South Tuen Mun Government Secondary School
Business, Accounting and Financial Studies
Products Strategies 5.1-5.4

5.1) Explain TWO ways that a company can use to expand its product line.

5.2 What are the differences between market skimming pricing and market penetration pricing?

5.4 Use a supermarket as an example to illustrate TWO major internal factors and TWO major external factors that affect a company's pricing decisions.

5.1 There are three ways to expand a product line:

(i) **<u>Downward stretching:</u>** the company adds new product items to an existing product line in order to attract lower-end new consumers. E.g a more budgeted or affordable product/greater valued.

(ii) **<u>Upward stretching:</u>** the company adds new product items to an existing product line in order to attract higher-end new consumers. E.g a higher quality and prestige image product.

(iii) **<u>Line filling:</u>** the company adds new product items to an existing product line to serve its existing consumers. E.g add more choices in colors, versions of the similar product line.

5.2 **<u>Market skimming pricing</u>** means that a company sets a high initial price in order to earn revenues from consumers who are willing to pay a high price for a new product. The marketer will gradually lower the price to attract other more price-sensitive consumers.

(2 marks)

<u>Market penetration pricing</u> means that a company sets a low initial price in order to attract a large number of consumers to try a new product. It aims to build a large market share as quickly as possible. (2 marks)

5.4 The factors that affect a supermarket's pricing decisions may include:

Internal factors

(i) **Marketing objectives:** The supermarket should consider its marketing objectives. For example, if it wants to capture a greater market share, it may set low prices for its products.

(ii) **Marketing mix strategy:** The supermarket should consider the total marketing mix when setting prices. To build a desired product position, it needs to coordinate its pricing decisions with those of its product, place and promotion strategies.

(iii) **Costs for the supermarket to operate its stores:** These include the costs incurred to secure goods from various suppliers, salaries of employees, utility expenses, rental costs, costs for free delivery to customers, etc. The supermarket should set prices that can cover all of its costs and also create profits.

(Any two of the above, 2 marks for each point)

External factors

(i) **Nature of the market:** Hong Kong has only a few large supermarkets (i.e., oligopoly). The pricing decisions of a supermarket are greatly influenced by those of the others. Therefore, the supermarket should take the pricing decisions of other large supermarkets into account.

(ii) **Demands of the supermarket's consumers:** When setting a price for a particular product, the supermarket should consider how much its target consumers are willing to pay for the product. For undifferentiated products, consumers are more price-sensitive. As such, the supermarket should not charge a high price for this kind of product. For highly differentiated products, consumers are less price-sensitive. The supermarket may charge a higher price for the product.

(iii) **Competitors' strategies:** The supermarket should also consider the pricing strategies and strategic moves (e.g., special promotions, aggressive advertising campaigns) of its major competitors (e.g., PARKnSHOP) when setting its own prices.