

Final Exam: 15:818

Extract from "With Select Apps, iPad is More Than a Pretty Face", New York Times, April 2010

Travelers can download 1,000 Experiences from Lonely Planet (\$10), a graphically rich look at a wide variety of trips. Lonely Planet cut the price for its app in half after a few days, which is a telling development. iPad developers started with prices that were often much higher than iPhone versions of the same software, based on logic that no one has yet unearthed. As competition builds in the App Store, that logic should fade quickly.

Additional Background facts to the case:

6 weeks after the launch of the iPad:

- 1 million iPads and 85 million iPhone devices had been sold in total.
- There were 196,000 iPhone applications and 5,700 native iPad applications

People can use iPhone applications on their iPads but the resolution is not as good as an iPad application.

Both iPhone and iPad applications are displayed in the application store in order of their popularity, so that the most popular application is always the first one that any customer sees.

Specific Data for Case:

These data cover the first 6 weeks after the launch of the iPad, for an application that allows users to access information and reviews about restaurants in cities across the US on their iPad and iPhone.

	iPad Price	iPad Downloads	iPhone Price	iPhone Downloads
Week 1	9.99	700	0.99	10,500
Week 2	9.99	500	1.99	1500
Week 3	4.99	1200	1.99	700
Week 4	4.99	1000	0.99	9,000
Week 5	2.99	1200	2.99	1000
Week 6	2.99	1000	2.99	900

Questions [Total 28 points]

1) Calculate the price elasticity for both the iPad application and the iPhone application, using the Excel "slope" methodology we covered in class. [2 points]

iPad: -.53

iPhone: -2.22

2) How would you explain the difference between the elasticity for the iPad and the iPhone application? [4 points]

Ultimately all the people who are price sensitive will buy the iPhone application and suffer the bad resolution.

iPad users are likely to be wealthier (it has a higher purchase price) meaning the purchase is a smaller proportion of their income.

There are fewer competitive applications meaning that there is a larger buffer in terms of differentiation value for the iPad application.

3) Do you agree with the New York Times when it says that the decision to price iPad applications higher than iPhone applications was "based on logic that no one has yet unearthed"? Why or why not? [2 points]

No. Makes a lot of sense given the price elasticities which the application developers could have easily anticipated. The logic is simple "value-based pricing" rather than cost-based pricing.

4) Calculate the price elasticity of the iPad application in weeks 1-3 and then again in weeks 4-6. How would you explain the difference, if any? You are welcome to list multiple explanations. [6 points]

Week 1-3	-1.01	-3.33
Week 4-6	-0.17	-2.03

The price change between 9.99 and 4.99 takes the application from being potentially a purchase that is perceived as a luxury to something discretionary. The price change between 4.99 and 2.99 may have felt small enough to not be meaningful in terms of influencing customer behavior (due to proportional price perceptions). It could also be that customers were educated by their previous experience with low priced iPhone applications that \$9.99 was just an 'unjust' price.

Also, it is possible that in Weeks 1-3 people were buying many different applications for their newly bought iPad and were consequently price sensitive, but the purchases in week 4-6 were just people who really needed a restaurant application.

There is also reasonably limited data. This may explain a rather surprising result, since we usually expect price sensitivity to go down over time. There also many have been limitations in how many iPad application could have been sold in the first week.

It could be that the fact the price was so much higher than the iPhone application made customer very resistant to price segmentation as it wasn't perceived as "fair". When the price came down this fairness issue was less salient.

They may have been also some form of network effects going on. Either the product needed "user based content" to be useful. Or it could be that it got enough downloads eventually to be featured in Apple's bestseller list meaning that customers perceived higher quality.

5) Do you agree with the statement, "As competition builds in the App Store, that logic [pricing higher on iPad applications than iPhone applications] should fade quickly."? Why or why not? [6 points]

iPad buyers are still likely to be wealthier and ultimately less price sensitive. It is difficult to see how that will go away.

However, competition in this market will be particularly ruthless because of Apple's decision to rank applications by popularity. This creates a winner takes all market and competitors may simply undercut prices and ignore the characteristics of their customers. If the NYT is silly enough to say that there is not rationale for segmenting the iPhone/iPad market there are bound to be even sillier competitors out there.

6) Do you think that product-based price segmentation is possible here? How would you adjust the iPad application to price-segment the iPad application market? [Remember the methodology we used in class.] [8 points]

Choose an aspect of the iPad application such as:

- coverage of high-end restaurants

- recency and coverage of the reviews

- Guaranteed reservations at these restaurants

That are likely to be related to whether or not an individual has an overall high EVC for a restaurant review application.

Create one version at "\$9.99" that has these features, and then mid-range version which has limited features (perhaps at 4.99 or lower), and then finally a low end version that does not have these features (perhaps at 2.99). Make sure to communicate the differentiation value so that people do not feel that the segmentation is unfair. Remember it is all about self-selection!

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