

Chapter 10

Pricing Model Dynamics in the Chinese Online Game Market

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ABSTRACT

This chapter examines how incumbent firms respond to the industrial pricing dynamics with the adjustment of their own pricing strategies so as to create and sustain their market share dominance. The empirical context of this chapter is the strategic behavior of online game operators (i.e. the companies who operate online games) in the Chinese online game market, one of the most active markets in the world with strong network effects. This chapter introduces Velu's business model theory in the market with strong networks. Further, in this research, the authors extend Velu's research by challenging some of his propositions by a careful observation of pricing dynamics in the Chinese online game industry since 2000 and how dominant and non-dominant incumbent firms adjust their pricing strategy. In the Findings Part, this paper explains why acquisition is regarded by main dominant game operators as the most effective way to complement their pricing model revolution.

INTRODUCTION

Background of the Research Problem

Pricing is generally recognized at the root of company philosophy and a company can be either as a price taker or price maker whose attitude to pricing may be passive or active (Winkler, 1983,

Gabor, 1988). In the discipline of marketing, Product, Price, Promotion and Place (i.e. 4Ps) are often referred to as the key elements of marketing mix. It is generally recognized that among the 4Ps, only price generate income while the rest involves cost (Fletcher & Russell-Jones, 1997). That is why in the competitions for customers, companies always utilise price as a tactical weapon since the effects of price are 'more immediate and direct, and appeals based on price are the easiest to communicate' (Rao, 1984, p. 39). Meanwhile, more

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and more academic and industrial professionals agree that ‘price is a dangerously explosive and complex variable’ (Oxenfeldt, 1973, p. 49). If the price is not right (i.e. too cheap or too dear), all the merchandising effort might be wasted, bring in new-product failure or even decrease the entire industry’s profitability (Gabor, 1988, p.3, Simon, 1992). If prices are too cheap, sales are not problems any more, but the producer will worry how to accrue the profit. If they are too dear, sales will almost certainly suffer, and profits will fall as well (Fletche & Russell-Jones, N., 1997). In terms of this, more and more firms realize that ‘price is a dangerously explosive and complex variable’ and its sufficient importance and complexity merit strategic attention (Oxenfeldt, 1973, p. 49; Dutta et al., 2003).

Apart from the importance of price setting, pricing decisions are the most difficult ones to make in marketing as the company may be (1) subject to government regulations, (2) controlled by a price leader or (3) in the case of a distributor (4) lack kinds of resources needed. All above reasons and other uncertain variables are inter-related and constrained with each other, and even can vary between different pricing situations within the same company (Dorward, 1987, p.1). In addition, environmental pressures such as technology advancement, customers’ increasingly unexpected demand for services and changes in legal and marketing context manifest the delicacy, complexity and importance of pricing.

Previous studies indicate that much academic research attention has been given to the issues of company pricing policy which concentrated on: how customers exchange value for benefit, pricing decision process and analysis of price variable natures and oligopoly pricing (Thaler, 1985; Farley et al., 1980; Monroe & Della Bitta, 1978; Rothschild, 1947). However, few academic attentions were paid to the pricing in managerial practice from the marketing point of view. Oxenfeldt (1973) regarded it as a ‘gap between pricing literature and practice.’ Bonoma et al., (1988, p.359) pointed out that scholars failed to

identify the complexity of price during the previous pricing study, and used to consider it as a single number. Besides, the dearth of published work of empirical study of pricing (Silberston, 1970) failed to win the recognition in practice and did not manage to offer enough advice to practitioners (Simon, 1982, p.23).

Three decades earlier, Monroe and Della Bitta (1978, p. 413) stated that “a lack of descriptive research on pricing practice” can partly explain “the lack of creative development of new approaches to solve marketing problems”. They then called for more qualitative research and more descriptive case studies for pricing study, which gained support from Ingenbleek (2002, pp. 161-162).

Diamantopoulos et al attributed the limited progress of pricing study to the misdirection of conventional price theory which “stimulated a search for end-state, universalistic and categorical explanations rather than contextual factors in an attempt to identify and explain variations in practices” (1991, p.137), while the company policy problems should have to resort to the study of inter-firm and inter-firm variations in pricing with the analysis of data collected at multiple organizational levels.

With the aim to turning theoretical pricing into more complex and more realistic, Dutta et al (2003) made efforts to overcome the above limitations. Their main contribution is the development of a resource-based perspective of the process by which prices in companies are determined. They suggest that pricing is a capability “which involves both capturing value and balancing competing interests within the firm”. Their conclusion is that value creating resources firms should compete by investing in value-capturing resources. Following this resource-advantage theory, Ingenbleek (2002, p. 151) also explored how firms can develop successful pricing practice. He deducted that “value extraction is rooted in value creation except in markets with high demand uncertainty. In these markets capturing value is rooted in customer orientation.”

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