

The Impact of Overvalue Brand Price Reduction to its Profitability

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Abstract

In the competitive market, the essence of the product competition is the brand. Building brand will help the firms to maintain the brand value effectively. Obviously, it is the key of successful operation.

The lower-price products in the same category often threatened the sales of overvalue brand products. Many firms which own overvalue brand usually reduce the price of overvalue brand products to reduce this kind of menace. Then, how does this kind of strategy affect the brand profitability?

A model specifying the role of reducing price strategy and affect in the brand profitability was proposed and tested using hypothetical reducing price of different brands. And, we researched the customers' market and firms by questionnaire, and analyzed the data by factor analysis methodology. We found that in the early days of reducing price, the market share of the brand increases quickly, but, after that, the profit will decrease. From the result, we can see that the reducing price policy of overvalue brand damaged the image of the brand deeply and reduced the market value of the brand.

Our final research found that the market sales performance of the brand decreased. So, we can draw a conclusion that reducing price of overvalue brand is a strategy that will benefit in the short term but harm in the long term. To the managers who want to build brand image and increase their brand's value, this paper maybe can provide them with a useful decision reference.

1. Introduction

Famous brands often have overvalued specialty. Usually, customs consider overvalue brands have higher quality and the higher price is acceptable. When product brands presents as the utility value, the price is viewed as the reflection of its utility value. If the customs consider the famous value have the additional value besides utility value, they would like to pay for the additional price for this product, even it is only of the mental satisfaction. Then, this brand can maintain overvalue by the form of its products.

In the brand promotion, many firms treat the building of famous brand as the aim of building image. Peter Doyle (1989) concluded the evidences of profitability of brands as follows: 1. Brand that possesses 40% market share will produce as 3 times profitability as the brand that possesses 10% market share. 2. To the British grocery products, the first brand will produce six times profit to the second brand and the third, fourth brand can not earn money. 3. Overvalue brand will produce more than 20% profit than the undervalue brand. So, we can say that the profitability of overvalue brand is by brand, the immaterial asset. And overvalue brand is one of the method for high profit.

There is some research about brand profitability but it still lacks the research of the effect of price changing to the profitability. Now, the research of profitability of overvalues brand is as follows: one is using comparatively compare method to validate the profitability. For example, Peter Doyle's (1989) conclusion of the 20% higher profitability of overvalues brand to undervalue brand. The other is using the track investigation of individual brand. For example, we can compare the profitability before and after the price reduction of Macrae.

2. Theory Structure

2.1 The initial price of overvalue brand

The curiosity and attempt mentality make the good opportunity to initial price for managers. If this product and its price are accepted by customs, then, customs will buy it again. To the firms, the fixed custom group has built and with

the promotion of operation, overvalue brand will build its own status. If the overvalue brand is not accepted by the customs, then the reasons may be as follow: 1. Lose of orientation in target market makes the product not accept, 2. The price is too high to make customs buy it. So, we can make the following hypothesis:

H1: If we can orientation the target market successfully, overvalue brand will meet the high-class customs.

2.2 the influence of price to purchase motivation

Because price is one of the most important factors for customs' purchase action, so, overvalue brand has longer acceptable time than other products. So, in the beginning, overvalue brand will take higher operation pressure. And, overvalue is not infinite, if the overvalue is too high, it will be rejected by customs. So, we propose the following hypothesis:

H2: The key of having loyal custom groups of overvalue brand is to hold reasonable quality to price ratio.

2.3 the price transfer of overvalue brand

The main reason of changing overvalue brand price is the pressure of market competition. The competition of market can be reached this by many methods, such as competitors have substitute product, customs are more reasonable, etc. Price is the most effective factor to affect purchase action, so, reducing the price of overvalue brand become a common thing. But, maybe this kind of strategy is not favorable to earnings. So, we have our hypothesis 3.

H3: The transfers of the higher price to its utility value of overvalue brand will make the profit reduce in the long term.

2.4 the levels of product market

There is overvalued brand among different industry and different product. We divide the product of overvalue brand to high consumable (HC, car, etc.), middle consumable (MC, family utility and clothes, etc.) and low consumable (LC, daily consumer goods, beverage, etc.). And the three consumer levels have three prices respectively. We call them overvalue product, par value product and undervalue product. We divided the customs into high price customs, middle price customs and low price customs.

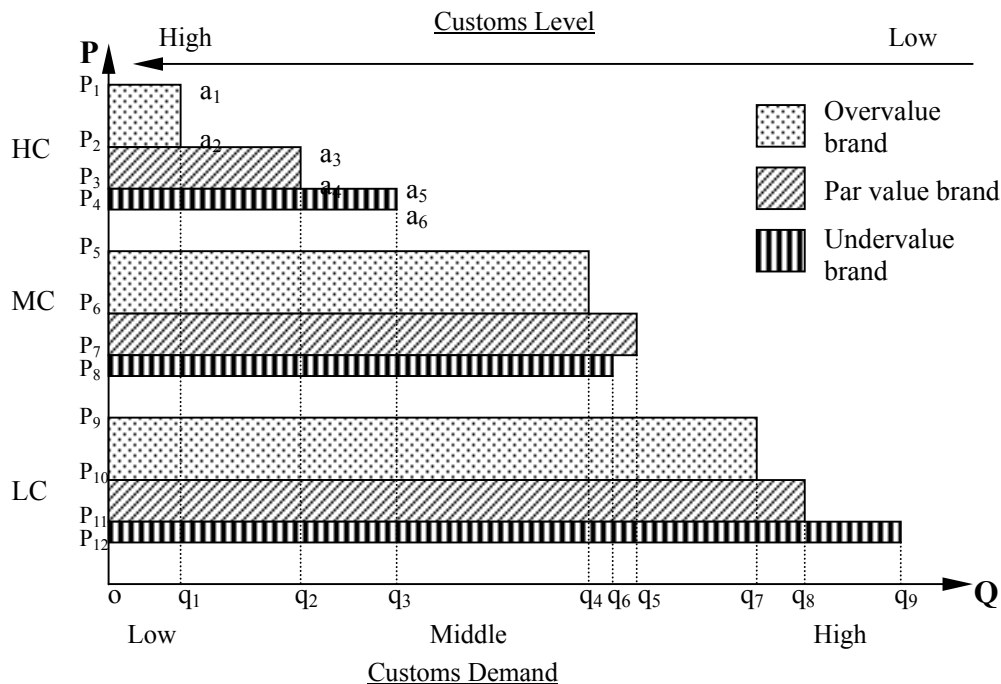


Fig. 1 Consumable Level and Purchase Amount Mode

H4: The price reduction of low consumable to the profit is stronger than the high consumable.

The above mode table are charted according to the China Statistic Annals. It reflects consume situation of different consume market. In the Fig. 1, p_1p_2 , p_2p_3 , p_3p_4 , $p_5p_6 \dots$ are the price units of different consume level, p_1p_2

$\geq p_2p_3$, $p_2p_3 \geq p_3p_4 \dots$ which means that the price of overvalue band products are higher than middle value

products and the middle ones are higher than the low ones. $q_1, q_2, q_3 \dots$ are the demand of different consume level.

So, we have the sales of different level, that is, the sales of overvalue brand in high consume level is $p_1 p_2 \times q_1$, and

the sales of par value brand in high consume level is $p_2 p_3 \times q_2$ and the sales of undervalue brand in high consume

level is $p_3 p_4 \times q_3 \dots\dots$

3. methods

3.1 summarizes

According to the above chart, we build a mode to evaluate the price reduction to the profitability in the long run.

First, we propose the profit of overvalue brand is higher than other products and build a model of profitability which is $S = y_{ij} - y_{ij-1} = \lambda f[(p_{ij} - p_{ij-1}) \times q_{ij}]$. Among which, S is the sales, y_{ij}, y_{ij-1} is the sales before and after the price reduction; p_{ij}, p_{ij-1} is the price unit of different level; q_{ij} is the demand of different consume level; i is the different consumable level; j is the products in different level and λ is the difference coefficient of different products in different level.

3.2 test

(1) Adjusting discount rate method

We will use two methods. One is testing the attitude change of customs of price reduction from the view of customs' knowledge. The other is to investigate the sales by the market investigation of producers.

According to the market investigation, we test H1 and H2. We select the representative products and by reviewing the sales statistics, to test our hypothesis. We found that to the overvalue brands, some of them have long lifecycle such as more than hundred years and the lifecycle of the others' is short. The successful ones' experience tells us that the market orientation is very important. But, what is the reason for short lifecycle? We line the overvalue brand and wish to find answers by consumer questionnaire investigation. By the research, we find that when consumers purchase overvalue brand products, they want to try. But, the main reason for them to decide not to buy is they think the price is too higher than the value. To the 230 persons, 86% consider the price is too high and they admit that they will not buy it again. 11% want to buy again, but if there are similar products, perhaps they will change. And only 3% want to buy it again. So, the key of have loyalty is to maintain a reasonable quality to price ratio. If the ratio is too low, it will not be accepted by customs. And, we tested H1 and H2 here.

(2) Test 2

A. Subject Selection

We select two group persons, 160 graduate students and 136 EMBA students. The difference lies in the consume ability.

We select a brand product in each level: Benz cars as high consumable, Toshiba TV as middle consumable and Nongfu Spring Water as the low consumable. These products are all overvalued ones and they adopted price reduction strategy in sales.

B. Process

We divide the products according to the price. We use different overvalue brand products to research. And test the tendency of their purchase. And, to reduce the differences of consumers, we use the sales data to make multi-test.

(3) Result

The data of investigation are presented in Table 1.

Table 1: The result of several main factors

Factors \ Values: 1—7	Graduate Students	EMBA students
The influence of brand	4. 72	6. 55
The feel of price change	6. 78	5. 12
Trust of overvalue brand	6. 64	6. 96

The probability of buy again	3. 02	6. 11
Buy after price reduction	4. 08	6. 02

We present some important factors and data. By data analysis, we find that: 1. Customs often have brand consume consciousness; 2. The effect of the change of the price of overvalue brand to higher consumers is lower than to the low consumers. 3. Overvalue brand can accept the approval of consumer. 4. Price is the key factors that affect purchase actions, especially to the low consumers.

We contract the data from the producer and from the agent and have the same results.

Using the data of different products to the model $S = y_{ij} - y_{ij-1} = \lambda f[(p_{ij} - p_{ij-1}) \times q_{ij}]$, we have the data of sales before and after price reduction. The data reflect the profitability before and after price reduction and the sales are reflected in Fig. 2.

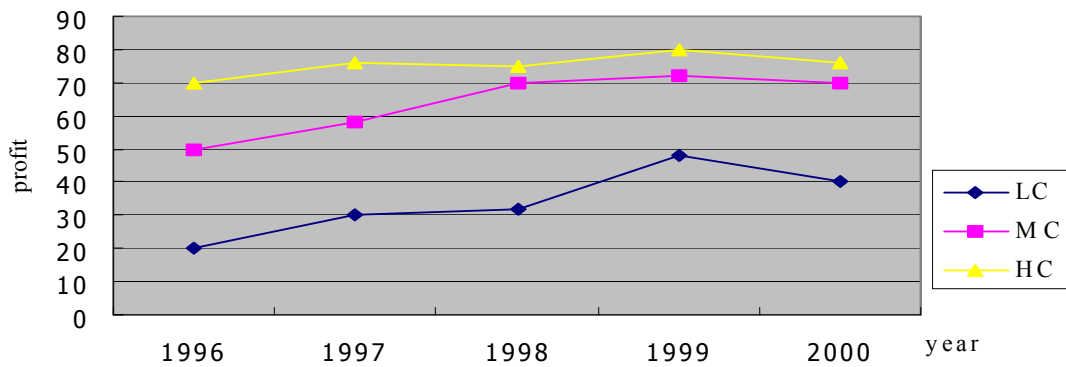


Fig. 2 Profit change after price reduction

We found that, the profitability all decreased after the price reduction and the biggest reduction is the in the beverage.

According to the data, the model and the customs investigation, we got a conclusion after considering the several factors. Our conclusion is the profitability of overvalue brand is reduced after the price reduction strategy. So, we testified H3.

In Fig. 2, we can see that the profit reduction of beverage is larger than to the others. This mains that H4 is testified. That is, the effect of price reduction is larger to the low consumable than the high one.

5. Conclusion

Our aim is to build reasonable price strategy for managers whose firms have overvalue brands.

The lower-price products in the same category often threatened the sales of overvalue brand products. Many firms which own overvalue brand usually reduce the price of overvalue brand products to reduce this kind of menace. We testified if this action would reduce or increase profit, as the managers' hope.

A model specifying the role of reducing price strategy and affect in the brand profitability was proposed and tested using hypothetical reducing price of different brands. And, we researched the customers' market and firms by questionnaire, and analyzed the data by factor analysis methodology. We found that in the early days of reducing price, the market share of the brand increases quickly, but, after that, the profit will decrease. From the result, we can see that the reducing price policy of overvalue brand damaged the image of the brand deeply and reduced the market value of the brand.

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In the operation, the firms which own famous overvalue brand have stable consumer group and the consumer also build loyalty of brand. Price reduction will change its target market while building a new target market will conflict with the former one. Our result shows that when managers make price reduction strategy about overvalue brand, they must be very careful. If not, perhaps they will lose the profitability that they have built.

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