International Marketing

BMA6100-20

Pricing in International Markets and Terms of Doing Business

Summary of the previous lecture

- We have now discussed all forms of market entry mode : Export, Intermediate and Hierarchical.
- Two more topics to go.... Pricing & Distribution Decisions.

What is in this lecture?

- To discuss the stages in setting export pricing.
- To define incoterms, and how it works in international trade.
- To discuss methods of payment in international trade.

Export Pricing Approaches

- Standard worldwide price- regardless of buyer’s location in the market(s)
- Cost-oriented pricing
  - Dual pricing differentiates between domestic and export prices
    - Cost-plus method allocates domestic and foreign costs to the product.
    - Marginal cost method considers direct costs of producing and selling exports as floor (lowest) price.
- Market-differentiated pricing
  - based on the dynamics of the marketplace
  - changes in competition, exchange rates, etc.

EXHIBIT 11.3

Export pricing alternatives

Production Costs	*Standard*	*Cost Plus*	*Marginal Cost*
Materials	2.00	2.00	2.00
Fixed costs	1.00	1.00	0.00
Additional foreign product costs	0.00	0.10	0.10
Production overhead	0.50	0.50	0.00
Total production costs	3.50	3.60	2.10
U.S. marketing costs	1.50	0.00	0.00
General and administrative	0.75	0.75	0.00
Foreign marketing	0.00	1.00	1.00
Other foreign costs	0.00	1.25	1.25
Subtotal	5.75	6.60	4.35
Profit margin (25%)	1.44	1.65	1.09
Selling price	7.19	8.25	5.44

Source: Adapted from Lee Oster, "Accounting for Exporters," *Export Today* 7 (January 1991): 28–33.

Export related costs

- **Export-related costs**
  - Cost of modifying a product for a foreign market
  - Operational costs of exporting
  - Cost incurred in entering the foreign market
- **Price escalation for exports results from**
  - Clear-cut and hidden costs
- **Methods for combating price escalation**
  - Reorganize the channel of distribution
  - Product adaptation
  - Change tariff or tax classifications
  - Overseas assembly or production

Terms of sale

- Incoterms are the internationally accepted standard definitions for terms of sale set by the International Chamber of Commerce (ICC) since 1936.
- They are a set of rules which define the responsibilities of sellers and buyers for the delivery of goods under sales contracts for domestic and international trade
- https://www.trade.gov/know-your-incoterms

Incoterms (Group 1)

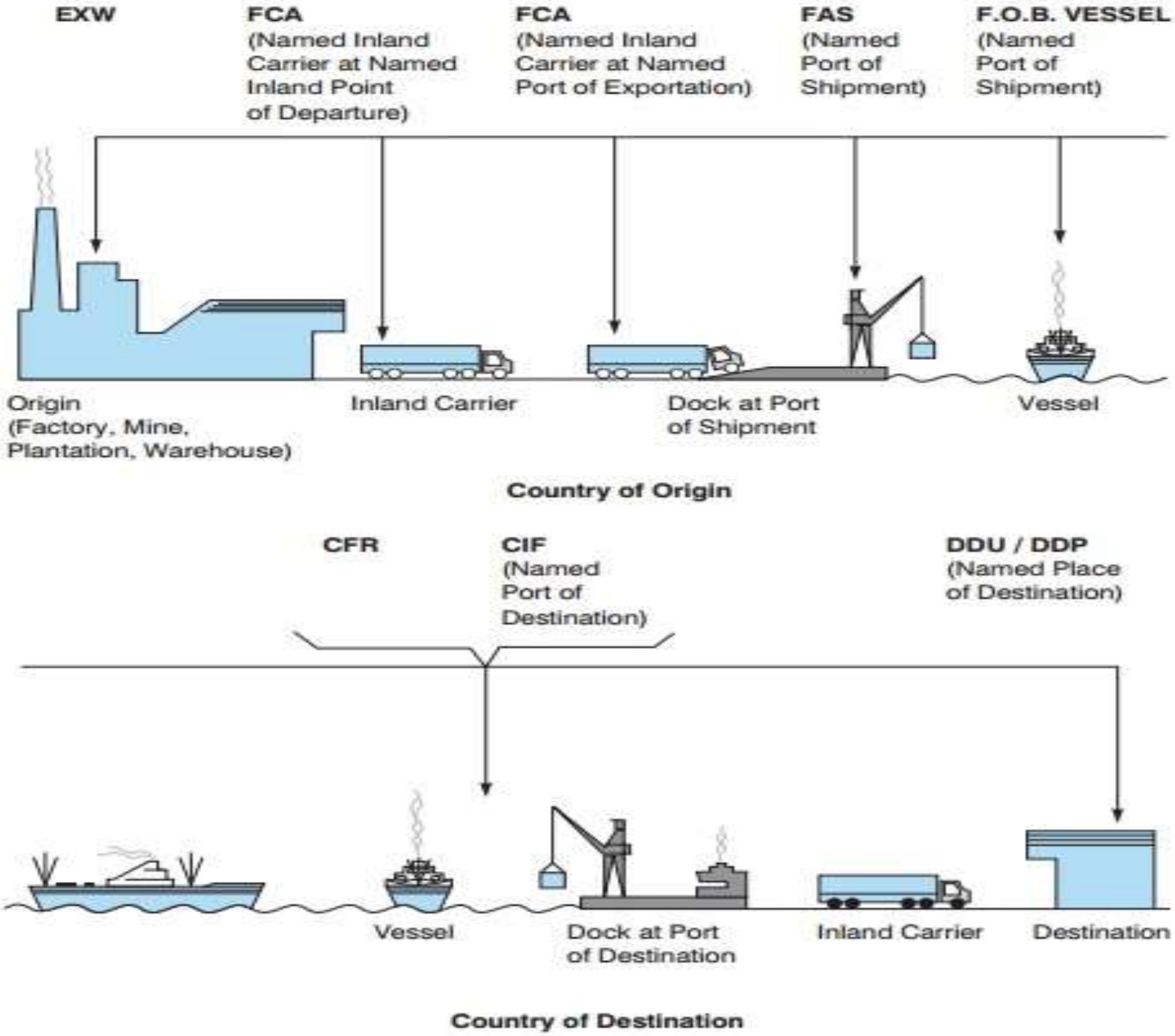
- Group 1. Incoterms® that apply to any mode of transport are:
- EXW: Ex Works
- FCA: Free Carrier
- CPT: Carriage Paid To
- CIP: Carriage and Insurance Paid To
- DAT: Delivered at Terminal
- DAP: Delivered at Place
- DDP: Delivered Duty Paid

Incoterm (Group 2)

- Group 2. Incoterms® that apply to sea and inland waterway transport only:
- FAS: Free Alongside Ship
- FOB: Free on Board
- CFR: Cost and Freight
- CIF: Cost, Insurance, and Freight

EXHIBIT 11.6

Selected trade terms (Incoterms)



Terms of payment

- Cash in Advance
- Letter of Credit
- Documents against payment
- Documents against acceptance
- Open account
- Consignment

Cash in Advance

- A method of payment for exported goods: The most favourable term to the exporter; not widely used, except for smaller, custom orders, or first-time transactions, or situations in which the exporter has reason to doubt the importer's ability to pay.

Letter of credit (L/C)

- An instrument issued by a bank at the request of buyer. The bank promises to pay a specified amount on presentation of documents stipulated in the letter of credit, usually the bill of lading, consular invoice (or proforma) and a description of goods.

- Bill of Lading (BOL) is a document issued by a carrier which details a shipment of merchandise.

Types of L/C

- **Irrevocable vs. revocable:** In the case of irrevocable, the L/C can not be modified without the consent of the exporter.
- **Confirmed vs. unconfirmed:** In the case of U.S exporter, a U.S bank might assess the risk of L/C and reconfirm it.
- **Revolving vs. no-revolving:** In the case of non-revolving, the L/C is valid only for one transaction.

Documents against payment (DP)

- In order to obtain shipping **documents,** a buyer is required to **pay** a seller's sight draft .
- The bank presents the sight draft to the buyer, usually one or two weeks after shipment, and then payment must be made.

Open account

- A method of payment in international trade where the exporter ships the goods before payment is due.
- It is advantageous for importer but risky for exporter.

Consignment

- It is a method of selling in which the buyer (importer) defers the payment until the products are actually sold.
- Very risky for exporter.

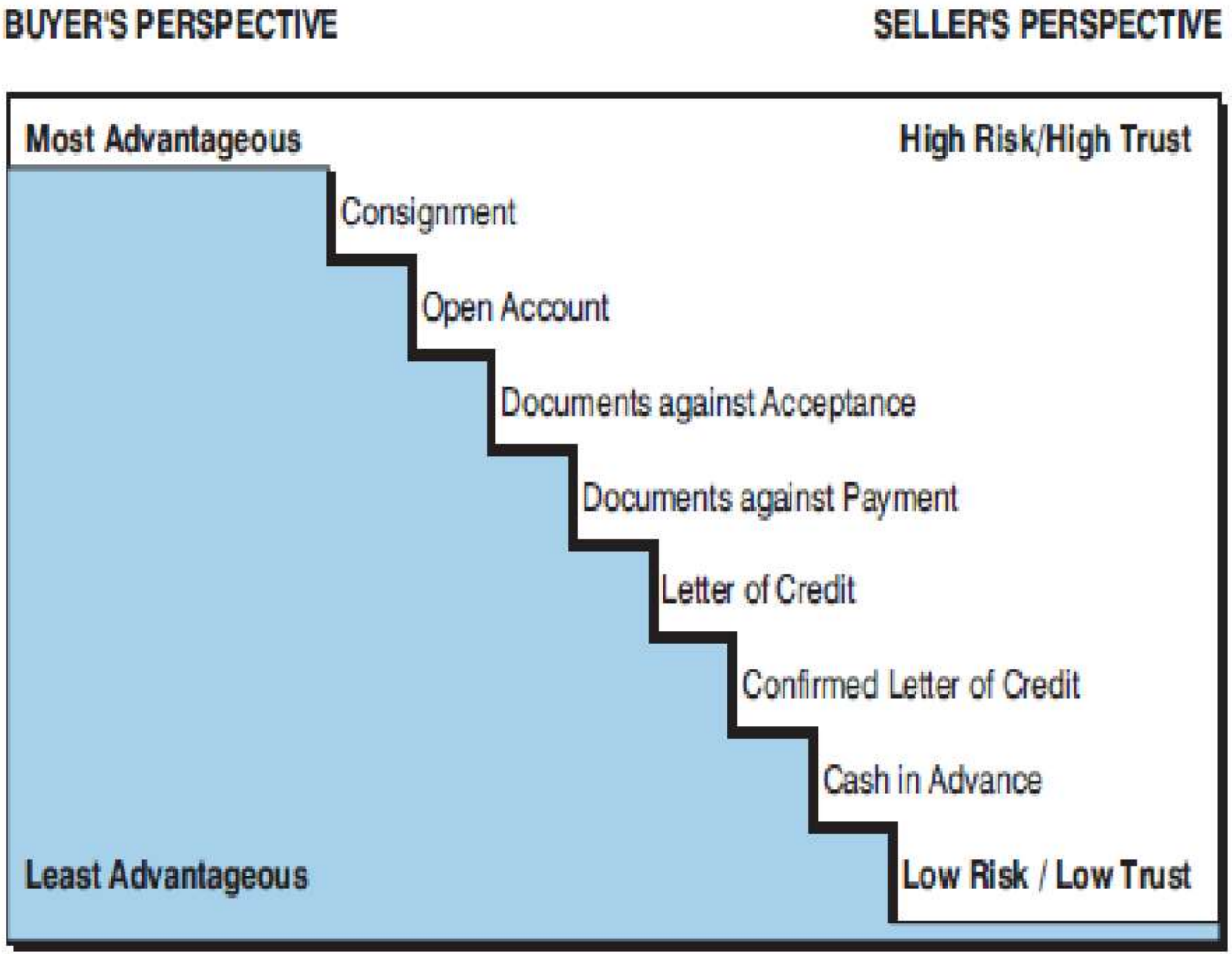


EXHIBIT 11.7

Methods of payment for exports

Source: Adapted from Chase Manhattan Bank, *Dynamics of Trade Finance* (New York: Chase Manhattan Bank, 1984), 5.