

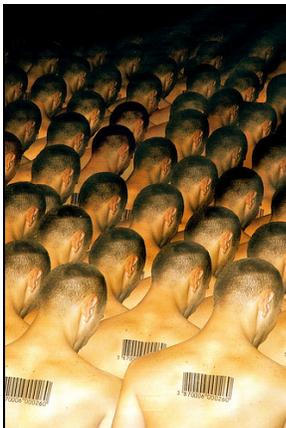
Ron Baker, Founder
VeraSage Institute



What and How People Buy

Antitrust Notice

- **The Casualty Actuarial Society is committed to adhering strictly to the letter and spirit of the antitrust laws. Seminars conducted under the auspices of the CAS are designed solely to provide a forum for the expression of various points of view on topics described in the programs or agendas for such meetings.**
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- **It is the responsibility of all seminar participants to be aware of antitrust regulations, to prevent any written or verbal discussions that appear to violate these laws, and to adhere in every respect to the CAS antitrust compliance policy.**



What are you really selling?

What are your customers really buying?



Not jet engines.

BUT

Flying time.



Not cement. **BUT** On-time delivery.

Charles Revson, Founder,
Revlon



“When it leaves the factory, it’s *lipstick*. But when it crosses the counter in the department store, it’s *hope*.”



Peter Drucker



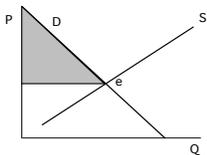
“The customer never buys a product. By definition the customer buys the satisfaction of a want. He buys value.”

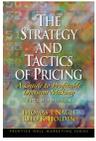
What People Really Buy?

- 1) Good Feelings
 - 2) Solutions to problems; or
- Expectations, according to Ted Levitt



Consumer Surplus

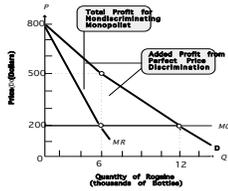




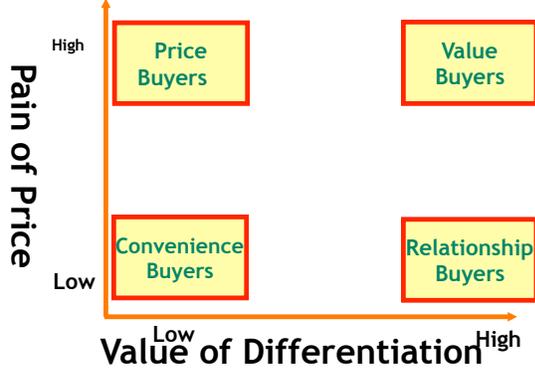
Tom Nagle and Reed Holden

"Managerial judgments of price sensitivity are necessarily imprecise while empirical estimates are precise numbers that management can use for profit projections and planning. However, precision doesn't necessarily mean accuracy. Accuracy is a virtue in formulating pricing strategy; precision is only a convenience. No estimation technique can capture the full richness of the factors that enter a purchase decision. In fact, measurements of price sensitivity are precise specifically because they exclude all the factors that are not conveniently measurable. Yet both measurements and judgment are complements, not substitutes."

Rogaine



Customer Segmentation by Value



4 Ways to Spend Money

	You	Someone else
Yours	Category I	Category II
Someone else's	Category III	Category IV

Relative vs. Absolute Price

	Expensive Date	Cheap Date
Couple w/o children	Dinner + Concert = \$150	Dinner + Movie = \$75
		2:1
Couple w/ children	\$150 + \$50 Babysitter	\$75 + \$50 Babysitter
		1.6:1

7 Customer Segmentation Strategies

- ❶ Buyer identification--Seniors, children, college students, coupons
- ❷ Purchase location--Professional offices, cafés near universities vs. resorts, Coca-Cola
- ❸ Time of purchase--Matinees, Chinese lunch vs. dinner, cell phone peak/off-peak
- ❹ Purchase quantity--Volume discounts, tiered discounts, minimum purchases
- ❺ Product design--GM, petrol, iPod

7 Customer Segmentation Strategies

- ⑥ Product bundling--a la carte vs. dinner menu, season tickets, HP/IBM
- ⑦ Tie-ins and metering--Razors/blades, copiers per page, rental cars per miles

Factors Affecting Price Sensitivity

1. Perceived substitutes effect--New customers (inexperienced)



Factors Affecting Price Sensitivity

2. Unique value effect--Heinz 27% > 48%; Volvo; "Positional" or "Expressive" goods



Factors Affecting Price Sensitivity

3. Switching cost effect—CPAs, Vets, Amazon.com



Factors Affecting Price Sensitivity

4. Difficult comparison effect—long distance, stockbrokers, IBM



“No one ever got fired for buying IBM”

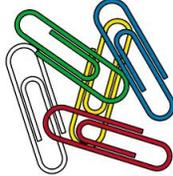
Factors Affecting Price Sensitivity

5. Price quality effect—Rolls Royce, Rolex,



Factors Affecting Price Sensitivity

6. Expenditure effect-Business looks at total purchase, households % income



Factors Affecting Price Sensitivity

7. End-benefit effect-Steel GM vs. Coach Luggage; "AOG"; Michelin; 2 for 1 coupon



Factors Affecting Price Sensitivity

8. Shared-cost effect-4 ways to spend money; tax deductible



Factors Affecting Price Sensitivity

9. Fairness effect—gas discount cash, or premium for credit card; rental car gas; coke vending machine





Warren Buffet

“The single most important decision in evaluating a business is pricing power. If you’ve got the power to raise prices without losing business to a competitor, you’ve got a very good business. And if you have to have a prayer session before raising the price by 10 percent, then you’ve got a terrible business.”

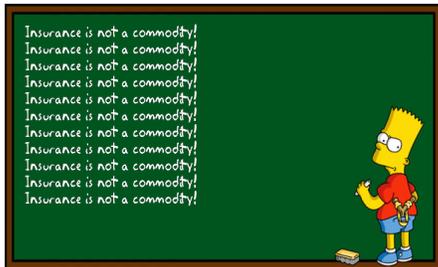
Jim Stengel, former Global Marketing Officer, Procter & Gamble



“I hate it when someone says they’re in a commodity category. We don’t accept that there are any commodity categories. We are growing Charmin and Bounty very well and if there is any category that people could say is a commodity, it’s paper towels and tissues. We have developed tremendous equities, tremendous loyalties from our consumers. So, no, I think that is a cop-out. That is bad marketing and an excuse. We are not in any commodity categories.”

What if Disney Sold Insurance?





Thank You!



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