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Differentiating Subjective and Objective Product Attributes For Pricing Experience Products:

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Differentiating Subjective and Objective Product Attributes For Pricing Experience Products:

Abstract: *Innovative experiences have been created by designers, architects and artists. These are being combined with foods and services in restaurant industry to deliver a unique experience. These experience products are often combination of subjective and objective attributes. Consumers' willingness to pay for experience products come from evaluation of both subjective and objective attributes. However there is no structured approach to find the willingness to pay of customers for subjective and objective attributes separately of an experience product. This research adopts categorical hybrid conjoint analysis for pricing such experiences in the context of restaurant industry. The research considers 13 attributes and 40 attribute levels under four facets. Data collected from 135 respondents in India. The unique finding of the research is that the customers have separate utility for subjective and objective attributes of a product and they are ready to pay significant premium for subjective attributes over objective attributes. It is also found that there is sufficient scope for the marketers to redesign experience product by combining different proportion of subjective and objective attributes to offer experience products. An optimal bundle of experience is obtained and price of the bundle is derived.*

Key Words: Subjective and objective attributes, Experience product, Price bundling, Hybrid conjoint.

Introduction

In this emerging economy, as suggested by Pine and Gilmore (1999), experience represents an 'unarticulated, still effective genre of business surplus'. Many organizations are striving in new economy due to severe competition and less barrier to entry in most of the industries. Whether an organization delivers service-product or product-service, a good amount of experience part is associated with it. When experience offering is considered to be independent from service, it gives enormous, still sustainable economic expansion for organizations struggling in declining industrial base. While goods, service are external to the buyers; experience is in buyer's mind who are engaged on an emotional level. For example, when we go to restaurant only to take food, we associate utility with some service component like the way it is served, time taken to deliver the food, price and few others. However, when the same restaurant stages an experience in terms of external and internal ambiance, food specialty, and some other attributes that cater to consumers' esteem needs in Maslow's need hierarchy, it becomes a distinct offering from good, product or service.

Previous research on designing new product considered objective attributes of products. This paucity of research considering subjective attributes of products might have caused limitation in unit level parameter estimation as large variation in individual's perception about subjective attributes called for individual specific analysis. At the same time, it is to be noted that selection of a product is not only made because of its objective characteristics; subjective product characteristics also play a significant role in consumer decision making (Luo, Kannan and Ratchford, 2008). This research tries to find out customers preference to pay premium for an offering that contains both subjective and objective characteristics and delivers sensory experience.

Objective of the study

A related problem in pricing of experience product having both subjective and objective attributes is the bundling of several subjective attributes (Goldberg, Green and Wind, 1984). Objective of this study is to find optimum bundle of subjective and objective attributes of experience product and the premium customers want to pay for such bundle. Another objective associated with this research is to test whether there is sufficient move of the consumers for an experience offering.

User of the study

This study is useful both to the practitioners and academicians. Industry will be able to implement the pricing method while delivering sensory experience along with basic services. Similar pricing method can be applied in other experience products like theme park, shopping mall, fast food chains, airline, coffee shops etc. At the same time this research will be of immense help to the academicians as this will pave a way towards structured approach in pricing experience product.

Literature Review

Previous research has recognized the role of subjective features of products as influencer in consumer purchase decision in very limited way (Luo, Kannan and Ratchford 2008, Lawton 2006). Luo, Kannan and Ratchford (2008) considered subjective attributes as latent construct in their model.

Pricing research in service industry does not depend much on economics and accounting theories (Schlissel and Chasin, 1991). The reason that pricing of services follows a special aspect of marketing theory is its relatively intangible constituents (Lovelock, 1981). Previous literatures have shown that absorption or cost plus pricing becomes ineffective for profit maximization due to such intangibility factor (Goldberg, Green and Wind, 1984). Selling price derived from such method is less likely to reach

consumers reservation price or competition's price. Another specialty in pricing research is information asymmetry. If consumer is unable to identify the product quality and differentiated attributes, they rely on average quality of the attributes (Nagle, 1984). It is rather more dominant in pricing of services as one can see the quality of service only when it is delivered. Wilson (1980) found that consumer will be more towards price-quality effect when they have less information about the product. Hence price competition has less effect as the intangibility increases in service than that of a tangible product.

Interaction between service providers and consumers is another aspect in service delivery and hence demand and supply conditions differ over local market which in turn tender more fragmented market structure (Taylor, 1972). Services are produced and consumed simultaneously. This consumption point production may not directly affect the pricing mechanism of services, but it does lead to restructuring subjectyive and objective attributes of service products to suit different consumers based on personal interaction at the point of delivery. Consequently, delivered services include several modifications based on the requirement of better half of consumer-producer dyad. There is inbuilt variability in service production for different consumers and accordingly cost of production varies. In contrast, experience, although do stimulate different customers differently, often standardized to deliver a particular theme or sensory memorabilia. Potentiality for maximizing customer satisfaction is high because it relies upon creativity, skill and personality of service producers. People, creativity and delivery trio provide an insuperable competitive advantage to the producers, but cost structure will be high (Groth 1995, 1995a).

Above literature entails that pricing of experience should be treated differently from pricing of tangible goods or intangible services. Academic research has encountered considerable growth of economic literature on utility theory and bundling of attributes during last couple of decades (Phillip 1981). Adams and Yellen (1976), identified three bundling strategy namely unbundled sales, where individual components used to be sold; mixed bundling strategy where both bundle as well as individual components are offered and full bundling strategy where only bundles are offered. In the bundle of experience in restaurant can be offered as third category. Bundle pricing is a wide spread phenomenon, however, very little is known about how to find optimal bundle price (Hanson and Martin, 1990). Stigler (1963), one of the researchers who pioneered price bundling approach, represented the demand as

dedicated customer segments. According to Stigler, customer will choose the product which maximizes individual surplus which is the difference between his reservation price and product price. However, capturing reservation price of experience memorabilia is quite intricate and ineffective. This is because describing experience attributes to the consumers in its actual form of full bundle is extremely difficult, if not impossible. Consequently, it leads to different perception of different consumers and becomes inadequate to capture actual reservation price.

Hybrid conjoint model (Green et al, 1981) is developed to cope with similar kind of price bundling issues. However, a constraint in handling price issue through conjoint is price-attribute correlation (Green and Srinivasan, 1978). At the same time, ignoring such correlation by making price levels independent of other attributes may lead to unrealistic attribute profile. An examples of such correlated attribute and bundling problem is pricing of experience in restaurant offering. Consumers believe that every additional sensory feeling will cost some premium over the basic price that a restaurant charges from a consumer. Hybrid conjoint analysis refers to streamline the data collection task while preserving individual differences in utility functions (Wind et al. 1989). Hybrid conjoint adopts old idea of self explicated utility of each respondent (Wilkie and Pessemier, 1973). In categorical conjoint analysis (Carol 1973) respondent has the option to give his response in discrete categories. Categories may be in nominal scale or ordinal scale. This fits the data well in conjoint analysis because the scale values of independent variables minimally correlates among them (Goldberg, Green and Wind 1982, Akaah and Korgaonkar 1983).

Methodology

The research methodology followed in this research is Categorical hybrid conjoint analysis (Goldbarg . Green and Wind, 1984).

Hybrid Conjoint Model

Pricing research recommend individual based preference data. Indeed, when the number of attributes and levels are small and well categorized, the traditional full profile conjoint analysis can be effective (Pallman et al. 1999). However, conjoint methodology is being used more extensively in commercial research where the numbers of attributes are larger and the levels within any attribute are more (Willin and Cattin 1989). Further, it is required to consider interaction effects (Louviere et al. 2000) along with main effects, particularly when the product classes are largely constituted with sensory, aesthetics and other intangible facets (Green, Goldberg and Montemayor,

1981). This trend has consequently necessitated estimation of more parameters and number of data points has increased. This has, in turn, increased interviewing complexity and time. Green and DeSarbo (1979) proposed componential segmentation method incorporating respondent parameters in the utility function.

Mathematical Model

This section describes mathematical form of the categorical hybrid conjoint model (Green and Krieger, 1996) and explain the procedure of fitting the data in the model.

Self-Explicated Model

First and second phase of proposed model deals with the procedure of self explicated utility model (Huber, Sahney and Ford 1969). Self-explicated model in this research follows following steps:

- Let F be the number of facets that define the set of restaurant experience profiles. Each of the facet (f) has m_f (m = 1,M) attributes. Let level l_{fm} (l = 1,L) be the levels of attribute m in facet f. Suppose that there are N number of total respondents and respondent (n) has given response of their self-explicated utilities of level (l) of attribute (m) under facet (f) which is defined as $u_{fml}^{(n)}$ one at a time. The respondents give their response of self-explicated utilities in categorical scale.
- In the second phase, the respondents are asked to give their relative importance of all m_f attributes under facet f in a 100 point summated scale. Higher value of scale denotes higher importance to that respondent. Weightage of each attribute given by respondent n is denoted by $w_{fm}^{(n)}$.

Hence we can express the utility of respondent n (n = 1,N) for alternative profile r

$$U_r^{(n)} = \sum_{m=1}^{M} w_{fm}^{(n)} \sum_{l=1}^{L} u_{fml}^{(n)} I_{rml}^{(n)}$$

$I_{rml}^{(n)}$ = 1 if level l of attribute m is present in the profile r

= 0 if otherwise.

The above model is compositional as each of the components i.e. importance and desirability are measured directly from the respondents and utilities are derived (Akaah and Korgaonkar, 1983).

The Hybrid Conjoint Model

A master and typically orthogonal experimental design of Q full profiles is designed using statistical software. Each product profile is expressed by a set of levels and q-th (q = 1,Q) stimulus profile which is a product description and is expressed by a vector:

$$\mathbf{X^{(q)}} = [X_{l1}^{(q)}, X_{l2}^{(q)}, \ldots\ldots, X_{lm}^{(q)}]$$

$X_{lm}^{(q)}$ denotes level l of attribute m in profile q. In this case, attribute levels are discrete values and presented through dummies. Each individual receives R profiles where R€Q and ideally range between five to seven profiles. An evaluation score Y_r is obtained through a 10 point rating scale for the r-th full profile (r = 1,R) received by individual n. Higher score represents higher likelihood of purchase by the respondent n and is assumed that it gives higher utility to the respondent.

This research considers main effect and two way interaction effects between selected attributes. Interaction attributes are chosen based on focus group interviews and related literature. Let us denote v_{lm} as main effect of level l of attribute m and $t_{lm.l(m+1}$ is two way interaction effects between two attributes. Two consecutive attributes are considered for two way interaction and is represented as (m, m+1). In line with the argument of hybrid conjoint analysis, this research assumes that both main effect and selected two way interaction effect will explain residual variance when we regress Y_r on Us.

Considering only the main effect and two way selected interaction effect, the response of r-th alternative is given by

$$Y_r \cong \sum_{m=1}^{M} v_{lm} + \sum_{m=m+1} t_{lm.l(m+1)}$$

The study considers three interaction effects (as explained by Louviere et al. 2000). It does not consider three way interaction for simplicity and reduction of manual effort in data analysis of such huge conjoint model. However, there can be significant contribution of three way interaction in experience industry where utility of one attribute may be related to other two attributes. In the above equation, stimulus profile is expressed through dummy variable for parameters estimation.

Hybrid model combines both self-explicated part-worth and regression derived part-worth (Lepak and Considine, 2001). The utility matrix of order N X D for N respondents was obtained and then row centered to minimize response bias problem and express deviation from their individual mean. The hybrid model parameters are then estimated and ordinary least square regression is used for the said purpose. Since

respondents evaluated intension to buy (in this case going to the restaurants) is expressed as Y_r the mathematical hybrid model is framed for this purpose is as follows:

$$Y_r = Y_{1\,(1,2,3.....M)} \cong \beta_0 + \beta_1 U_{1,2,3...M} + \sum_{m=1}^{M} v_{lm} + \sum_{m=m+1} t_{lm.l(m+1)}$$

Where each $U_{1,2,3...M}$ is separately computed as represented in N X D. Matrix. β_0 is intercept and β_1 is regression parameter that represent strength and relation of self-explicated utilities to Y.

In this hybrid model, we combine both self-explicated part-worth and regression obtained part-worth as per above model. For the phase-I response, we convert the predictor variables in (l_m-1) dummy variable for each set of l_m attribute level of attribute 'm'. Since the part worth function is measured in interval scale that has common unit but arbitrary origin, we are free to set lowest part worth at zero. Hence, derived partworth of any level is the actual part-worth but the difference between that particular level part-worth and lowest level part-worth. As suggested by Goldberg, Green and Wing (1984), we have normalized the result under each facet to compare the part worth across facets and the range from 0 to 10. Total four facets with 13 attributes are involved in the analysis.

Facets, attributes and levels of this research

Four focus group interviews of six members each is carried out to find out the preferred attributes and levels of restaurant offering that consumers prefer. Facet wise attributes and its levels (number shown in parenthesis) are given below.

CONSTRUCTION: Outdoor construction (3), Indoor construction (3), Landscaping (3), Size (3), Location (3).

AMBIENCE: Indoor environment (5), Outdoor environment (4), Table spacing (3)

FOOD: Preparation (4), Chef (3)

SERVICE: Attendant (3), Waiting arrangement (3)

Data Collection

Data for this research is collected from those respondents who visit restaurants for dinner at least once in two months. 135 samples are collected through personal interviews. Photographs of several attributes and levels are shown to the respondents to explain the attributes and levels. The data collection is administrated in three phases. After the introduction, respondent's preference for restaurant experience is captured. Each respondent, in the first phase, received four cards depicting the attributes within each facet. They provided responses in 3 point categorical scale (most preferred,

acceptable and least preferred). In phase –II, the importance of the attribute is captured in a 100 point summated scale. In phase – III, five full profile cards are given to the respondents to rate their purchase intention in 1-10 scale. All these full profiles contain price of the experience product. Price of each profile is calculated by summing up each attribute's minimum base price and premium of the level that is presented in the profile.

Analysis

Statistical software namely SPSS 13.0 and SAS 9.0 are used for the analysis. The analysis is carried out in four phases are as per following steps:

1. In the first phase of the analysis, utilities of 40 attribute levels of 135 respondents are calculated. Hence, the utility matrix is a 135 X 40 matrix. This matrix is row centered so that sum of utilities of all levels in each attribute for every individual respondent is equal to zero. All the part worth is scaled such a way that minimum utility within each facet will be at zero and the maximum will be at 10.
2. In phase –II, self-explicated utility of each respondent is calculated by multiplying individual weights of each attribute with the utilities of first phase. This matrix is then used as predictor variable for phase-III calculations.
3. Parameters for regression equations are then calculated (i.e. intercept and slope of the utility function) .Parameters for both main effect and interaction effect are also calculated simultaneously.
4. Least square residuals of the regression equation is then computed to examine the price effect. This residual is regressed on total full profile experience price that is shown to the respondents with phase-III full profile cards.

Results and discussion:

Results of the analysis are interpreted on the basis of research objectives and specific analytical steps as described earlier. Canonical correlation between set of criterion variable and set of predictor variables are analyzed to comment on degree of correlation between prices and attribute bundle. It is found that there is high correlation while analyzing variables under subjective facet 'Ambiance' (0.89), however facets, which are objective in nature namely 'construction', 'service' and 'food' have moderate correlation (0.68, 0.72 and 0.65 respectively). All the correlation coefficients except for service are significant at 1% level. Moderate to high canonical correlation suggest that there is an ordinal change between three categories of the dependent variables (i.e. most preferred, acceptable and least preferred). However this finding does not say anything about the distance between these three categories. Normalized canonical regression coefficient is analyzed to get between category distances. Table -1 shows normalized

canonical regression coefficients for four facets. 'Acceptable' categoriy of all three facets other than service are very close to normalized value of 'most preferred' category. This signifies that consumers are inclined to have higher subjective characteristics of experience product and not ready to settle in lower levels of experience attributes.

TABLE – 1: Normalized scale value from canonical regression coefficient

Facets	Most Preferred	Acceptable
Construction	1.00	.89
Ambience	1.00	.95
Service	1.00	.72
Food	1.00	.95

Constant sum results of facet importance data are analyzed for camparison between facets. Food is given highest importance (40%) followed by ambience (23%) and service (22.5%). Construction takes relatively low importance (14.5%) while explaining experience attributes.

Part-worth results for each facet are derived and interpreted. Optimum utility bundle is derived from maximum desired part-worth and respective price is derived by adding corresponding premium with the base price.

Following table shows that part worth (canonical regression coefficients) of most preferred levels of all attributes.

Experience Description	Part worth	Price Premium (RS)
Oval / octagonal/ unusual shape of construction (Objective characteristic)	1.02	30
One side unrestricted view of outdoor garden (Subjective characteristic)	0.89	20
Outdoor landscape with garden (subjective characteristic)	0.9	20
Medium size cozy (subjective characteristic)	1.12	30
4 Km from the center of the city	.89	20
Exclusively decorated with sensational light and soft music + some fun for all (subjective characteristic)	2.46	40
Sensational lighting to create theme environment (subjective characteristic)	2.45	25

Table spaced 4.5 feet with 4 persons sitting arrangement (Objective characteristic)	3.24	25
One girl to take order and serve	2.96	40
Waiting arrangement in the garden with snack joint (subjective characteristic)	2.99	50
Rare dishes with advance order along with multi-cuisine (subjective characteristic)	2.54	50
Chef from 3 star hotel (Objective characteristic)	0.9	20
Total Additional Premium over base price Rs. 400/- ($10)		320 ($8)

The study suggest that people are ready to pay approximately 80% premium over the price of restaurant to buy experience product. As the self explicated study design While basic restaurant services (which was stated in self explicated cards as the first level with zero premium) offer a full range of restaurant amenities, attributes does not any eRespondents prefer to pay such premium to associate themselves at different levels of experience in restaurant offering.

Further research

Experience economy is growing day by day. Similar research can be done in other services that deliver experiences. Industries like airline, theme park, theatre etc are contemporary for experience research. The method described here may be applied to these wide varieties of industries that deals with product having both subjective and objective characteristics. Considering the methodological perspective, one can use Stepwise Multinomial Logit Analysis as a fitting procedure to analyze categorical data. Hierarchical Bayes methodology is another methodological perspective. Researchers can model individual level heterogeneity through HB and segment the market based on certain underlying dimension like price sensitivity.

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