Pricing Strategy Tips

IRELAND

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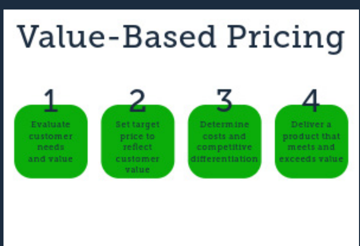
As consumers, a product's price represents what we must pay to acquire it. From the seller's perspective, the price is the only revenue-generating component of the marketing mix. Product, promotion, and placement are all cost components.

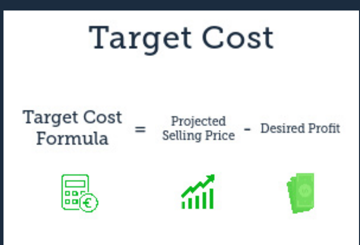
The price can also serve as a marketing tool and is often used in promotional campaigns. Trying to set the right price can be a real challenge for marketers. The price of a product must be low enough to motivate customers to buy it but high enough that a company can cover its costs and earn a profit from the good or service. In addition, market and economic conditions are always changing, as are the prices of competing products. As a result, companies should evaluate their pricing strategy to remain competitive.

Although there is no one right way to determine the price of a good or service, there are several strategies sellers can use. The most common pricing strategies include: Cost-based pricing, This pricing strategy (also known as cost¬ plus pricing) is based on covering a firm's costs and providing for a set amount of profit. There are many advantages of cost based pricing. Besides being easy to calculate and easy to administer, it requires a minimum amount of information. However, Cost-based pricing ignores whether a price is compatible with consumers' expectations or can compete with the prices of similar products. Cost-based pricing also provides a firm with little incentive to operate more efficiently to hold its costs down.

Demand-based pricing (sometimes called value-based pricing) is the strategy of setting the price of a product based on its demand or its perceived value. A higher price will be charged when the demand or the product's perceived value is high. A lower price will be charged when its demand or perceived value is low. Demand-based pricing can be defined further by other pricing strategies: target costing and price discrimination.



Target costing estimates the value customers receive from a product and, therefore, the price they are willing to pay for it. The firm then subtracts an acceptable profit margin to obtain an estimated cost for the product. Firms then work to get costs down to this targeted level. IKEA has successfully used target cost pricing.



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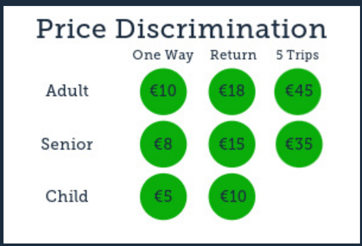
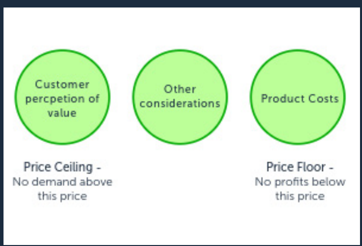
Price discrimination occurs when a business charges different prices to different customers for an identical good or service for reasons not associated with costs. Price-insensitive customers are charged higher prices, and customers who are more price-sensitive are charged lower prices. For example, because senior citizens/students are often on fixed budgets, restaurants and movie theatres frequently offer them lower prices.

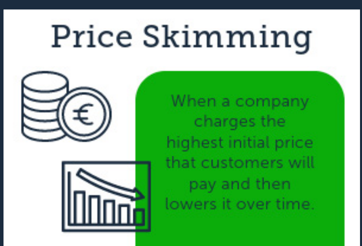


Competition-based pricing is a pricing strategy that is based on the degree of competition in a market, which, in turn, affects a company's price-setting ability. Some retail stores rarely put individual products on sale and instead offer everyday low pricing on all their products. Walmart has successfully used this strategy.



When launching a new product, companies may need to use a different type of pricing strategy than they would for an existing product, such as:

- **Price skimming** involves charging a high price for a product when it is first introduced and there are few if any competitors. The idea is to initially skim off as much profit as possible to recoup the product's development costs. However, the high price is likely to encourage competitors to enter the market at a lower price. When they do, the firm then lowers the product's price.



- **Penetration pricing** involves charging the lowest possible price for a new product to quickly build market share for a product. If the increased production to satisfy growing sales results in lower per unit costs, then the product's profits can rise even though its price is lower. Penetration pricing is also appropriate during the growth stage of a product's life cycle and when customers are price-sensitive. It may also create goodwill among consumers and inhibit competitors from entering the market.

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Perception pricing: For many consumers, a high price indicates good quality. Consumers are more likely to associate price with quality when a product is complex and they are not familiar with it or its brand name. There are several types of pricing strategies that can be used to affect people's perceptions of a product:

- **Prestige pricing** (also known as premium pricing) is the practice of charging a high price to invoke perceptions of high quality and privilege.

- **Psychological pricing** (sometimes called odd or fractional pricing) is the practice of charging a price just below a whole number to give the appearance of a lower price.

- A **loss leader** is a product that is priced below its costs. Stores use loss leaders to attract customers into the store with the hopes that they will be attracted to buy other more expensive items.

- **Reference pricing** refers to using an inflated price (the regular retail price or the manufacturer's suggested retail price) that is then discounted to appear as if the product is a good value