Economics of Economy Pricing

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Introduction

The economies of the western countries in the twenty-first century have already moved to a new level of mass production and technological progress as never seen before, at least not following a traditional Keynesian economy, thanks in part to globalization, advanced technologies, new organization management methods, and innovative supply chain strategies. A new phenomenon that has caught the attention of researchers and analysts is that a relatively large number of mass-produced commodities and services in western economies is somehow sold at discount price rather than the regular price at a much higher frequency than was ever seen before in a pre-pandemic world.

In a globalized world, the economies of advanced countries have entered a new phase called the "Economy Pricing System," where most of the mass commodities are sold at a discount price during certain periods of the year, called 'sales events,' due to decreased production costs thanks to enormous technological progress, implementation of advanced ERP systems in many medium and large corporations, high capital mobility, huge improvements in transportation and infrastructure, innovative global supply chain management and low commercial barriers. An increasing number of push and pull demand/ supply strategies used for different mass-produced commodities have helped many economies stay on the economy pricing phase.

The proposed innovative book is indented to introduce new ideas and theories by challenging the current modern foundations of micro and macroeconomics theories. In fact, the challenges at the microeconomic level are more focused on the standard theory of the firm and profitability in all its aspects, such as cost function, production possibility frontier, isocost lines, marginalism, etc., and at a macroeconomic level, the challenges are more directed to inflation theory, monetary policy, interest rate theory, the role of the central bank, the IS-LM model, the aggregate demand and aggregate supply curves, and the new role of sovereign government debt.

Most of the industrialized countries, in addition to low prices, have had record low inflation (except for the global pandemic years of 2020-2023 and the war in Ukraine of 2022-2023), low-interest rates (especially after the 2008 financial crisis), low growth rates and record low unemployment rates. The decline of interest rates close to zero level during the 2008 global financial crisis and afterward, creating the perfect conditions for cheap money for the mass of borrowers, has "sealed the fate" of the economies of industrialized countries to reach a phase that we normally call the "economy pricing system" or simple "economy pricing" characterized by low inflation, low-interest rates, low growth rates, low unemployment rate, mass production and demand-push strategies into customers for a large assortment of non-premium products.

By looking at the microeconomic level, we have that competitive firms use different pricing and marketing strategies to offer customers a variety of multi-products classified as premium and non-premium. The introduction of premium and non-premium commodities concept is the core of the economy pricing, which make the firm survive in a very competitive environment. A viable multiproduct firm producing both premium and non-premium commodities will charge a higher price for premium products sold to consumers with a less elastic demand (market niche) and offer discounts for non-premium products to the majority of customers whose demand is more elastic during different sales events all year around. A characteristic of economy pricing is that by using the push-demand-to-customers strategy, reaching the maximum profit is not the firm's main objective. The firm's main objective is to hold the market share by reaching the desired sales target, which does not always equal maximizing profit for every unit sold. It guarantees a net monetary position (NMP) greater than one and a reasonable desired profit which is a key parameter for many firms operating in economy pricing.

The introduction of production capacity utilization for a given firm is another microeconomic metric of the economy pricing system. Lower capacity utilization for firms selling non-premium products is viewed as a bad sign of the economy's health. Instead, higher capacity utilization selling substantial volumes of non-premium products above the trend rate is a leading indicator of a healthy economy pricing system. For a manufacturer, the higher the unutilized production capacity, the higher the number of sales promotions offered on non-premium products and, eventually, premium goods to break even and start making a coherent profit.

The marginalist approach analysis says that a necessary condition for profit to be maximized is when the firm sets its quantity so that the difference between the firm's marginal revenue and its cost equals zero or when marginal revenue equals its marginal cost. However, the new *competitive pricing approach* based on the economy pricing system puts a different perspective on a multi-product firm that manufactures and sells a combination of premium and non-premium products to help reach a positive net monetary position (NMP) and hit the desired target profit as required by management.

At the macroeconomic level, it's interesting to analyze how monetary policy is managed in an economy pricing system dominated by low inflation, low-interest rates, and low unemployment rates. This economy is also characterized by competition, where firms bring to different market categories of premium and non-premium products to stay competitive and control costs through global supply chain management. A fascinating topic to discuss is how monetary policy works when inflation, interest rates, and unemployment rates are kept low in an economy characterized by a high level of competition in different sectors. There is also a relationship between monetary policy and low-interest rates. The low inflation is the result of competitive prices, which is mostly determined by globally managing the supply chain, which allows companies to be able to cut excess cost and deliver products to final consumers much faster and cheaper (with the exception of the global supply chain disruption during pandemic years of 2020-23).

Another area to be analyzed at the macroeconomic level is central bank independence. Due to the low-interest rate environment in the last two decades, the monetary tools used by Central Bank to operate during the financial crisis have been reduced further. Therefore, it is suggested to have a more transparent process controlled by administrative orders between treasury departments and central banks. The main idea is to reduce the independent role of the central bank and eliminate central banks' ties to large financial corporations. The new process of administrative orders between the treasury department and central banks is supposed to allow voters and stakeholders to exercise greater control over central banks’ monetary policies in different countries by allowing central banks to collaborate with governments under the control of a democratic and transparent process.

The aggregate demand in an economy pricing system is another subject taken into consideration in this book. Based on our analysis and using a different concept, we’ll try to explain how the global aggregate demand for an economy should be split between the aggregate demand for the private sector, public sector, and import-export sector. The interesting point is that on one side, the aggregate demand in the private sector could be measured as the total demand for all finished goods, premium and non-premium, manufactured and commercialized in different sectors of the economy. On the other side, for the aggregate supply in the private sector, we need to consider a new concept that takes into consideration the aggregate production capacity utilization of firms offering premium and non-premium products in different sectors.

This book provides a detailed analysis of the economic implications of the business strategy known as economy pricing by insightfully and efficiently connecting important concepts in business administration, finance, and economics.

The new Economy Pricing System theories introduced in this volume are written to challenge microeconomics and macroeconomics foundations and update their theories in a new economic reality of the twenty-first century dominated by low-interest rates, low inflation rates, low growth rates, and low unemployment rates. The main scope of this book is to analyze how the micro and macroeconomic events are interconnected in a globalized economy pricing system. The global COVID-19 pandemic and the war in Ukraine during 2020-2023 have disrupted the global chain supply and sharply increased the price of commodities and inflation. However, the principles and concepts of an economy pricing system remain pretty much the same in the long run, where the economies of industrialized countries converge to the trend of having low-interest rates, low inflation, low growth rates, and low unemployment rates.

Structure of the book

The introduction part of this work motivates the study and brings out some definitions and objectives of economy pricing. The book is composed of two parts and six chapters, three chapters for each part. The first three chapters in part one discuss the microeconomics of the economy pricing system, and the last three chapters in part two focus on the macroeconomics of economy pricing.

Chapter One outlines economy pricing, competition, pricing strategies, mass production, and economies of scale. The chapter will start by discussing the microeconomics of the pricing strategies in economy pricing. Economy pricing is extensively used in supermarkets and superstores, especially in the retail food business for groceries, and is based on the idea that a high anchor price being reduced by an impressive discount price would create a high perceived value to push consumers to buy as much as they can afford. This will lead to the new microeconomic model of the Three-levels of demand-push and Cost Approach in economy pricing.

Chapter Two considers the firm's theory in an economy pricing system. This chapter will discuss the concept of production and cost from an economy pricing perspective. By using the volume-based analysis, there is the introduction of a New Theory of the Firm in Product-Mix Profitability. This chapter will introduce the microeconomics techniques of a new Competitive Production Function Model and Behavioral Relationships approach based on economy pricing. A firm can use different levels of technologies to produce output by using a variety of input vectors, which different sets of production functions can summarize. This will lead to the introduction of a new cost function model in the Competitive Product-Mix associated with the Isocost lines approach.

Chapter Three talks about how the pricing strategy is influenced by several factors that might be beyond the firm’s control. Here will be discussed how a firm adopting price discrimination strategies can reach different objectives. From an organization’s perspective, price discrimination can offer many advantages based on the size of the company. An interesting argument will be to explore the revolutionary path from marginalism to competitive pricing by introducing the *Price Competition Approach* to explain *Marginal Cost Approach.*

Chapter Four considers how inflation, interest rates, and unemployment rates work at the macro level in an economy pricing system dominated by competition and characterized by different categories of non-premium products in almost all sectors of the economy. This chapter will explain how inflation is determined and what are the causes of inflation.

Chapter Five treats how monetary policy works when inflation, interest rates, and unemployment rates are kept low in an economy pricing characterized by a high level of competition between firms. The chapter will discuss the relationship between money growth and inflation. It will consider the *Quantity Theory of Money* (QTM) and the optimum quantity of money as proposed by Friedman in the 1960s and how this theory has evolved in the last decades.

Chapter Six discusses public debt and fiscal policy. There is a debate about whether a government uses its debt-raising capacity cautiously, which depends on its ability to render the borrowed money into economic growth without raising inflation. The growth in government spending and debt has been seen by some economists as a welcome policy to stimulate growth and finance infrastructures thanks to the borrowing costs that have been at historic lows since the global financial crisis of 2008. This chapter will talk about some criticism of aggregate demand and curve supply and introduce a new approach to aggregate demand and aggregate supply based on economy pricing concepts.

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