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When 2 + 1 Is Less Than 3: Comparative Pricing Strategies For Premium Upgrades

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Using both field and laboratory studies we show that consumers selecting between vertically differentiated products (i.e., between a standard and a premium--objectively better, but more expensive--version) are more likely to choose premium options when premium prices are quoted as the cost of the upgrade rather than the total price. Specifically, we show that Comparative Pricing (CP) strategies make premium options appear less expensive (vs. All-Inclusive Pricing; AIP) due to the smaller numbers used in the price difference representation.

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EXTENDED ABSTRACT

Using both field and laboratory studies we show that consumers selecting between vertically differentiated products (i.e., between a standard and a premium—objectively better, but more expensive—version) are more likely to select premium options when premium prices are quoted as the cost of upgrade rather than the total price of the premium option. Specifically, we show that Comparative Pricing (CP) strategies make premium options appear less expensive than objectively identical All-Inclusive Pricing (AIP) due to the smaller numbers used in the price difference representation.

From fuel surcharges to required printer ink cartridges, managers have long used various approaches separating the total cost of products into various mandatory components, to reduce price sensitivity and increase demand, by making the total purchase price less transparent, increasing reliance on the base price (Morwitz, Greenleaf, and Johnson 1998). The current research builds on and extends the research on price partitioning to the context of voluntary upgrades, by introducing the notion of CP. By highlighting the price difference between vertically differentiated products, CP will lead consumers to anchor their value judgments on the highlighted tradeoff between a particular feature improvement and the price of that improvement. As such, because the difference in price will always be a smaller numeral than the total price of the premium option, we expect CP to increase the proportion of consumers selecting a premium option by making such an option appear relatively less expensive. In other words, we expect consumers facing price information using CP to undergo a process akin to saying “it’s not \$120, it’s only \$20 more [than \$100],” lead to more upselling under such conditions.

In Study 1 we partnered with a local food bank, using a between-participants design (CP vs. all-inclusive pricing). We set-up a booth advertising for a food bank donation at the heart of a busy Student Union building. A research assistant spoke the following instructions to passing students (N=81): “Did you know that a bag of nutritious food for a person in need costs about \$10 to fill completely? Thinking about students’ budgets, we have two levels of suggested donation. The Basic food pack is \$4 or, if you want to donate more, the Helper food pack is [\$6/\$2 more].” Depending on the price framing condition, this more generous option was offered for either “\$6” in the all-inclusive-pricing (AIP) condition or for “\$2 more” in the CP condition. A significantly higher proportion of people selected the premium donation tier (i.e., Helper food pack) in the CP condition (P=69%) compared to the AIP condition (P=39%; $\chi^2=5.78$, $p<.05$).

Study 2 provides evidence that CP makes the premium option seem cheaper than AIP, and proposes a moderator to reverse the effect. If quoting the sales price using CP leads to increased choice of the premium option because consumers perceive the premium option as cheaper, we should observe the opposite effect when the participant acts as a seller and receives an offer using a CP frame because the offer price in the CP frame will appear cheaper and thus undesirable to the seller. This experiment uses a 2 (framing: CP vs. AIP) X 2 (transaction domain: buyer vs. seller) between-participants design.

Participants (N=221) read a scenario about a buyer-seller interaction for a used bicycle sold through classified ads. Participants

took either the role of the buyer or the seller. In the buyer [seller] scenario, they had shown interest in purchasing one of two second-hand bicycles a seller had put up for sale [a buyer had shown interest in purchasing one of two second-hand bicycles they had put up for sale]. One bicycle, the premium product, was superior because of better gear options (21-speed vs. 3-speed model) and better parts (brand-name parts vs. generic parts). In the AIP condition, the seller [buyer] was offering to sell [purchase] either the regular bicycle for \$150 or the premium bicycle for \$210. In the CP condition, the price of the premium bicycle was framed as “for \$60 more”. Participants selected which of the two bicycles they would purchase [sell] and rated the expensiveness of the premium option (1-7 item).

In the buyer condition, participants in the CP condition were more likely to purchase the premium bicycle (P=70%) than those in the AIP condition (P=50%). In the seller condition, we observed a significant reversal where participants in the CP condition were less likely to sell the premium bicycle (P=26%) than those in the AIP condition (P=46%; interaction (B=1.69, SE=.57, Z=2.91, $p<.01$). Consistent with our prediction, perceived expensiveness mediated the effect.

In Study 3, we examine how heuristic processing (measured by response time) magnifies the upselling effect following CP (as opposed to heuristic processing for Price Partitioning). Participants (N=219) were instructed to imagine themselves shopping for a plane ticket from New York to Los Angeles and shown two different flight options. One of the two flights was cheaper at \$169.00 but took longer to reach the destination because of a connection through San Francisco. The other flight was direct. Participants could select this premium flight for either “\$219.00” (AIP condition) or “\$50.00 more” (CP condition).

Those who made quicker, and presumably more heuristic, decisions (5.8 seconds: 1SD below the mean), were more likely to choose the premium option in the CP (P=60%) than in the AIP condition (P=31%). In contrast, those who made slower, and presumably more systematic decisions (35.5 seconds: 1SD above the mean), showed no significant difference between the CP (P=62%) and AIP conditions (P=63%); interaction B=-.88, SE=.43, Z=2.06, $p<.05$.

Study 3 supports our account that comparative pricing increases preference for premium options because participants focus their value assessment on the price difference, not the total price. Consistent with this theorizing, the CP framing leads faster, hence more heuristic decision-makers to select more premium choices than the AIP framing. However, this difference between CP and AIP framing disappeared for participants who spend a longer time on their choice, because those in the AIP condition are more likely to extract the price difference, replicating the effect of the CP manipulation.

REFERENCES

- Morwitz, V., Greenleaf, E., and Johnson, E. J. (1998). Divide and prosper: consumers’ reaction to partitioned prices. *Journal of Marketing Research*, 35, 453-463.