Price Analysis


Anoop Howard D’Souza

ANOOP HOWARD D’SOUZA

Master thesis

Subject Category: Industrial Management and Pricing.

Series Number 6/2007

University College of Borås
School of Engineering
SE-501 90 BORÅS
Telephone: +460334354640

Examiner: Göran Stjernman
Supervisor: Olinda Duarte, Volvo Trucks.
Client: Volvo Trucks, Göteborg, Sweden.
Date: 2007/12/14
Keyword: Pricing, Industrial Management, Discounts.
Abstract

Purpose: The purpose of this study is to map and find best practices in the way of working with additional discounts and provisions in addition to standard and options discounts in Volvo Trucks’ European markets. The study is carried out at the dealer level in the demand chain.

Frame work/Methodology: A total of eleven market companies were studied. Extensive study of pricing literature helped give a perspective on pricing in different industries. Also, it revealed there is limited literature devoted to understanding pricing. A questionnaire had to be prepared with open ended questions to collect information from market representatives.

A mixed method approach was deemed suitable to conduct the study over quantitative and qualitative methods.

Observations and Analysis: Pricing is one of the important aspects in any industry; it can determine the level of revenue generated and also helps creates a brand image of a product or service. Discounts and provisions were unique to Volvo markets that operated via dealers and those that operated via salesmen. The discount structure in most markets differed to reach similar end results to adapt to market requirements. The study revealed practices that could be implemented across all markets.

Keywords: Pricing discounts, vendor management, process flow, demand chain.
# Index

<table>
<thead>
<tr>
<th>Section</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Abstract</strong></td>
<td>2</td>
</tr>
<tr>
<td><strong>Index</strong></td>
<td>3</td>
</tr>
<tr>
<td><strong>1. Introduction</strong></td>
<td>4</td>
</tr>
<tr>
<td><strong>2. Background for the Study.</strong></td>
<td>5</td>
</tr>
<tr>
<td>2.1 Volvo pricing concept</td>
<td>5</td>
</tr>
<tr>
<td><strong>3. Objective of Study</strong></td>
<td>7</td>
</tr>
<tr>
<td>3.1 Scope of the study</td>
<td>7</td>
</tr>
<tr>
<td><strong>4. Theoretical foundation.</strong></td>
<td>8</td>
</tr>
<tr>
<td>4.1 Pricing</td>
<td>8</td>
</tr>
<tr>
<td>4.2 Pricing in Logistics</td>
<td>9</td>
</tr>
<tr>
<td>4.3 Logistical Implication</td>
<td>9</td>
</tr>
<tr>
<td><strong>5. Methodology.</strong></td>
<td>10</td>
</tr>
<tr>
<td>5.1 Volvo’s pan European retail pricing- Overview</td>
<td>10</td>
</tr>
<tr>
<td>5.2 Literature and method to be used to for the investigative study-</td>
<td>10</td>
</tr>
<tr>
<td>5.3 Questionnaire preparation</td>
<td>11</td>
</tr>
<tr>
<td>5.4 Interviews and Data Analysis</td>
<td>12</td>
</tr>
<tr>
<td><strong>6. Market Study- Collection of Empirical Data.</strong></td>
<td>13</td>
</tr>
<tr>
<td><strong>7. Observational Analysis of Empirical Data.</strong></td>
<td>14</td>
</tr>
<tr>
<td><strong>8. Conclusions and Recommendations:</strong></td>
<td>16</td>
</tr>
<tr>
<td>8.1 Conclusion</td>
<td>16</td>
</tr>
<tr>
<td>8.2 Recommendation</td>
<td>17</td>
</tr>
<tr>
<td>8.3 Logistical implication of this study</td>
<td>17</td>
</tr>
<tr>
<td><strong>References</strong></td>
<td>18</td>
</tr>
<tr>
<td><strong>Appendix</strong></td>
<td>19</td>
</tr>
<tr>
<td>Questionnaire</td>
<td>19</td>
</tr>
<tr>
<td><strong>Figure 1: Discount structure</strong></td>
<td>144</td>
</tr>
</tbody>
</table>
1. Introduction

An increasingly borderless world has given rise to greater business opportunities and scope (Sheth and Parvatiyar, 2001) but at the same time intense competition has increased between manufacturers as customer demands have vastly increased and there is greater transparency in deals. Volvo believes that this results in customers demanding highly competitive prices and the need for effective price management.

Volvo Trucks is the first manufacturer to use Pan European pricing, meaning that the price of a Volvo truck will be the uniform, regardless of any European market. Pan-European pricing ensures greater transparency in its business model and also promotes a standardized method of functioning. Volvo customers are mainly technology driven, image driven, network oriented and modern professionals.

Each market however, is authorized to offer discounts known as standard discount to ensure that prices are market acceptable while keeping the possibility of price negotiations open. Discounts on options i.e. additional truck add-ons are also offered. The option discounts are the same for all markets.

Further discounts are offered which are termed as additional discounts. There are also provisions, which although do not affect the final invoice amount are used as a support to enhance a deal.

This study is carried out to map the additional discount structure and provisions strategy used in different European markets during negotiations with its dealers. This will enable Volvo to understand the working structure of these markets and the differences between the markets and why the markets function the way they do. This study could help to chalk out changes on a European scale.

A mixed method approach is carried out due to the nature of information to be collected, although the study is largely qualitative in nature. A detailed analysis of the data collected is carried out and a generic process flowchart is mapped; existing good as well as bad practices in each market are compared and changes suggested that could be applicable to all markets.
2. Background for the Study.

2.1 Volvo pricing concept

Volvo is the second largest producer of trucks in the world. Volvo trucks employs a Pan European pricing strategy, the price positioning is determined from a European perspective which is displayed in a Pan European Retail Price list. This means that the price for a ‘standard’ Volvo truck model anywhere in Europe is the same, although the standard models offered in each market have different specifications and may differ from country to country. The standard trucks may differ on the engine, axles and cab.

Volvo has 200 different truck specifications to choose from with various permutations and combinations of different options for the trucks. The pricing strategy is as follows; first we have the basic truck which has its list price and this basic truck is a standard offering to markets in EU. The end price of truck would result in adding options for specific requirements of the customer, they could be additional horse power in the engine, sleeper cabs etc. The price offering of a truck cannot be below the list price of the basic truck even if the customer decides to strip down his truck specification.

Each market company within its frame of authorization then provide discounts during price negotiations. The market could operate via a dealer sales network or Volvo employed salesmen. The discounts are classified as standard discounts and additional discounts which is then dependent on the negotiation capacity, pre determined criteria’s and the profitability target by Volvo salesman or dealers. Additional discounts are ways to ensure obtaining the best deal possible.

Options Discount: Options are accessories that the customer would purchase in addition to the standard truck model. The options could be a more powerful engine, bigger cab body etc. The options discount is fixed at 20 percent for all markets.

Provisions: Provisions are an extra amount kept aside to support a deal; the provisions do not affect the final invoiced price to the dealer. Provisions can be in the form of dealer bonus, trade-in of old trucks etc.

Need: Since the introduction of its Pan-European pricing there has been a need to oversee how the relative market companies function in Europe. Although having a Pan Europe pricing
ensures a clear working method, there are several other factors that affect pricing. These factors are unique to every market in Europe and could range from purchase capacity to brand image. Hence to have an in-depth understanding and to have the ability to compare between the markets, has introduced the need for this study. The study aims to collect information through correspondence with relevant market representatives. The findings would help the company to understand the direction in which their pricing policies are headed towards and also verify that markets have set up robust processes to ensure non ambiguous pricing policies in terms of discounts and provisions. The study also aims to find out how the pricing policies are observed from a person not operating within the company and suggest changes which could be incorporated in the future decision making.
3. Objective of Study

A. The objective of this study is to map Volvo’s current method of working with additional discounts and provisions in their individual markets across Europe in conjunction with standard and options discounts.

B. Analyze the current working method and determine good practices which could be implemented in other markets and identify unfavorable working methods.

C. Observe current pricing strategies from a third person view point and provide an input on practices to be considered in future pricing improvements.

3.1 Scope of the study

The study is aimed at understanding the discount process at the dealer end and hence discounts offered by dealers to its customers are not in the scope of the study. The information gathered is from the market representatives and not dealers. The aim of the study is not to cross question the market companies on existing processes but to simply understand their method of functioning with discounts and document the findings to have a holistic view of the existing practices in each market.

An understanding of the flow of the discount process is of importance, and the factors that contribute to the offering of discount from the market companies to its dealers are covered. The discount rates, although essential are not compared between the markets.
4. Theoretical foundation.

4.1 Pricing
According to Robert J Dolan and Hermann Simon ‘Price is an economic sacrifice a customer makes to acquire a product or service. The customer compares this sacrifice with his perception of the products value. Price and Value are the cornerstones of every economic transaction.’

Price is a language to customers and a quality/price ratio helps to establish a customer’s quality perception of a product or service. Pricing objectives could be long term or short term. In a long term situation the company prices its products lower in the interest of building a larger market share and then reaping profits when its product attains a greater market share, while in a short term situation the company concentrates on profits rather than market share. Both over pricing and under pricing result in sub-optimal sales price. Mis-pricing is costly in terms of time and money as it would create the wrong impression in a customers mind over the perceived value of the product.

When deciding on a purchase two factors namely category risk and retail image (Sheinin and Wagner, 2003) help to alleviate the effect of the price of a product.

Category risk is the uncertainty in terms of financial loss, poor performance, resale value which makes a customer reason on his intent to purchase. Higher the category risk, the less likely he would be willing to pay the price demanded.

Retail image determines how a customer views a retailer based on its utilitarian and symbolic attributes. High retail image equates to a high quality product and superior status and vice versa.

Price Elasticity: It is a measure of the impact of price changes on sales volumes. Price elasticity is the ratio of the percentage change in sales volume to the percentage change in price. If a price elasticity is less than 1, a price increase can be recommended as the percentage decrease in sales volume is smaller the percentage of increase in price.

Discount: A discount is an incentive to make a particular deal enticing to a customer; discounts are a way to attract a customer’s attention and have to be used very carefully as a
customer’s perception of a product is dependent on the amount of discount offered on a product.

4.2 Pricing in Logistics.
Monetary flow is one of the flows in a supply chain transaction along with material, information and resource flows, Lumsden.K (2005). Buyer-Seller relationship can be strengthened by enhancing these flows. Monetary flows are important as this flow is connected to all the other flows in a supply chain.

Cost is usually the scope of interest during a supply chain study, however pricing is what actually generates revenue. Having an understanding of how pricing works in a supply chain gives a holistic view and a better understanding when negotiating deals. Having knowledge of pricing in both, upstream and downstream in a supply chain flow gives an edge and helps strengthen relationships, which is important in developing fruitful and long lasting partnerships.

Also, price is an indicator of the image of a service or product, which is crucial when a customer is ascertaining the particular value of any product. Demand of a service or product increases when the price is right.

4.3 Logistical Implication
Monetary flow is one of the four flows along with material, resource and information flow in a supply chain between suppliers and buyers. According to Dolan et al effective pricing can increase profitability through increased volume sales and revenue. Pricing decisions are often left to finance managers while logistics managers keep a log on inventory, planning, transportation etc. A greater need for understanding pricing is needed, as according to Nagle and Holden (1995) effective product development, promotion, distribution and effective pricing are essential for financial success and important aspects in any business. Pricing in particular generates revenue while all other aspects in a firm generate costs. From a logistics view point effective pricing can help enhance and sustain the following areas- Purchasing, Vendor management, outsourcing, brand positioning etc. to name a few. Having knowledge of how pricing affects an industry can give future logistics managers the tools to have better negotiation capacities and take part actively during price negotiations with its suppliers and customers, thereby having a say in the revenue generating aspect of their business.
5. Methodology.

A thorough understanding of the objectives of the study was essential in establishing a method of conducting the study. Pricing literature from Dolan and Hermann provided a theoretical background to pricing. Research methods by Creswell, J.H provided directions to conduct the study and identify the best suiting method for this study. The procedure for carrying out the study involved the following process-

5.1 Volvo’s pan European retail pricing- Overview

Volvo’s pan European pricing is a base to understand the discounts and provision strategy used. Volvo’s price positioning is made keeping the European market in mind. A standard truck differs across markets and depends on what is perceived as a standard truck for the specific transport environment of the market. Market requirements help to determine the standard offering in a specific market region; differentiators can be Cab body, engines, axles etc. and may vary among the markets. Brief presentations on the above were made by Jan-Olof Carlson and Andreas Stepien of Volvo Truck Corporation. A pan European method of pricing provides greater transparency and a standardized way of functioning. Each market may then use a standard and additional discount to reach a market acceptable price within its frame of authorization rules.

5.2 Literature and method to be used to for the investigative study-

Qualitative, quantitative or mixed methods

Pricing literature has been a good resource for understanding pricing concepts. Various published papers on pricing and discount in the demand chain were also beneficial in understanding pricing methods and challenges in pricing.

Research methods

The study has followed Creswell J.H. (2003) in its research method for conducting the study. Creswell has described 3 methods of conducting research—Quantitative Qualitative and Mixed methods

Quantitative methods is used to quantify an observation, it can be used to quantify an observation made during a qualitative analysis. Quantitative methods are mostly used in measuring the effects of certain processes or phenomena and are usually associated when
dealing with anything that needs to be measured in terms of numbers. Quantitative methods of study provide a conclusion to the study conducted from the data collected.

**Qualitative** methods are used when the need to understand reasons for a particular phenomena and relies greatly on observation and conducting interviews to gather the relevant information needed and subsequent analysis. Qualitative methods of research are mainly exploratory.

The procedure used for the investigative study was a **mixed method** approach as it was considered the most suitable method due to the nature of the study.

**Mixed method approach**- A mixed method approach tends to base a study on pragmatic knowledge claims Creswell, J.H. (2003). This method for data collection uses both open and close ended questions and collects data which are quantitative and qualitative in nature for analysis. The data can be collected concurrently or sequentially. In a concurrent approach, priority is equal for both quantitative and qualitative data and integration is at data collection; while in a sequential approach, the data can be either quantitative or qualitative at first with priority for either quantitative or qualitative aspect and the integration of these two data may be at data analysis, data interpretation or with some combination.

The data collected during the investigative study was concurrent with integration done at data collection; however priority was given to qualitative data, as understanding the market procedures of working with discounts and provisions was the key task in the study. The theoretical perspective of the data was partly implicit and explicit.

**5.3 Questionnaire preparation**
A questionnaire to obtain specific information on the use of discount and provision strategy was prepared and reviewed and had to be approved and suitable changes made accordingly. The questions were created keeping a specific time frame and the nature of information to be obtained. The questions were open ended questions and forwarded to respective markets to help them prepare for the interview. Open ended questions are encouraging questions to obtain a meaningful answer using the interviewed person’s knowledge. The final questionnaire used contained eleven questions after an initial twenty seven question. Although specific questions pertaining to discounts were formulated, the market representative was given the opportunity to provide any other relevant information that could enhance the study.
5.4 Interviews and Data Analysis

Information was gathered from market companies by setting up a phone or physical meeting. The market company representative would provide details on their present method of functioning. The information was collected and additional data was requested which could be used to further understand the discount and provision method in the market company. The data collected from the various market companies were then analyzed to understand and differentiate how each market functions and map a way of working with additional discounts and provisions within the market company.

The following market companies were investigated- Central Europe (Germany, Switzerland, Austria), Central East Europe (the new EU member states), East Europe (Russia, Ukraine, Belarus, Romania, Bulgaria, Serbia), Italy, Spain, Netherlands, Belgium, Sweden, Finland, United Kingdom, France
6. Market Study- Collection of Empirical Data

A total of eleven markets participated in the study. Meetings were set up after taking prior appointments with the market representatives. The meetings were mostly physical due to representatives visiting the company or vice versa and some meetings were conducted through telephonic and via e-mail. The initial information was a brief introduction of the markets and then progressed to the discount and provision structure of each market.

Each meeting lasted approximately one hour and information was noted down during the interview. The representative provided subsequent clarifications and information via email. Great care was taken to ensure that all information collected has been objective. The market representatives also provided further information to get a better understanding of how they function with their discounts and provisions. Representatives were also encouraged to give feedback, both positive and negative, on existing discount systems. The interviews helped me ascertain various tools required to conduct a similar market study in the future. A few things to note are cultural backgrounds, communication skills and most importantly keeping an open mind and not restricting any additional information, however irrelevant it may seem.

Due to nature of information collected from the various markets being termed as classified, the study of each individual market cannot be published. If however, the reader wishes to access the information, they can contact Volvo Trucks, Göteborg, Sweden.
7. Observational Analysis of Empirical Data.

A generic model of the discount process is explained following the data collected from various markets.

Figure 1: Discount structure
A generic representation (Fig.1) of the discount procedure at the market companies of Volvo trucks is displayed. This flow has been determined after analyzing of all markets. The pan European retail price (PEP) for the standard market model is made available to each market.

During the sales discounts process with dealers of the respective regions the following discounts are offered:

**Standard discount**- these are discounts offered on every truck irrespective of the type of buyer. The standard discount is the ratio of initial offer price to the PEP. The markets are authorized to calculate their own standard discounts. This discount requires approval before being offered to the dealers. The standard discount may differ for each model; usually dependent on the truck category.

**Options discounts**- These are discounts offered on the purchase of truck add-ons, it may be a more powerful engine, type of cab- day or sleeper cab. The options discounts are fixed at 10 percent for every market, the exceptions being a few market which offer a different discount rate.

**Additional discount**- A market may offer further discounts known as additional discounts. Additional discounts are used to strengthen a particular deal and provide some leverage during a price negotiation. It is largely dependent on a criteria set by the market company; additional discounts can vary depending on a number of aspects which are at the discretion of the respective market head.

**Provisions**- In addition to discounts that are offered, there are provisions. Provisions do not affect the final invoice price to the dealer, but are used as a tool to motivate the sales for trucks and to take care of future expenses for the truck sold. Provisions can be made for market company determined criteria. Some markets have provisions, while some try to minimize provisions.

A combination of the various discounts and provisions help to strengthen a deal. These are tools that are used by market companies to compete with various manufacturers.
8. Conclusions and Recommendations:

8.1 Conclusion
Every market has a procedure for offering discounts; the end result is similar with methods adapted to the market characteristics. Markets that operate through a dealer sales network have similar discount structure as compared to a sales network operating with Volvo employed salesmen. Additional discounts are used to strengthen a deal during price negotiations and pre-determined criteria are used to determine the eligibility for additional discounts. A dealer network is more structured and organized compared to a salesman operated network.

The best practice in discount structure among the markets studied is the Dutch model, due to proper checks in place to ensure a smooth operation in pricing. This model is ideal in every way and is flexible and ensures a quick response as well better control on the discount structure.

The East European discount structure appears fragmented and there is a lot of scope for having a structured process to be introduced in this market.

Provisions are less prevalent in a Volvo employed salesman network. Provisions are used as per the requirements of the market and provisions are not observed to be standard across the markets. Provisions can be used as per market needs. Although provisions should be limited they cannot be completely eliminated.

Most of the markets have good additional discount and provision structures and changes should be made only after assessing the market needs. Additional discount are adopted to suit the market needs while ensuring profitability.
8.2 Recommendation

In following its discount strategy, Volvo must take into account its competitor pricing, however the competitors have to be a similar tier e.g. Scania, Mercedes Benz. Reference pricing as used by some markets is a useful method to reach market acceptable pricing. The pricing objectives should greatly support the goals of the organization.

While the procedure of having fixed option discount is good; the options can have a variable discount or fixed amount discounted off the options value. This method would give a sense of a getting a better deal if higher valued options are purchased.

A discount matrix is highly important while offering additional discounts, the best model that could be incorporated across all markets is the Dutch model, and the Central European discount structure too is well structured.

8.3 Logistical implication of this study

This study provided me as a logistics student a great exposure to various pricing techniques and various pricing methods followed in the market. The study can be used as a tool to understanding the ‘art’ of pricing. Logistics managers need to have an understanding of pricing and this would leverage their negotiation capacities during a business deal. Also having an understanding on how price discounts function, would greatly help during the pricing process of a logistics process of purchasing or selling a product or service.

Pricing will always be a challenging field, but with proper pricing customer loyalty can be secured.
References


Appendix

Questionnaire

1. Could you give a brief outline of your truck markets? (I.e. number of markets, market situation, share, competition, etc.)

2. Who are the target customers for Volvo trucks? What is the customer perception of Volvo trucks? Who are Volvo trucks main customers? (Segmentation- price sensitive, brand sensitive etc.)?

3. Are standard discounts offered in your market? What is the standard discount range? How do you calculate the standard discount percentage to be offered to your market?

4. Do you offer additional discounts in your market? What are additional discounts and what are the exceptions made while offering additional discounts? What is the additional discount range and how often is it used? Is a rule based method followed for additional discounts?

5. Do you use provisions in your market? What are the different provisions used define and differentiate between each of them. State when provisions are used?

6. What are Volvo’s discount and provision strategy as opposed to its competitors? Are discounts made to match competitor pricing?

7. Describe the truck life cycle discounting strategy (i.e. percentage bandwidth-discounts at the beginning, mid and end of life.) How does the market mature?

Campaigns-

8. Why and when do you initiate a campaign? What is the standard campaign discount offered? How do you measure a campaign performance?

9. How do campaign discounts affect the final pricing? How are they used in conjunction with discounts and provisions? How many times a year do you hold campaigns? Do campaign
discounts differ during different periods? (Applicable if you have more than one campaign per year)

10. Are customers of selective competitors offered higher additional discounts and provisions to make them buy Volvo trucks? Does being a loyal Volvo customer, attract higher discounts and provisions?

11. How much increase in price can a strong brand image justify?

12. What are your feedbacks, positive and negative on the current discounts and provisions? What changes would you like to see?

# Documents and materials that can be provided for reference.