

Pricing Products:
Pricing Considerations
and Approaches



Lesson 8

Definition

- **Price**
 - The amount of money charged for a product or service, or the sum of the values that consumers exchange for the benefits of having or using the product or service.

What is Price?

Price Has Many Names

- Rent
- Fee
- Rate
- Commission
- Assessment
- Tuition
- Fare
- Toll
- Premium
- Retainer
- Bribe
- Salary
- Wage
- Interest
- Tax



What is Price?

- **Dynamic Pricing on the Web allows SELLERS to:**
 - Monitor customer behaviour and tailor offers.
 - Change prices on the fly to adjust for changes in demand or costs.
 - Aid consumers with price comparisons.
 - Negotiate prices in online auctions and exchanges.



What is Price?

- **Price and the Marketing Mix:**
 - Only element to produce revenues
 - Most flexible element
 - Can be changed quickly
- **Common Pricing Mistakes**
 - Reducing prices too quickly to get sales
 - Pricing based on costs, not customer value

Factors to Consider When Setting Price

Internal Factors

- *Marketing objectives*
 - *Marketing mix strategies*
 - *Costs*
 - *Organizational considerations*
- **Market positioning influences pricing strategy**
 - **Other pricing objectives:**
 - **Survival**
 - **Current profit maximization**
 - **Market share leadership**
 - **Product quality leadership**

Factors to Consider When Setting Price

Internal Factors

- *Marketing objectives*
 - *Marketing mix strategies*
 - *Costs*
 - *Organizational considerations*
- Pricing must be carefully coordinated with the other marketing mix elements
 - Target costing is often used to support product positioning strategies based on price
 - Nonprice positioning can also be used

Factors to Consider When Setting Price

Internal Factors

- *Marketing objectives*
- *Marketing mix strategies*
- ***Costs***
- *Organizational considerations*

- **Types of costs:**
 - Variable
 - Fixed
 - Total costs
- **How costs vary at different production levels will influence price setting**
- **Experience (learning) curve affects price**

Factors to Consider When Setting Price

Internal Factors

- *Marketing objectives*
 - *Marketing mix strategies*
 - *Costs*
 - *Organizational considerations*
- **Who sets the price?**
 - Small companies: CEO or top management
 - Large companies: Divisional or product line managers
 - **Price negotiation is common in industrial settings where pricing departments may be created**

Factors to Consider When Setting Price

External Factors

- *Nature of market and demand*
- *Competitors' costs, prices, and offers*
- *Other environmental elements*
- **Types of markets**
 - Pure competition
 - Monopolistic competition
 - Oligopolistic competition
 - Pure monopoly
- **Consumer perceptions of price and value**
- **Price-demand relationship**
 - Demand curve
 - Price elasticity of demand

Factors to Consider When Setting Price

External Factors

- *Nature of market and demand*
 - *Competitors' costs, prices, and offers*
 - *Other environmental elements*
- Consider competitors' costs, prices, and possible reactions
 - Pricing strategy influences the nature of competition
 - Low-price low-margin strategies inhibit competition
 - High-price high-margin strategies attract competition
 - Benchmarking costs against the competition is recommended

Factors to Consider When Setting Price

External Factors

- *Nature of market and demand*
 - *Competitors' costs, prices, and offers*
 - *Other environmental elements*
- **Economic conditions**
 - Affect production costs
 - Affect buyer perceptions of price and value
 - **Reseller reactions to prices must be considered**
 - **Government may restrict or limit pricing options**
 - **Social considerations may be taken into account**

General Pricing Approaches

- **Cost-Based Pricing: Cost-Plus Pricing**
 - Adding a standard markup to cost
 - Ignores demand and competition
 - Popular pricing technique because:
 - It simplifies the pricing process
 - Price competition may be minimized
 - It is perceived as more fair to both buyers and sellers

General Pricing Approaches

Cost-Based Pricing Example

- Variable costs: \$20
- Fixed costs: \$ 500,000
- Expected sales: 100,000 units
- Desired Sales Markup: 20%

Variable Cost + Fixed Costs/Unit Sales = Unit Cost

$$\$20 + \$500,000/100,000 = \$25 \text{ per unit}$$

Unit Cost/(1 – Desired Return on Sales) = Markup Price

$$\$25 / (1 - .20) = \$31.25$$

General Pricing Approaches

- **Cost-Based Pricing: Break-Even Analysis and Target Profit Pricing**
 - Break-even charts show total cost and total revenues at different levels of unit volume.
 - The intersection of the total revenue and total cost curves is the break-even point.
 - Companies wishing to make a profit must exceed the break-even unit volume.

General Pricing Approaches

- **Value-Based Pricing:**
 - Uses buyers' perceptions of value rather than seller's costs to set price.
 - Measuring perceived value can be difficult.
 - Consumer attitudes toward price and quality have shifted during the last decade.
 - Value pricing at the retail level
 - Everyday low pricing (EDLP) vs. high-low pricing

General Pricing Approaches

- **Competition-Based Pricing:**
 - Also called going-rate pricing
 - May price at the same level, above, or below the competition
 - Bidding for jobs is another variation of competition-based pricing
 - Sealed bid pricing