CHANNEL-BASED PRICE DIFFERENTIATION: DOES IT AFFECT CUSTOMER RETENTION AND IS IT FEASIBLE FOR MOBILE COMMUNICATIONS RETAILERS?

Michael Paul, University of Muenster, Germany
Julia Beckmann, University of Muenster, Germany

SUMMARY

Most firms nowadays use multiple channels to distribute their products and services to customers. Recent studies report that more than 80 percent of U.S. retailers and more than 90 percent of the most successful ones use two or more distribution channels (DMA 2005; Kilcourse and Rowen 2008). Accordingly, more and more research in marketing investigates issues of multichannel management (e.g., Neslin et al. 2006; Neslin and Shankar 2009).

Crucial decisions for every multichannel retailer are whether and how to engage in channel-based price differentiation (Gulati and Garino 2000; Wolk and Ebling 2010). Channel-based price differentiation means setting different prices for the same product across multiple channels (Wolk and Ebling 2010). As a second-degree price differentiation strategy, channel-based price differentiation builds on customer heterogeneous channel preferences who self-select into their preferred channel-price combination (Phlips 1989; Wolk and Ebling 2010). While price differentiation in general promises to increase profitability (Khan and Jain 2005), several researchers and practitioners assume negative effects on customers when it comes to channel-based price differentiation (e.g., Ashcraft 2001; Neslin and Shankar 2009). Given that up to 60 percent of multichannel retailers engage in channel-based price differentiation (Wolk and Ebling 2010), we need to know how customers react toward this type of price differentiation and under which conditions it is feasible.

This study has two objectives. First, we develop and empirically test a conceptual model which identifies four different price instruments for realizing channel-based price differentiation (online discount, online promotion, online clearance, service fee) and specifies their effects on customer perception (perceived value, price unfairness, limited self-determination) and retention outcomes (relationship quality, repurchase intention). Although researchers recognize the opportunity and possible risks of channel-based price differentiation (Cavero, Cebollada, and Salas 1998; Dulleck and Kerschbamer 2005; Dzienziol et al. 2002; Wolk and Ebling 2010; Zettelmeyer 2000), we are not aware of any research that empirically studies its effects on customers. We test the model using a laboratory experiment with 590 participants in which price instruments of a fictitious mobile communication provider are manipulated. Interestingly, we find that channel-based price differentiation positively affects customer retention through perceived value, but negatively impacts retention through price unfairness and limited self-determination. In particular, a service fee in the store channel increases unfairness perceptions and limited self-determination. Overall, we find a positive net effect of price differentiation on customer retention as effects from perceived value on customer retention outcomes are much stronger than those from price unfairness and limited self-determination.

Second, we determine conditions under which channel-based price differentiation is feasible, namely cost and self-selection conditions. Crucial feasibility conditions for channel-based price differentiation are lower operating costs in the channel in which prices are lower and that the right customers self-select into the right channel. The common situation that prices are lower in the Internet than in stores reflects the lower operating costs in the Internet which are due to the lower service level offered (Anderson, Day, and Rangan 1997). Consistent with this, customers which are price-sensitive and do not require personal advice provided by service personnel should choose the Internet, whereas customers which are service-sensitive and willing to pay an extra charge for service should choose the store channel (Iyer and Seetharaman 2003). We formalize conditions in a generalizable manner and apply them to the example of mobile communications. Results show that 5.1 percent lower operating costs are required in the Internet than in the store to ensure profitability and that the right customers are steered to the right channel (i.e., price-sensitive ones to the Internet). However, low price-sensitive customers are steered as well, though to a smaller degree. All in all, findings should encourage multichannel firms to engage in channel-based price differentiation, but they should be aware of its possible ambivalent outcomes depending on which price instruments are used and how they are perceived by customers. References are available upon request.

For further information contact:
Michael Paul
Marketing Center Muenster
University of Muenster
Am Stadtgraben 13–15
48143 Münster
Germany
Phone: +49.251.83.22046
Fax: +49.251.83.22032
E-Mail: michael.paul@uni-muenster.de