Pricing Strategies

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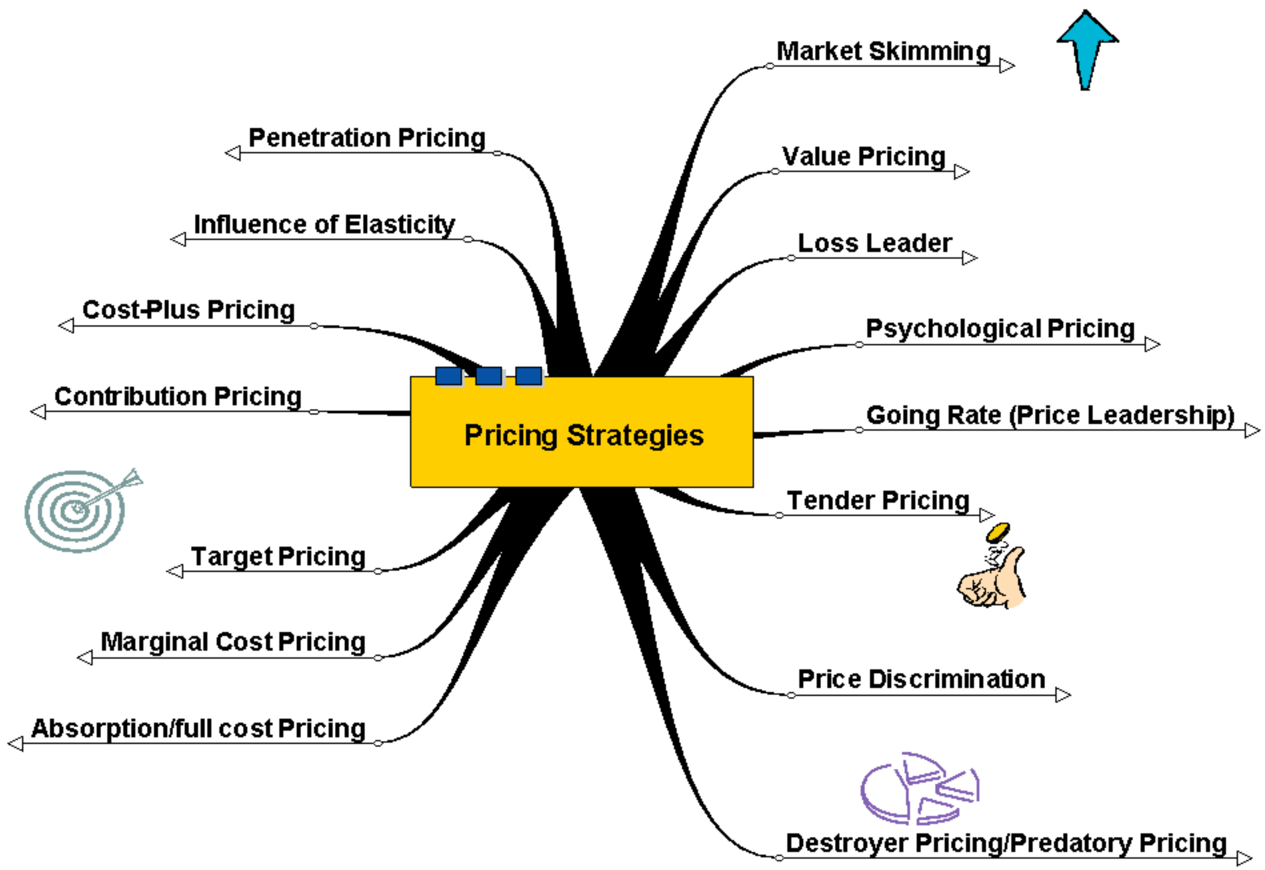
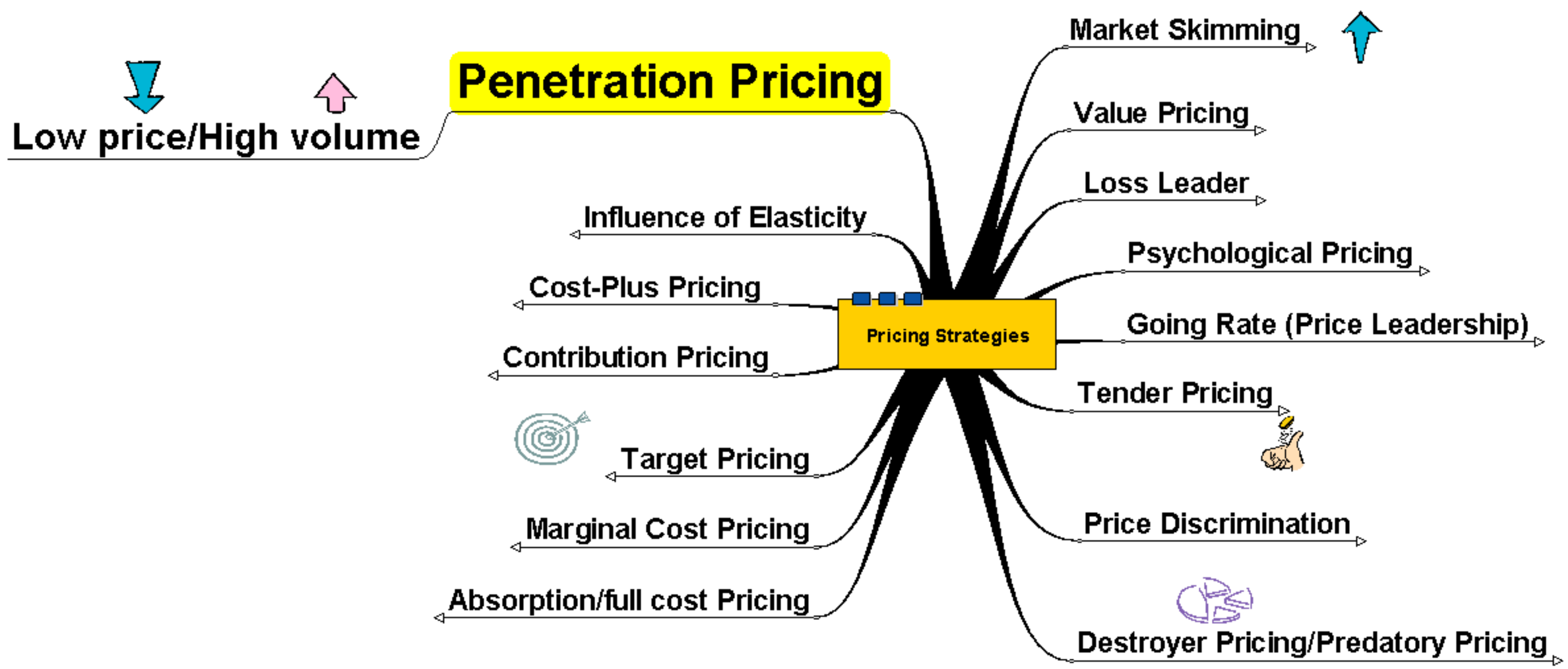


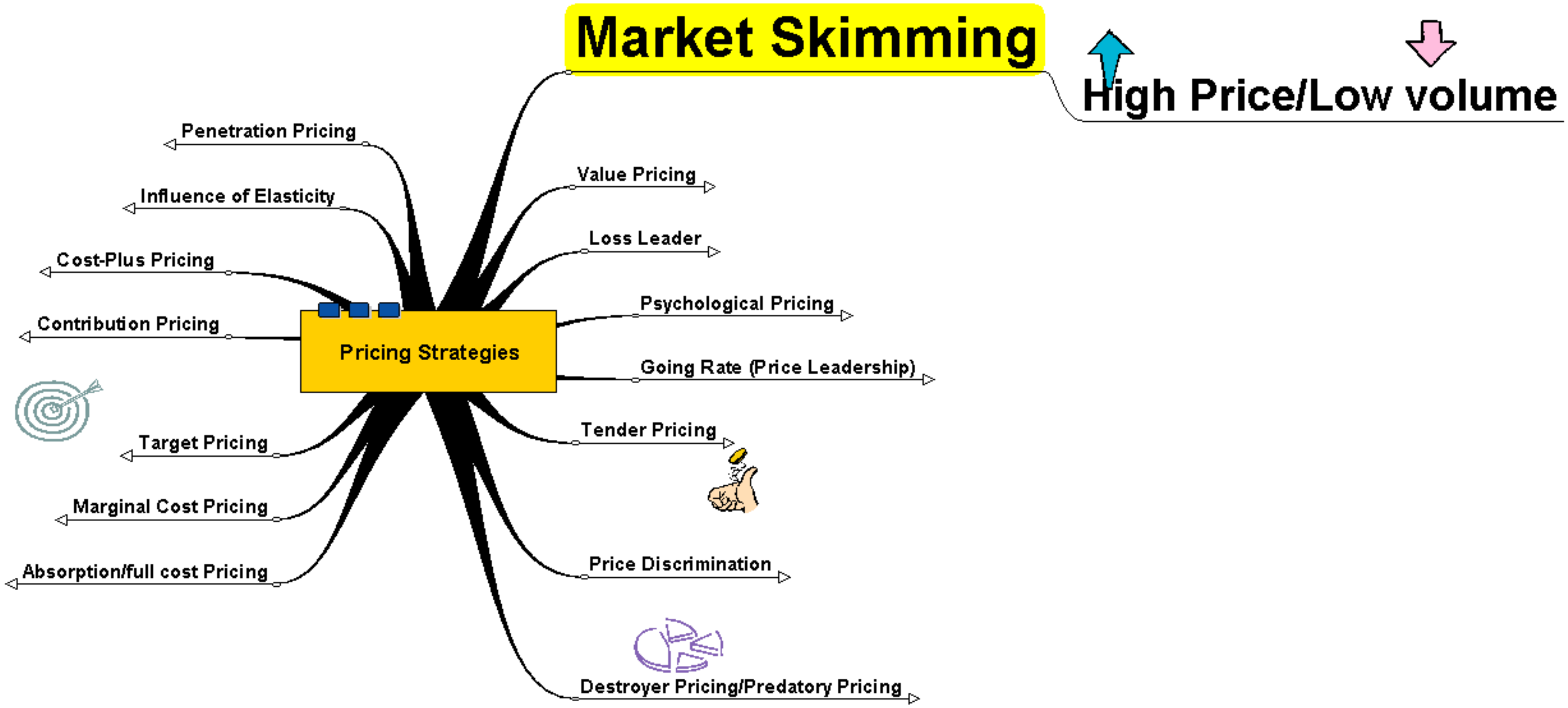
Penetration Pricing



Penetration Pricing

- Price set to 'penetrate the market'
- 'Low' price to secure high volumes
- Typical in mass market products – chocolate bars, food stuffs, household goods, etc.
- Suitable for products with long anticipated life cycles
- May be useful if launching into a new market

Market Skimming

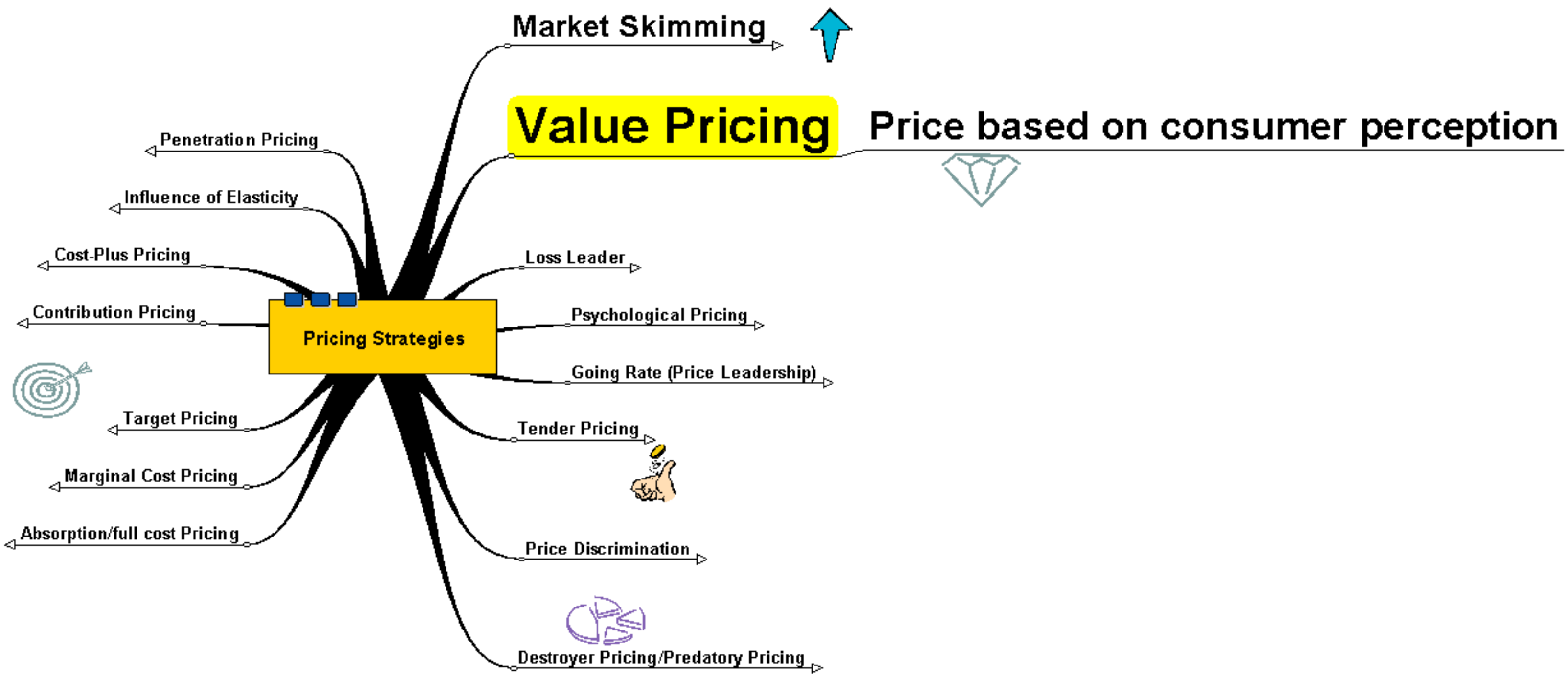


Market Skimming

Many are predicting a firesale in laptops as supply exceeds demand.

- High price, Low volumes
- Skim the profit from the market
- Suitable for products that have short life cycles or which will face competition at some point in the future (e.g. after a patent runs out)
- Examples include: Playstation, jewellery, digital technology, new DVDs, etc.

Value Pricing



Value Pricing

- Price set in accordance with customer perceptions about the value of the product/service
- Examples include status products/exclusive products

Companies may be able to set prices according to perceived value.

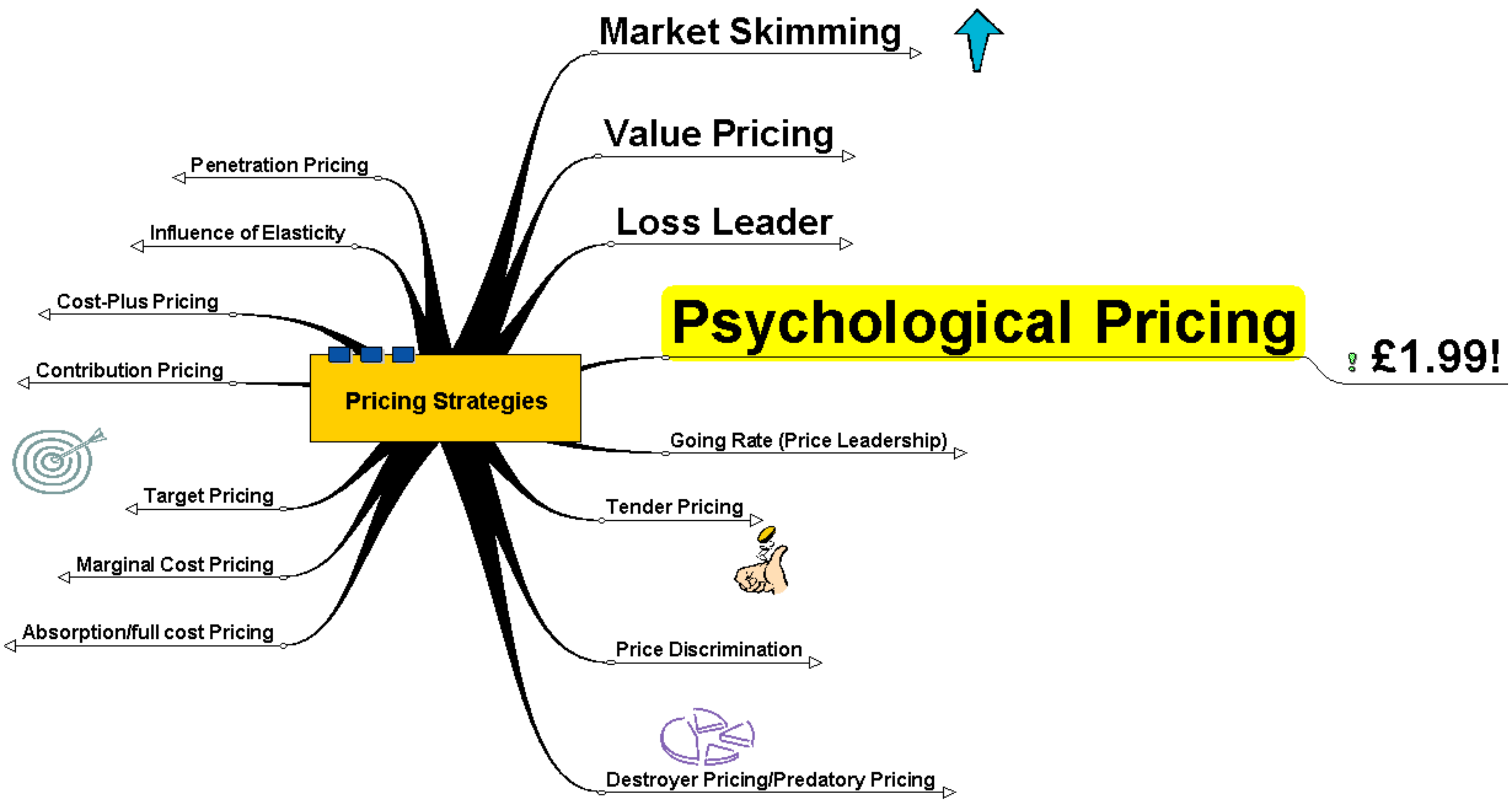
Loss Leader


Market Skimming
Value Pricing
Loss Leader
Sold below cost to attract sales elsewhere
Penetration Pricing
Influence of Elasticity
Cost-Plus Pricing
Contribution Pricing
Pricing Strategies
Psychological Pricing
Going Rate (Price Leadership)
Target Pricing
Marginal Cost Pricing
Absorption/full cost Pricing
Tender Pricing
Price Discrimination
Destroyer Pricing/Predatory Pricing

Loss Leader

- Goods/services deliberately sold below cost to encourage sales elsewhere
- Typical in supermarkets, e.g. at Christmas, selling bottles of gin at £3 in the hope that people will be attracted to the store and buy other things
- Purchases of other items more than covers 'loss' on item sold
- e.g. 'Free' mobile phone when taking on contract package

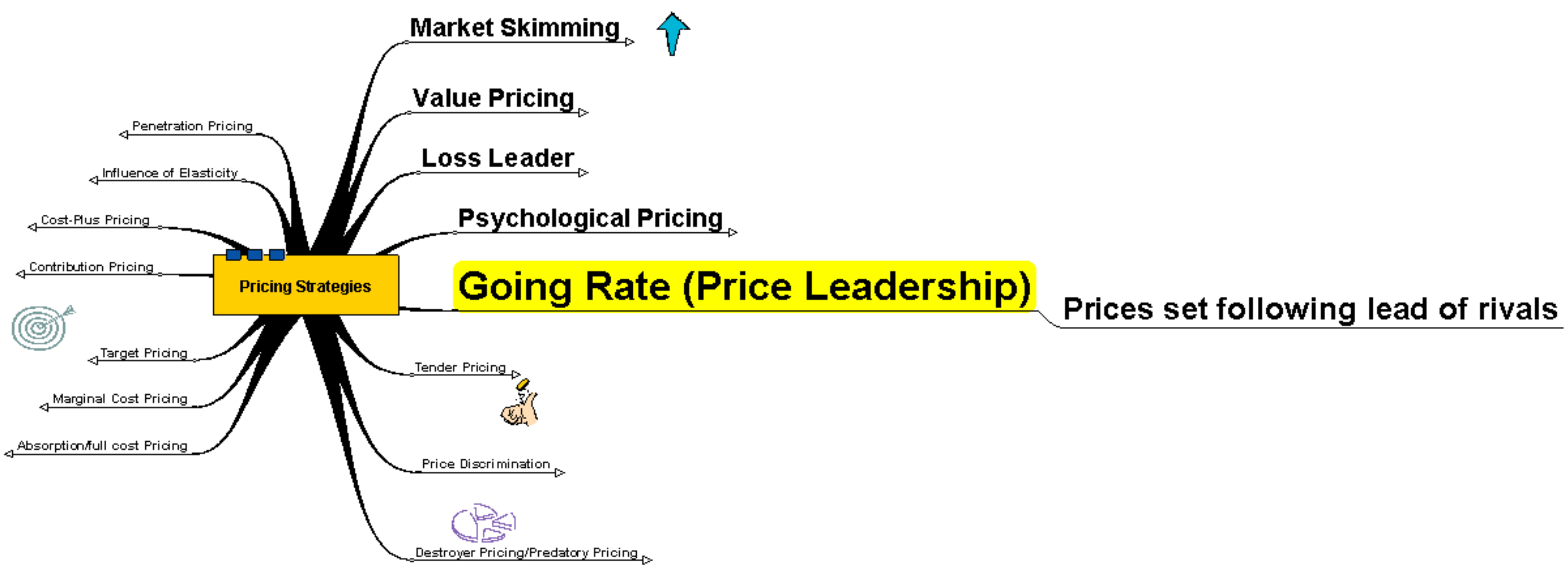
Psychological Pricing



Psychological Pricing

- Used to play on consumer perceptions
- Classic example - £9.99 instead of £10.99!
- Links with value pricing – high value goods priced according to what consumers THINK should be the price

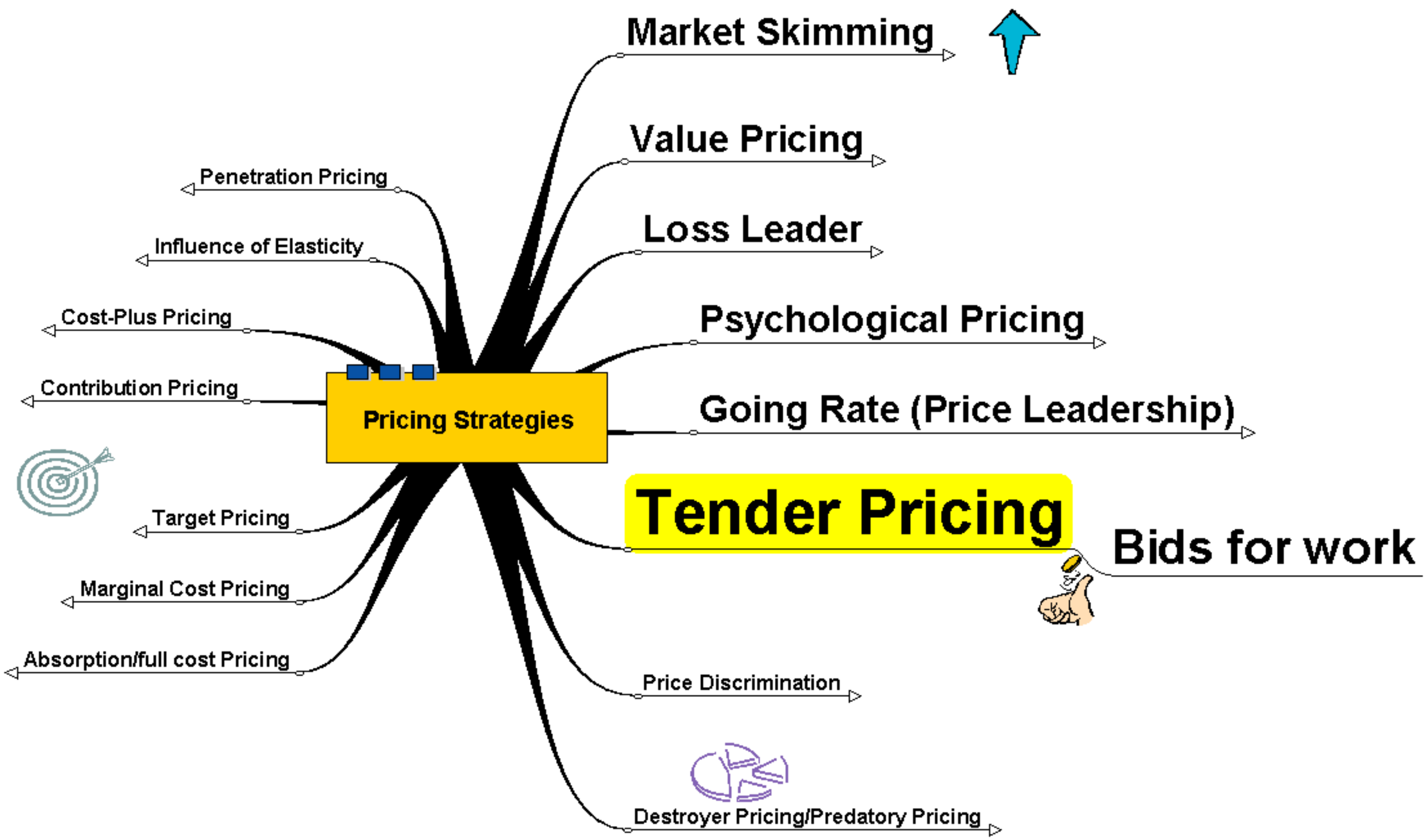
Going Rate (Price Leadership)



Going Rate (Price Leadership)

- In case of price leader, rivals have difficulty in competing on price – too high and they lose market share, too low and the price leader would match price and force smaller rival out of market
- May follow pricing leads of rivals especially where those rivals have a clear dominance of market share
- Where competition is limited, 'going rate' pricing may be applicable – banks, petrol, supermarkets, electrical goods – find very similar prices in all outlets

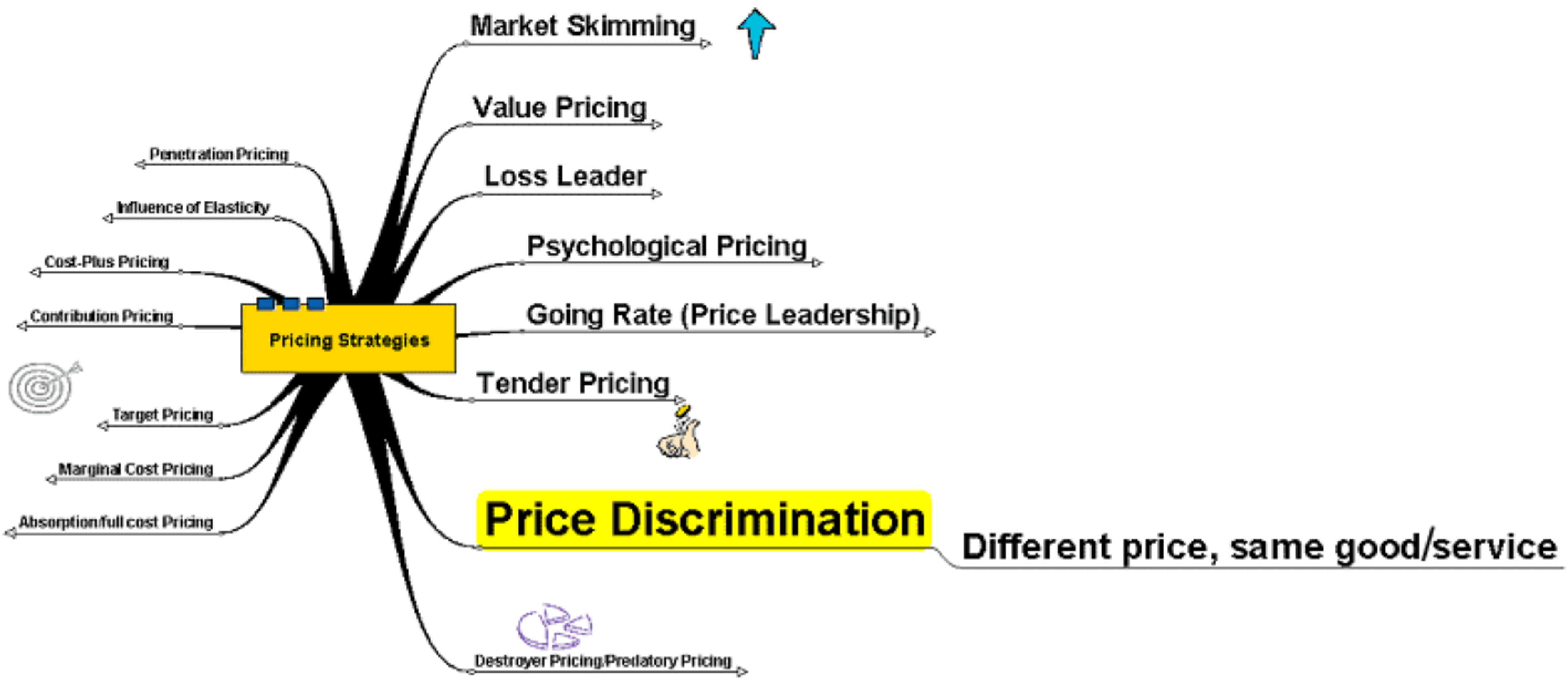
Tender Pricing



Tender Pricing

- Many contracts awarded on a tender basis
- Firm (or firms) submit their price for carrying out the work
- Purchaser then chooses which represents best value
- Mostly done in secret

Price Discrimination

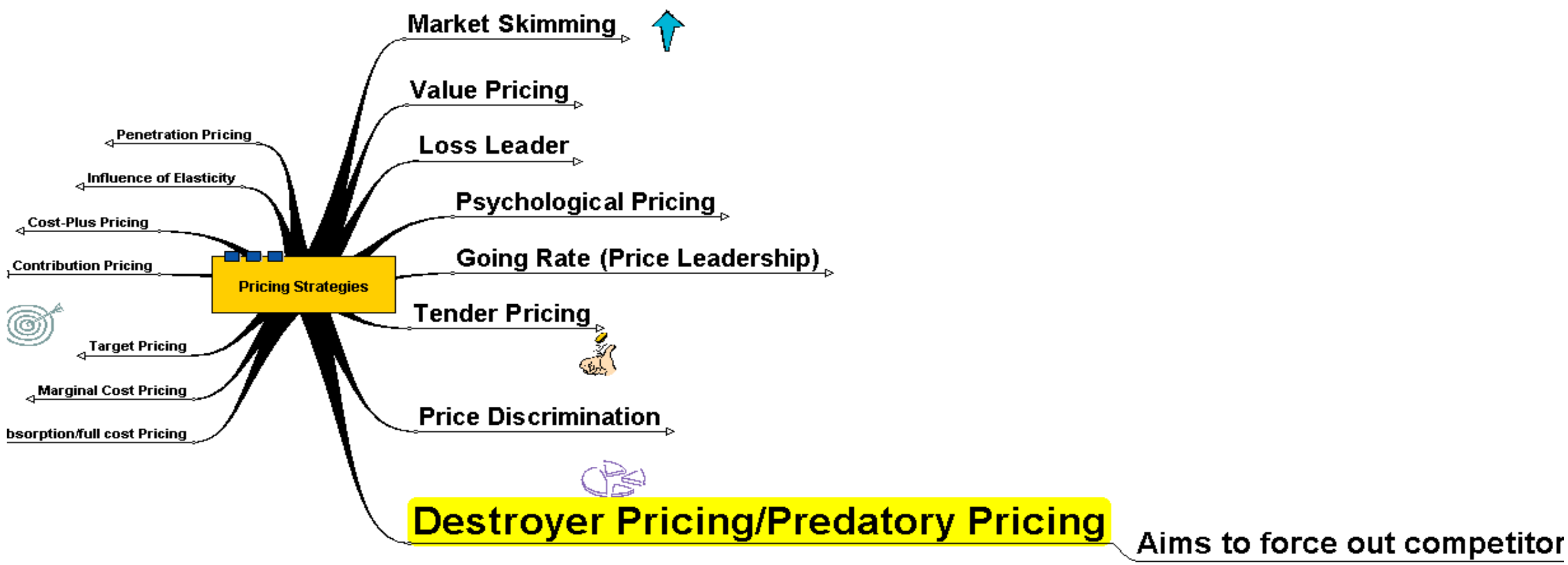


Price Discrimination

Prices for rail travel differ for the same journey at different times of the day

- Charging a different price for the same good/service in different markets
- Requires each market to be impenetrable
- Requires different price elasticity of demand in each market

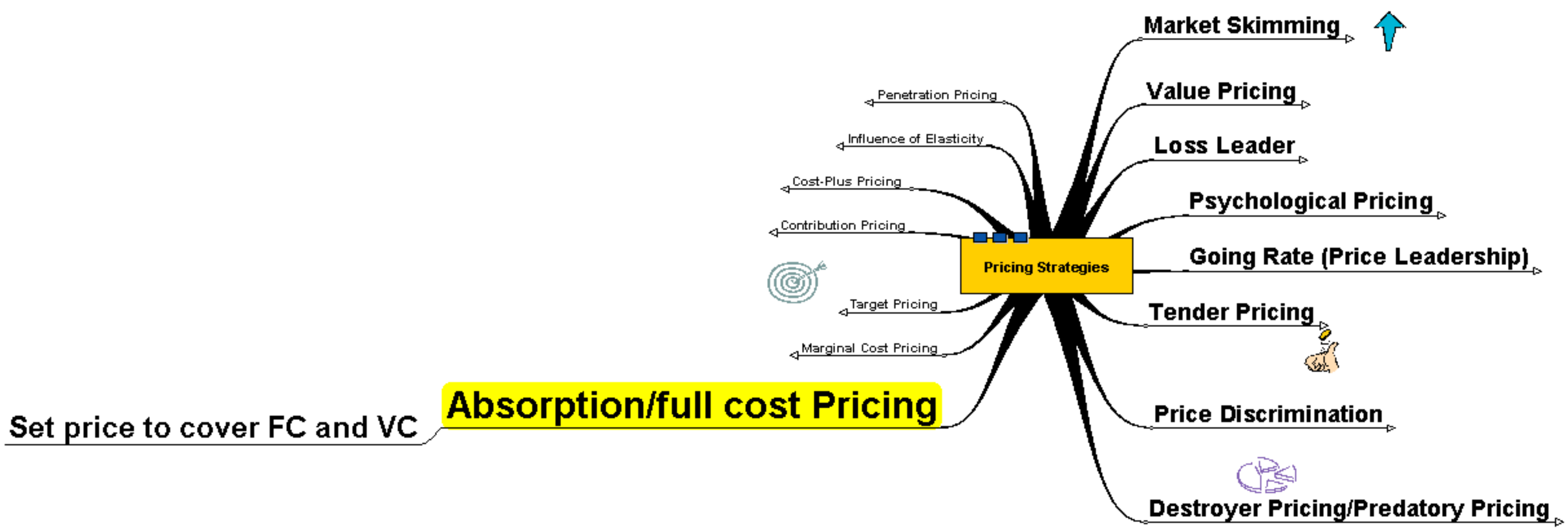
Destroyer Pricing/Predatory Pricing



Destroyer/Predatory Pricing

- Deliberate price cutting or offer of ‘free gifts/products’ to force rivals (normally smaller and weaker) out of business or prevent new entrants
- Anti-competitive and illegal if it can be proved

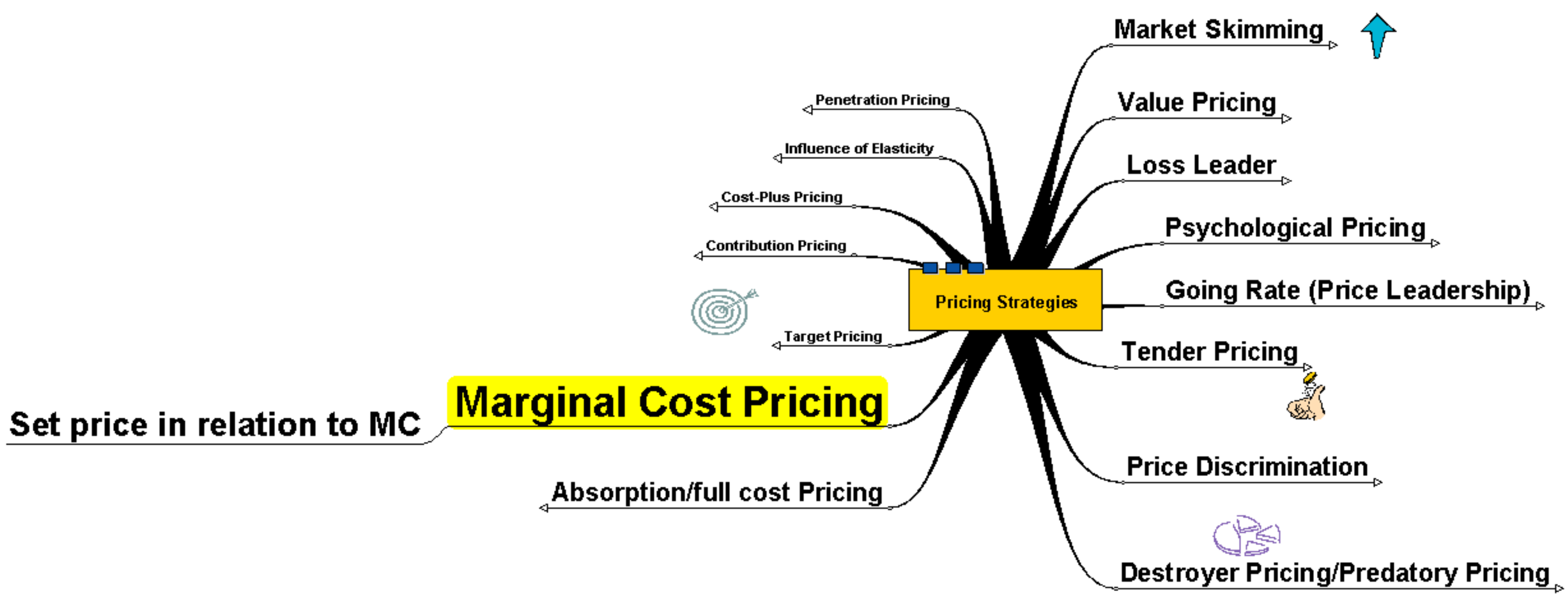
Absorption/Full Cost Pricing



Absorption/Full Cost Pricing

- Full Cost Pricing – attempting to set price to cover both fixed and variable costs
- Absorption Cost Pricing – Price set to ‘absorb’ some of the fixed costs of production

Marginal Cost Pricing



Marginal Cost Pricing

- Marginal cost – the cost of producing ONE extra or ONE fewer item of production
- MC pricing – allows flexibility
- Particularly relevant in transport where fixed costs may be relatively high
- Allows variable pricing structure – e.g. on a flight from London to New York – providing the cost of the extra passenger is covered, the price could be varied a good deal to attract customers and fill the aircraft

Marginal Cost Pricing

- Example:

Aircraft flying from Bristol to Edinburgh – Total Cost (including normal profit) = £15,000 of which £13,000 is fixed cost*

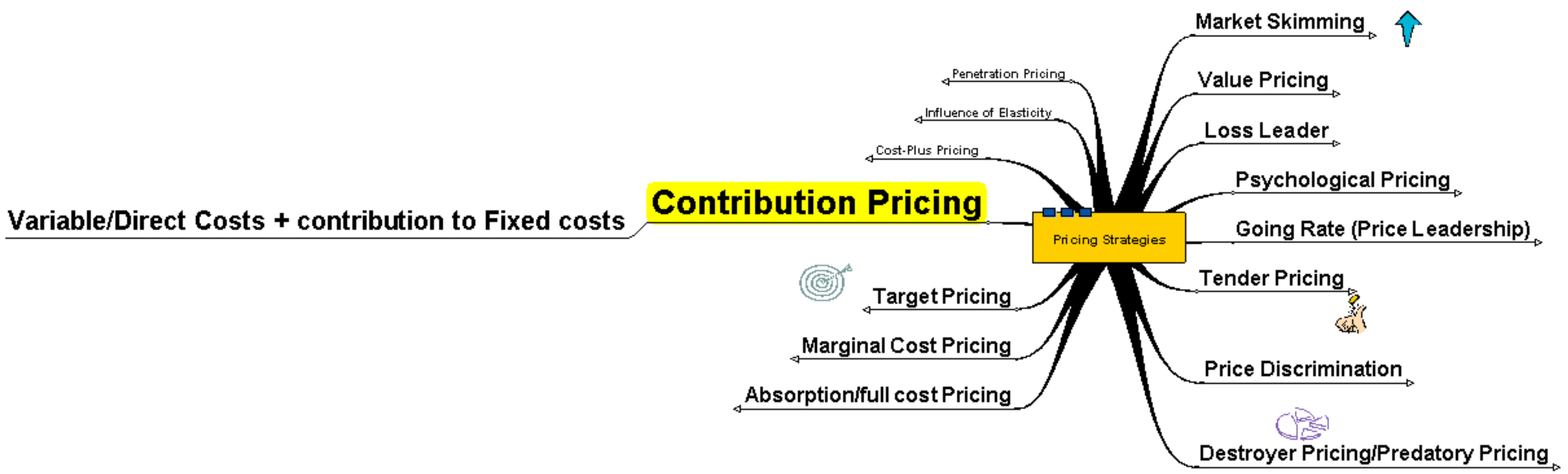
Number of seats = 160, average price = £93.75

MC of each passenger = 2000/160 = £12.50

If flight not full, better to offer passengers chance of flying at £12.50 and fill the seat than not fill it at all!

***All figures are estimates only**

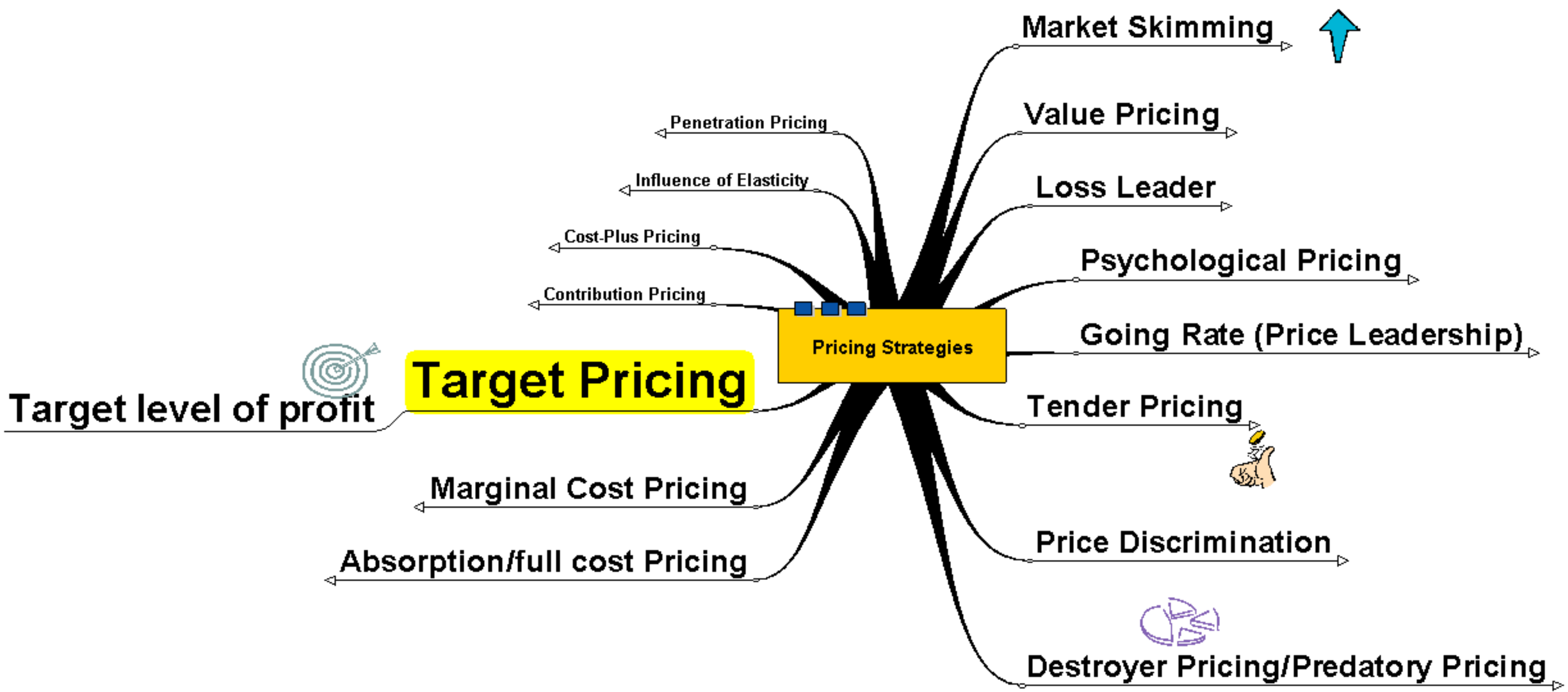
Contribution Pricing



Contribution Pricing

- **Contribution = Selling Price – Variable (direct costs)**
- Prices set to ensure coverage of variable costs and a 'contribution' to the fixed costs
- Similar in principle to marginal cost pricing
- Break-even analysis might be useful in such circumstances

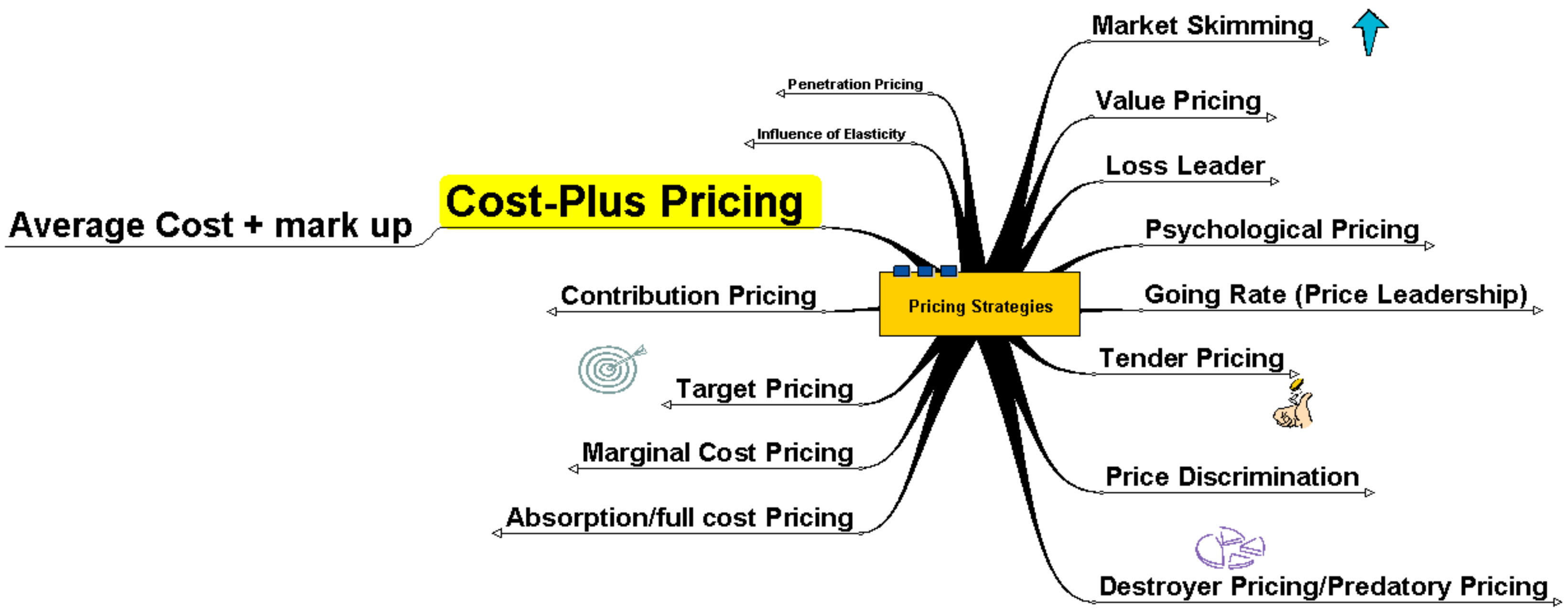
Target Pricing



Target Pricing

- Setting price to 'target' a specified profit level
- Estimates of the cost and potential revenue at different prices, and thus the break-even have to be made, to determine the mark-up
- Mark-up = Profit/Cost x 100

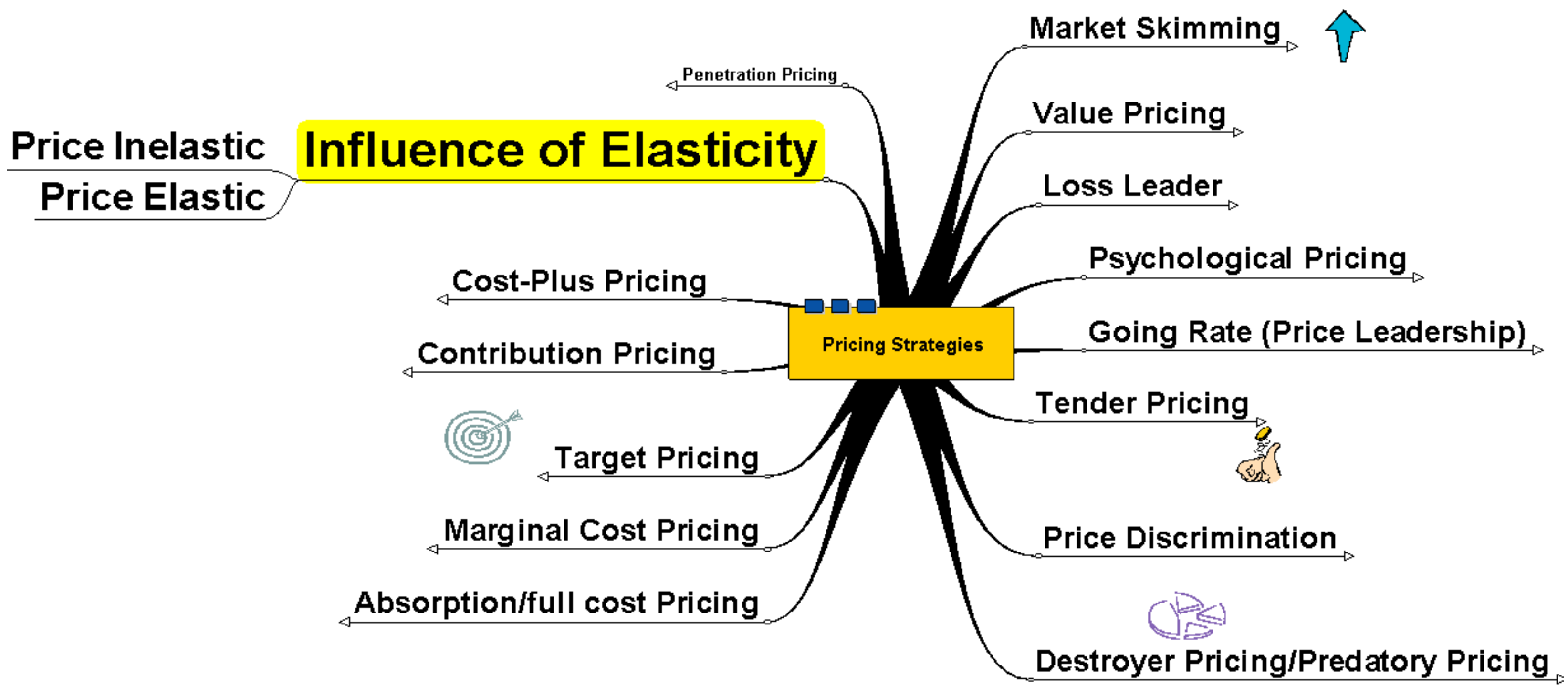
Cost-Plus Pricing



Cost-Plus Pricing

- Calculation of the average cost (AC) plus a mark up
- AC = Total Cost/Output

Influence of Elasticity



Influence of Elasticity

- Any pricing decision must be mindful of the impact of price elasticity
- The degree of price elasticity impacts on the level of sales and hence revenue
- Elasticity focuses on proportionate (percentage) changes
  - **PED = % Change in Quantity demanded/% Change in Price**

Influence of Elasticity

- **Price Inelastic:**
- % change in Q < % change in P
- **e.g.** a 5% increase in price would be met by a fall in sales of something less than 5%
- Revenue would rise
- A 7% reduction in price would lead to a rise in sales of something less than 7%
- Revenue would fall

Influence of Elasticity

- **Price Elastic:**
- % change in quantity demanded > % change in price
- **e.g.** A 4% rise in price would lead to sales falling by something more than 4%
- Revenue would fall
- A 9% fall in price would lead to a rise in sales of something more than 9%
- Revenue would rise