

Chapter 3

The Case for Variable Pricing of IDM

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ABSTRACT

This chapter proposes different variable pricing strategies that can be implemented in IDM market-places to increase revenues and consumption of IDM content. Adverse reaction of consumers to price discrimination, where they consider it unfair, is the greatest hindrance to successful application of variable pricing schemes.

INTRODUCTION

Media is being increasingly delivered through and consumed on the Internet via both legal and illegal means in this digital age. Most popular information portals in the initial years of the Internet provided free content and generated revenues through advertising. On the other hand, media companies opposed this practice of providing content for free, with the exception of a few select services like Internet radio. Some industries, like the music

industry, were late in embracing the Internet as a mainstream means of distribution and failed to legally provide content online. Consequently, music industry suffered lost sales opportunities due to piracy and illegal file sharing.

Many research studies claim that online consumers are not used to making payments online and that it is better to earn revenues through advertising. Advertising however, especially in recessionary times, is not adequate to cover costs of producing content and yet leave a profit.

While it is difficult to generate revenues online, Internet also offers unprecedented opportunities

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for employing different pricing schemes (Leyland et al., 2001) to maximize revenue generation. Media companies can use pricing as a strategic tool that can help them build and sustain competitive advantage and protect areas of vulnerability (Stern, 1989). In contrast to other strategic moves, such as new product development or new market penetration, change in pricing schemes requires little investment and can generate quick results.

Media companies have always employed creative pricing techniques to extract maximum possible revenues from consumers. One such technique is the bundling of different items of content (singles for music, articles for newspaper) to cover production and distribution costs. Such an approach helps increase revenues as different consumers place different value on different items in the bundle (Viswanathan & Anandalingam, 2005). Another technique is the use of 'release windows' where the price of content is reduced with the passage of time. This is often legitimized by offering content in a different medium. An example of this practice is the release of books in hardback forms which have a higher price tag compared to paperbacks which are released much later.

Although pricing models for digital media content delivered through internet have evolved considerably from yesteryears when content was delivered through physical media, they still do not fully exploit the opportunities offered by online delivery mechanisms (Waterman, 2001). Many services delivering interactive digital media (IDM) content online are still using fixed or relatively fixed pricing schemes used in the era gone by.

BACKGROUND (PRICING OF IDM CONTENT)

Flat Pricing

Flat rate or fixed pricing schemes refer to charging all the consumers the same price for the me-

dia goods. Sometimes, even different items are charged at the same price. An example of such flat rate pricing is the price of 99 cents per music single offered by iTunes music store till 2008. It later moved to a simple variable pricing structure with three price points.

The major drawback of flat pricing schemes is the lack of price segmentation, i.e. not charging different prices to different user segments. Flat pricing drives away some potential consumers whose prices are higher than they are willing to pay and leaves money on the table in case of high value customers for whom the price is lower than what they are willing to pay.

Variable Pricing

Variable pricing can be defined as a pricing strategy where prices change over time, across consumers, and/or across product bundles (Jayaraman & Baker, 2003). In the e-marketplace, usage related factors such as purchase & usage history and WebPages visited, are used to vary the prices of products (Avlonitis & Indounas, 2006).

Variable pricing is particularly apt for information goods such as IDM as the value derived by consumers is significantly different for different consumers for the same type of content (Viswanathan & Anandalingam, 2005). Variable pricing enables revenue maximization by charging different consumers different prices based on the differences in the value derived by them or their willingness to pay. Variable pricing can also be the weapon against loss of revenues due to piracy, since charging consumers based on their willingness to pay reduces the incentive to resort to illegal means.

Extreme forms of variable pricing in IDM content have become possible due to possibilities offered by online delivery mechanisms:

- **Economics of abundance:** Unlike tangible goods, media content does not deplete with consumption and with falling tech-

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