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Intraorganizational influences on business-to-business pricing strategies: A political economy perspective

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Abstract

Historically, researchers have addressed pricing issues from many different perspectives, including the firm's business model (cost structure, experience curve), stakeholders (customers and channel partners), competition (market structure and intensity), and macroeconomic issues (interest rates, economic growth). An important dimension of organizational price setting that has been neglected is the impact that the firm's internal political system, reflected in interdepartmental coordination and rivalry, has upon price setting. A study of managers who are influential in shaping the firm's pricing strategy was conducted to identify intraorganizational issues and their relative impact on the firm's pricing strategy. The results of the study provide important implications for the development and execution of a firm's pricing strategy.

Keywords: Pricing strategy; Intraorganizational influence; Business-to-business pricing strategies

1. Introduction

How a firm assigns value to its "output" through its pricing strategy has implications for stakeholders both within and outside of the firm, such as employees, competitors, suppliers, customers, government, and third party service providers like transportation contractors. From a demand side perspective, a firm's pricing strategy is essentially a quantification of the perceived value that the firm creates for its customers. From a supply side perspective, pricing is a strategic and tactical expression of how the firm wishes to compete to generate revenues and, in light of its business model, realizes a profit. Several seminal review articles (Monroe & Della Bitta, 1978; Rao, 1984; Gijsbrechts, 1993) on pricing have recognized the importance of understanding the dynamics of developing a pricing strategy, as well as the complexity inherent in such a task.

A firm's pricing strategy may have a substantial economic impact on the firm in contrast to other financial management options. For instance, Hinterhuber (2004) documents that "...a 5% increase in average selling price increases earnings before interest and taxes (EBIT) by 22% on average, compared with the increase of 12% and 10% for a corresponding increase in turnover and reduction in costs of goods sold, respectively." A systematic approach to price setting is important if the firm is to realize its financial objectives; however, Shipley and Jobber (2001) note that price setting "...is a much-neglected and ineptly administered marketing responsibility, and numerous errors are made [p. 313]."

The process of setting and modifying prices must be understood as a component of the firm's overall marketing planning process. Oxenfeldt (1973) was an early proponent of establishing systematic procedures in the context of an overall planning process for the developing of pricing strategies. As markets change, firms are thought to alter their respective marketing plans to take advantage of the new situations and profit accordingly. This change necessitates that all aspects of the marketing plan be treated with the same degree of interest characterized by new market research information, new product development, test mar-

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keting, revised promotional and advertising strategies, competitive analysis, updated supply chain strategies, and revised pricing strategies. Vertical and horizontal interdepartmental cooperation is supposed to take place for each element, with equally high levels of scrutiny (Roger & Whetten, 1982), to ensure that the result of this planning process is an integrated marketing strategy. In addition, any organizational roadblocks that could hinder the immediate implementation of any part of the marketing plan would be eliminated.

This article will explore the experiences of managers who are influential in shaping their firms' pricing strategies across a number of industries. Of particular interest is the documented existence of internal "roadblocks" that managers must face from within their own organization, as they attempt to develop and modify pricing strategies. In the next section, we will incorporate a political economy framework to briefly review the literature on pricing and establish a conceptual context for the contribution of this research. Next, the research methodology will be described, and the results of this study will be presented. Subsequently, the authors discuss managerial implications and study limitations.

2. Background

2.1. Political economy framework

Price setting has long been a difficult process in business-to-business marketing. The complexity inherent in developing and modifying pricing strategies can be seen in the plethora of internal and external economic and political influences that shape a firm's pricing decisions. One framework that may be useful for identifying these various influences is a variation on the political economy approach that was applied to the study of distribution channels by Stern and Reve (2000). The application of this framework will be modified with the individual firm, as opposed to a collective of firms, as the focus. Furthermore, since we are applying this framework to broadly address managerial price-setting considerations, we will not discriminate between process and structure within the economic or political dimensions. The political economy framework, as applied here, is not intended as a means to structure an extensive literature review on pricing, which has been admirably done elsewhere (Gijsbrechts, 1993; Nagle & Holden, 2002). Our purpose is to demonstrate the contribution of this research study, given the work on pricing to date, and to propose a line of managerial research that complements existing research in pricing.

2.1.1. External economic considerations

Firms interact within a network of other firms that comprise an industry or set of industries within a national and global economy. The external economy shapes the firm's access to critical resources, such as raw materials, finished products, capital, and labor. Economic growth and stability directly affect opportunities to generate revenues and to realize a profit in light of the cost of critical inputs, manufacturing, and marketing. A selling firm's potential to generate revenue is shaped by the extent of economic activity within a buyer's industry, which affects a firm's willingness to buy in general and also impacts price sensitivity specifically. One dimension that economists have used to address pricing activity and constraints is through the application of market structure dimensions (pure, monopolistic, monopoly, and oligopolistic competition) on pricing (Mansfield, 1986). This approach has been used extensively in the business-to-business area by researchers attempting to address the dimensions of industry structure on pricing (c.f., Shipley & Bourdon, 1990). Other important contributions in this area include a large body of work stimulated by Porter's (1980) work on competitive intensity and also the incorporation of economic costs in the form of experience curves and pricing (Dolan & Jeuland, 1981).

2.1.2. Internal economic considerations

A truism in organizational price setting is that costs set the floor, and demand sets the ceiling for prices (Dolan & Simon, 1996). From a resource allocation perspective, firms must balance revenues, costs, and investment bases across a number of market opportunities. These opportunities may represent brands, product lines, and strategic business units. Decisions for allocating resources and setting prices are also constrained by the firm's external economic environment in the form of competition and customer price sensitivity. Given that pricing deals directly with revenues and costs, a great deal of attention has been directed towards this area of pricing. Some examples include transfer pricing (Gox, 2000), new product pricing (Bernstein & Macias, 2002), product line pricing (Reibstein & Gatignon, 1984), price change decisions (Monroe & Della Bitta, 1978), strategic pricing (Tellis, 1986; Rao & Bass, 1985), brand life cycle pricing (Simon, 1979), and the impact of the environment on pricing strategy (Monroe & Zoltners, 1979).

2.1.3. External political considerations

Systematic economic decision making concerning the allocation of tangible resources does not take place in a social vacuum. Firms, while interacting with important stakeholders, develop sociopolitical relationships with these stakeholders. Stakeholders that have the potential to have a substantive impact on the firm include customers, suppliers, stockholders, government agencies, and third party service providers. External political relationships have been studied along several dimensions, including power, conflict, and cooperation (Stern & Reve, 2000). Of particular interest is the impact of marketing relationships of channel members on pricing (Perrien & Ricard, 1995) and customer relationships. The importance of relationship marketing in the business-to-business area has long been a distinguishing