Full Length Research Paper

Pricing of Banking Products and Services: A Case Study of Commercial Banks in Zimbabwe

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This paper reports on the findings of a study which was conducted to establish the factors that influence prices of bank products and services and investigate the pricing strategies used by commercial banks in Zimbabwe. The research was also intended to establish the challenges that are being faced by banks in Zimbabwe. The research used a sample of 10 commercial banks which were randomly selected in Harare. Data was collected using questionnaires and interviews and presented using tables and graphs. The research found out that pricing of bank products was mainly influenced by the profit motive, competition and the need to abide by regulations. Strategies used to set prices were cost and competition based as well as dictated by market trends. It was also established from the research that challenges faced by banks were loss of customer confidence, stiff competition and failure by the Central bank to perform the role of lender of last resort. The study recommended that there is need to take into consideration various factors in pricing bank products so as to cater for both the institutional and individual customers. Optimal pricing is pivotal in ensuring that banks remain in business and achieve set objectives. Further research on the effect of the multi currency system on pricing of bank products were recommended.

Key words: Bank, Pricing, Products, Services, Customers

INTRODUCTION

Banking institutions play an integral part in the economic development and growth of any economy. They are the vehicle through which an economy drives growth through channeling funds from the surplus units of the economy to the deficit units in the economy. Thus government and regulators have sought to maintain stability and soundness of financial systems in order to achieve both economic objectives and social outcomes.

Zimbabwe’s financial services sector has witnessed phenomenal growth since economic deregulation in 1991 (Muranda, 2006). A consequence of deregulation has been a dramatic increase in competition in the financial services sector. New entrants in the sector comprise of financial institutions whose shareholding is mainly indigenous and domestic. Financial deregulation has resulted in the removal of entry barriers leading to increased competition. This also allowed banks some latitude to operate in non-core services. The increased competition resulted in the introduction of new products and services such as e-banking and store banking.

The financial sector reforms introduced in 1991 entailed the removal of market-segmentation and facilitated the entry of more institutions into the sector. The period 1991 to 2000 was characterized by dynamic change in Zimbabwe’s banking sector. The reforms undertaken during this period led to the entry into the market of several commercial banks, discount houses and asset management companies. The entry was sudden and appeared to be anchored on a laissez faire policy of bank license approvals. No prior diligence appeared to have been conducted on license applicants.

The liberalisation was also designed to move the economy away from an inefficient and monopolistic private sector, which hardly paid any attention to sound corporate governance. The reforms also led to a review of strategy and operations in areas such as loan...
The research sought to answer the following questions: 1) What factors influence the pricing of bank products? 2) What pricing strategies are being used by commercial banks to price their products and services? 3) What challenges in pricing are being faced by commercial banks in Zimbabwe?

LITERATURE REVIEW

Price in the eyes of consumers is the evaluation of the total product offering which includes the brand name, package, product benefits, service delivery, credit extended etc. Price affects the cost and also plays a key role in decision making of the buyers (customers).

Pricing affects sales volume, profit margin, rate of return on investment, product position and the image of the organization. Kucher (2010) states that pricing in the banking industry today is often focused on the company’s own costs or the competitor’s price. He went on to say that in contrast, the customer’s perception of value and their expectations are given little regard, money is given away due to inadequate value extraction in pricing banking services. Financial services value pricing focuses on determining the willingness to pay of different customer segments and setting the price accordingly.

Factors influencing the pricing of bank products

Rose (2008) asserts that in pricing services banks are caught between attracting, holding funds and also avoid paying an interest that is costly to erode any potential to make profit. Different aspects are put into consideration to bring about a price for different products and services. Pricing is important because it can be strategically used as a tool to meet or reduce the competition. According to Winston (1986), pricing of financial products is highly complex involving internal and external factors. The factors that influence the calculation of bank services pricing are depicted below:

Company objectives

The pricing strategy to be adopted depends upon the objectives of the company. Pezzullo (1998) states that the pricing of bank products directly affects the bank’s profitability in two ways. Firstly the price paid by customers generates income and secondly price influences the volume of sales. Certina and Mohail (2007) state that the objectives that can be set a company can be growth in sales, market share, competition, predetermined profit and corporate objectives to have a payback period in a specific period.

Legal restrictions and regulations

According to Wuebker et al (2008), regulation is increasing its influence on the pricing of financial services. Since 2003 the Swiss Investment fund Association (SFA) has required its members to include a total Expenses ratio (TER) in any investment price quote. In the UK, the Office of Fair Trade has increased levels of intervention on the UK finance service market.

Governments manage economies to achieve key economic objectives using monetary policy, fiscal policy and supply side policy. A review carried out by Calomiries (2008) shows substantial empirical evidence that when monetary policy is accommodative banks
charge less for bearing risk, and this seems to be a pattern common to many countries.

**Competition**

To face competition, prices can be lowered to maintain sales or in the absence of it, prices can be revised but stable prices help in maintaining image or brand name and quality. Tirole (1998) observed that new entrants significantly undercut prices of established banks and have already influenced pricing of banking products. Ennew and Waite (2007) stated that in some respect, competition has less influence in the pricing of financial services stating that the complexity and lack of transparency of financial services pricing acts as inhibitors to highly competitive pricing. Schaeck and Cilak (2008) argue that strong competition implies significantly lower spreads between bank and market interest rate for most market products in line with expectations. A number of studies by Berger and Hannan (1989), Neumark and Shapiro (1992) and Okeahalam (1998), support the Structure Conduct Performance (SCP) framework. The framework assumes that measurements of market structure and concentration can provide reliable deductions regarding the extent of competition. The extent of how competition affects the price that consumers pay for banking services, determines the level of profits and performance. The SCP framework suggests that higher concentration leads to higher prices, which in turn lead to higher profits.

Llewellyn and Drake (1993) relates charging in the UK where competitive pressures have forced banks to pay interest on a larger proportion of deposits (including current accounts) and the general policy is for a tiered structure of interest rates to be applied. Thus small balances carry low rates of interest while larger balances carry a higher rate of interest. Rose (2008) stressed that more competition faced by banks for a consumer will help to keep the price in line with interest rates on similar products available in the market place. Consumers’ perception about the products and services and the level of request are found in the final price of a product or service

**Technology**

White (2009) observed that commercial bank business has changed dramatically over the past 25 years due in large part to technological changes. According to Mzumara (2006) technology helps banks to operate efficiently thus reducing costs. He indicated that a leader in technology may attract many customers and be able to meet their expectations, and the provision of innovative products which can then be passed along to consumers in terms of lower rates.

Llewellyn and Drake (1995) suggest that when considering the pricing of financial services, it might be helpful to distinguish between two forms which are explicit (overt) pricing and implicit (covert) pricing. Explicit pricing is when cost is mostly obvious and monetary. This allows an organization to signal costs of different services and uses price as a way of influencing consumer behaviour for example branch based transactions were priced relatively higher because of their high cost and ATM were priced relatively lower the reason being to move from branch based transaction in favour of ATM. Ennew and Waite (2007) support that pricing is far more complex for financial services as the terminology associated with pricing is itself complex and a diverse issue.

Implicit pricing on the other hand is where the actual price to customer is unclear and appears not to be paid by consumers, it may be non monetary for example a bank that offers free banking but pays no interest on credit balances. Implicit pricing includes requirements on customers to maintain minimum balances and the non payment or low payment of interest on credit balances. Implicit pricing has the general effect of leading to an oversupply of services and for the customer to overuse some bank services. This in turn has the effect of increasing the overall costs of the bank.

**Pricing Methods**

There are a number of pricing approaches which can be classified into three main groups namely market based pricing, cost based pricing and competition related pricing. These are grouped as indicated in table 1 below:

**RESEARCH METHODOLOGY**

The purpose of the study was to determine the factors that influence the pricing of banking products and the challenges that financial institutions face in attempting to price their services. The study focused on commercial banks in Zimbabwe. Primary data in the form of questionnaires and interviews were used as data collection instruments. Secondary data in the form of publications, manuals and business magazines were also used. The population comprised of 15 commercial banks in Zimbabwe and a random sample of 10 commercial banks was used for the purpose of the research. Questionnaires with open ended questions were distributed by hand to 30 respondents whilst 15 respondents were interviewed.

**RESEARCH FINDINGS**

Findings from the research indicate that 40% of the respondents felt that external factors were more
Factors and their influence on pricing

Figure 1: Factors influencing pricing of bank services

Table 1: Factors Influencing market price of product

<table>
<thead>
<tr>
<th>Market based pricing</th>
<th>Cost based pricing</th>
<th>Competition based pricing</th>
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</thead>
<tbody>
<tr>
<td>Perceived value pricing</td>
<td>Standard cost pricing</td>
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<tr>
<td>Psychological pricing</td>
<td>Cost plus pricing</td>
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<tr>
<td>Promotional pricing</td>
<td>Break even analysis</td>
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<tr>
<td>Skimming</td>
<td>Managerial Pricing</td>
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</tbody>
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Pricing strategies

The research sought to establish the pricing strategies that banks were using to determine the prices they charge. The table below gives a summary of the responses.

The pricing strategies used by the banks were either cost based, competition based or market oriented. As shown in Table 2 above, 24% of the respondents indicated the use of cost based pricing strategy, 36%
Figure 2: Factors influencing pricing of bank products

![Factors influencing pricing](image)

Figure 2: Factors influencing pricing of bank products

Source: Primary Data

Table 2: Factors influencing pricing

<table>
<thead>
<tr>
<th>Factor</th>
<th>Percentage response</th>
</tr>
</thead>
<tbody>
<tr>
<td>Internal</td>
<td>40</td>
</tr>
<tr>
<td>External</td>
<td>20</td>
</tr>
<tr>
<td>Both</td>
<td>36</td>
</tr>
<tr>
<td>Not sure</td>
<td>4</td>
</tr>
</tbody>
</table>

Source: Primary data

Table 2: Pricing strategies

<table>
<thead>
<tr>
<th>Strategy</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost based</td>
<td>24%</td>
</tr>
<tr>
<td>Market Oriented</td>
<td>40%</td>
</tr>
<tr>
<td>Competition based</td>
<td>36%</td>
</tr>
</tbody>
</table>

Source: Primary Data

Of the total respondents 80% indicated that they were facing challenges in pricing their services. Challenges cited were loss of confidence by bank customers, stiff competition, ascertaining risk and the fact that the central bank is undercapitalized and cannot claim its role as lender of last resort.

DISCUSSION

This research sought to identify the factors that influence pricing of bank products and the challenges faced by banks. Results from the research revealed that banks follow a set benchmark to price their products. The need to make profit and stay abreast of competition turned out to be the major factors influencing the prices of bank services. It was found out that the pricing strategies followed by commercial banks were aimed at profit maximization and the need to survive the stiff competition. Regulations also played a significant role in influencing the prices that banks can charge. Challenges faced by banks were found to be competition, economic difficulties and lack of customer confidence. It was also noted that currency reforms had rendered the central bank unable to perform the role of lender of last resort. This was in concomitance with the findings of Ferrari (1992) as similar factors seemed to dominate. It was also found out that there are two areas in which the bank can compete, that is price (interest rate) and credit quality. As the market becomes stronger, more lucrative all the participants will become more aggressive. This is used the competition based whilst 40% of the respondents indicated that prices were determined by market trends. Results from the interviews established that in addition to the above factors, economic and regulatory conditions dictate the pricing strategy in use as well.
in line with the findings of Ruckes (2004).

The major pricing strategies that were being used were, cost based, competition based and the need to follow market trends. It was found out that banks in pricing their products need to be able to cover costs and realize a calculated profit. Whilst that was important prices were also competition dictated as overpricing would result in loss of customers to competitors. The study revealed interesting results as far as the bank strategies were concerned. Commercial banks were using a strategy of bundling where multiple products/services are offered as a package and used to tackle competition, acquire new customers and to cross sell new services to the already existing customers. This then would enable them to lower prices of these products.

CONCLUSION

In light of the findings of this research, it was recommended that there is need to take into consideration various factors in pricing bank products so as to carter for both the institution and the customers. Optimal pricing is pivotal in ensuring that banks remain in business and achieve set objectives. It was also suggested that banks consider relationship based pricing in which prices of services are determined by an individual’s or a household’s overall product purchases rather than being determined on a product by product basis. The study recommends that further research be taken to determine the effect of the multi currency system on pricing of bank products. A research can also be conducted to determine whether the same factors influence prices of services offered in non banking financial institutions. The research concluded that competition, regulation and the profit motive are the major determinants of prices of bank services. Strategies used to price products were found to be cost based, competition based as well as detected by market trends. Challenges faced were stiff competition, loss of customer confidence, and failure by the central bank to be lender of last resort.

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