyal'. For them, product rather than price is the crucial criterion when making a purchase. They rely on familiar brands and manufacturers with which they've had good experiences. They're not keen to experiment and they don't like lengthy decision processes, so

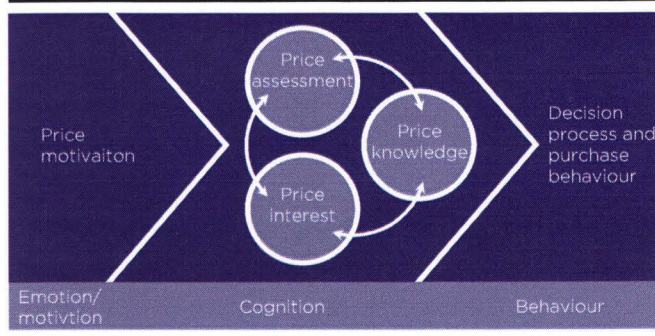
they tend to opt for the same brand and product even though their corresponding knowledge of prices is limited – even at the moment of purchase.



Dynamic Price Accepters

'Dynamic Price Accepters' are open-minded and view the purchase as an experience in itself. They're open to innovations and are always on the lookout for new offers and alternatives. However, they focus on the product rather than the price. For example, when

THE PSYCHOLOGICAL PRICE PROFILE



buying a new car, they may have set themselves a price limit, but when faced with 'soft leather seats' and the 'fancy sat nav' they're more than willing to exceed this original budget.



Price Indifferent

The 'Price Indifferent' consumer is defined by a lack of interest in prices as well as products; they refuse to be tempted by bargains or discounts, but high prices don't necessarily scare them off either. They simply have a need for a certain product and then go out and grab it without any further ado. People

running out of petrol tend to behave like the prototypical 'Price Indifferent': they drive into the next petrol station without regard to brand or price.

These examples suggest that no consumer behaves in exactly the same way when it comes to the totality of their purchase decisions. In the supermarket they will often automatically opt for their usual product, whereas they will look for bargains in the electronics store and gladly exceed their budget for a nice pair of shoes.

MARKETING INITIATIVES

This typology demonstrates that it's high time to exorcise the ghost of the *homo oeconomicus* from pricing management, and to be guided instead by real-life consumers. This leads to more valid forecasts of purchase behaviour, and to more profitable and sustainable pricing strategies, since consumers are much likelier to focus on aspects such as quality and trust than price.

If companies understand how to appeal to consumers' actual motivations they can exploit new margin potentials and innovative pricing strategies. Pricing research amounts to more than just measuring WTP, and pricing involves more than simply setting price points. Defining the pricing structure and price communication are equally important. **WW**

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