Retail Pricing Strategies and Tactics

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Price is simple, but pricing is challenging

- **Price** is the amount of money charged for a product or service.

- **Pricing** is the determination of prices. Pricing can be monetary or non-monetary. Pricing decisions will lead to specific pricing strategies and tactics.

- Price seems to be simple, but pricing is challenging. It is the number-one problem facing many business and marketing executives.

Major Pricing Strategies

Customer perceptions of Value

Marketing Strategy, objectives , and marketing mix
Nature of the market and demand
Competitors' strategies and prices

Product costs

Price ceiling

Price floor

Basic Pricing Strategies

- Customer value-based pricing
- Cost-based pricing
- Competition-based pricing

Value-based vs. Cost-based pricing

value-based pricing

Assess customer needs and value perceptions → Set target price to match customer perceived value → Determine costs → Design product to deliver desired value

Cost-based pricing

Design a good produce → Determine product costs → Set price based on cost → Convince buyers of the product value

Value-base pricing

Good-value pricing: offers the right combination of quality and good service at a fair price

Everyday low pricing (EDLP) charging a constant everyday low price with few or no temporary price discounts

High-low pricing charging higher prices on an everyday basis but running frequent promotions to lower prices temporarily on selected items

Cost-based Pricing

- Cost-plus pricing adds a standard markup to the cost of the product
- Sellers are certain about costs, and buyers feel it is fair
- But the disadvantage is that it Ignores demand and competitor prices

Competition-based pricing

- For companies that employ Competition-based pricing, they set prices based on competitors’ strategies, costs, prices, and market offerings.

- Consumers will base their judgments of a product’s value on the prices that competitors charge for similar products.

Other Internal and External Considerations Affecting Price Decisions

Demand-based pricing

Demand-based pricing means that the firm bases the selling price on an estimate of the quantity that it can sell in different markets at different times.

- Target costing starts with an ideal selling price based on consumer value considerations and then targets costs that will ensure that the price is met.

- Yield management pricing is very popular in the service industry whereas companies charge different prices to different customers. In economics, this is often called price discrimination.

Loss leader pricing

- Relatively an aggressive pricing strategy
- Sells selected products below cost
- Attract store traffic from competition
- The store may make up its loss by customers buying additional profitable goods

Price Elasticity

Price elasticity of demand illustrates the response of demand to a change in price

Inelastic demand
occurs when demand hardly changes when there is a small change in price

Elastic demand
occurs when demand changes greatly for a small change in price

$$\textbf{Price elasticity of demand} = \frac{\text{\% change in quantity demand}}{\text{\% change in price}}$$

New-Product Pricing Strategies

New-Product Pricing Strategies

Market-skimming pricing is a strategy with high initial prices to "skim" revenue layers from the market

Market-penetration pricing sets a low initial price in order to penetrate the market quickly and deeply to attract a large number of buyers quickly to gain market share

Product Mix Pricing Strategies

Product Mix Pricing Strategies

- Product line pricing
- Optional product pricing
- Captivate product pricing
- Product bundle pricing

Product Mix Pricing Strategies

Product line pricing takes into account the cost differences between products in the line and consumer perceived value.

Product Mix Pricing Strategies

Optional-product pricing takes into account optional or accessory products along with the main product

Product Mix Pricing Strategies

Captive-product pricing involves products that must be used along with the main product

Price Mix Pricing Strategies

Product bundle pricing combines several products at a reduced price

Price-Adjustment Strategies

Price-Adjustment Strategies

- Discount and allowance pricing
- Segmented pricing
- Psychological pricing
- Promotional pricing
- Geographic pricing
- Dynamic pricing
- International pricing

Psychological pricing

The old classic

magic number

"9"

The magic #9 --- does it make sense?

$35 vs $39

Was $60, now only $45!
Was $60, now only $49!

Research related:

Quantitative Marketing and Economics, March 2003, Volume 1, Issue 1, pp 93-110
Effects of $9 Price Endings on Retail Sales: Evidence from Field Experiments
Eric T. Anderson, Duncan I. Simester
http://link.springer.com/article/10.1023%2FA%3A1023581927405

Price as a signal for quality

- Price can act as a signal for quality,
- Especially when prior experience is limited
- But consumer’s choice is context dependent

$299 or $300

Small Difference can make big Difference

Scenario 1: ¢63 vs ¢63

Scenario 2: ¢62 vs ¢64

Two different packs of gum provided

Choices:

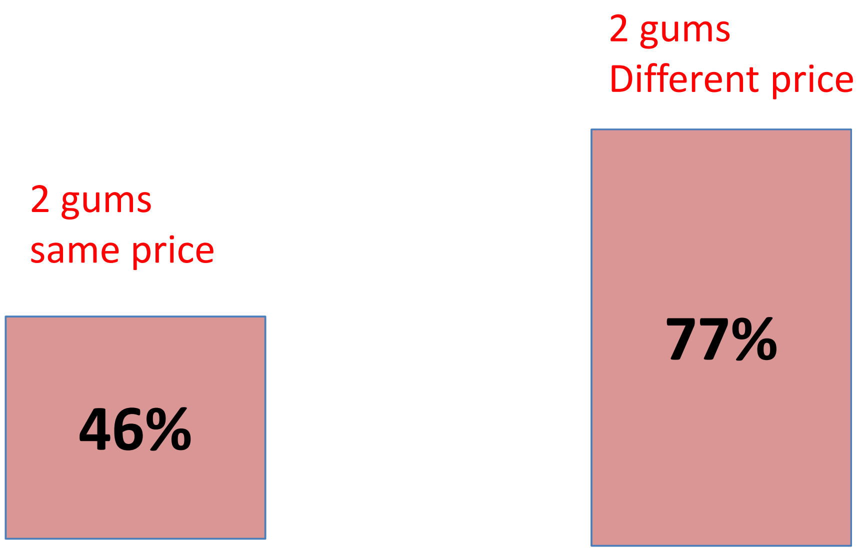
- Buy
- pass and keep the money

Source: Yale research published on Psychological Science

Adding Small Differences Can Increase Similarity and Choice

Small Difference can make big Difference

% made a purchase



Slightly different prices, more likely to buy

The Weber-Fechner Law

- "Just Noticeable Difference" - the minimum level of change to a stimulus that is required in order for the change to be noticed

- The just noticeable difference between two stimuli is directly proportional to the magnitude of the stimuli

- Weber's law states: 'the stronger the initial stimulus, the greater the change required for the stimulus to be seen as different'

- Small quiet price raise; and loud and/or bigger price cut

Reference pricing

Reference price is what buyers carry in their minds and refer to when looking at a given product.

Different consumers may have different reference price for the same product.

In some cases, marketers try to influence consumers' expectations of what a product should cost when they use reference-pricing strategies

National Brand

Erasmus+

Fairness in pricing?

$1.80 $2.50

20% **80%**

See William Poundstone's book: *Priceless: The Myth of Fair Value*

Fairness in pricing?

$1.60	$1.80	$2.50
0%	**80%**	**20%**

Fairness in pricing?

$1.80

5%

$2.50

85%

$3.40

10%

WHY?

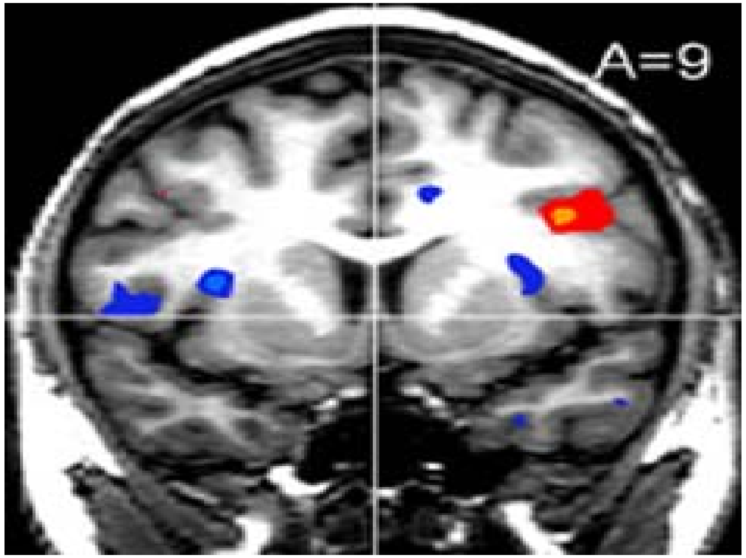
Why does reference pricing works?

Why is it easier for people to pay for a product when there is another more expensive product next to it?

How do you feel when you pay money to buy stuff?

Erasmus+

Spending can cause REAL pain



Knutson, Brian, Scott Rick, G. Elliott Wimmer, Drazen Prelec, and George Loewenstein (2007), “Neural Predictors of Pur- chases,” *Neuron*, 53 (January), 147–56

“prices do not deter spending purely through thoughts of foregone pleasures, as assumed by standard economic theory, but also through immediate pain.”--Scott Rick

Three types of buyers

Characterized by the “pain” they experience when purchasing something

- Ouch, it hurts! ☹ ---”tightwads” (24%)
- Regular pain --- unconflicted (61%)
- Not much--- spendthrift (15%)

Rick, Scott I., Cynthia E. Cryder, and George Loewenstein. "Tightwads and spendthrifts." *Journal of Consumer Research* 34.6 (2008): 767-782.

So… how can retailer apply psychology pricing to reduce the pain?

Reduce the pain--Reframing the value

- Reframing the value – make it looks smaller

€84/month vs €1,000/year

Or maybe this only works for those who can’t do the math?

Reduce the pain--- Bundling

- – reduce the pain points
  - Individual purchases create individual pain points
  - Customers prefer to complete purchase in one time than separately
    - upgrade car packages all at once
    - Compute and accessories

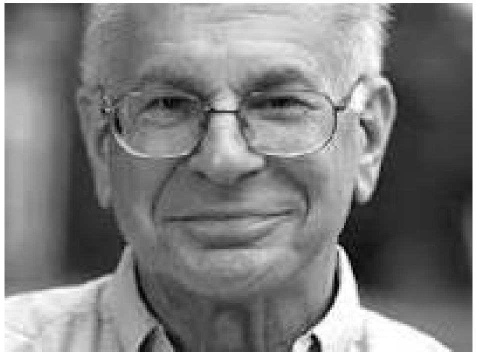
Reduced the pain– the right wording/reminder

convert consumer **without** changing the price

“a $5 fee” to “a small $5 fee”

Effect = 20%

Are consumers (we) rational?



Daniel Kahneman

Thinking, Fast and Slow

Notable for his work on the psychology of judgment and decision-making, as well as behavioral economics
Awarded the **2002 Nobel Prize** in Economic Sciences.

"System 1" is fast, instinctive and emotional;
"System 2" is slower, more deliberative, and more logical.

His empirical findings **challenge the assumption of human rationality** prevailing in modern economic theory.

In 2014, The Economist listed him as the 15th most influential economics in the world.

Source: http://en.wikipedia.org/wiki/Thinking,_Fast_and_Slow

Experiment about framing (context)

Experiment:
Would you opt for surgery if…

Scenario 1: the “survival” rate is 90 percent,
Scenario 2: the “mortality” rate is 10 percent.

The first scenario increased acceptance, even though the situation was no different.

Time v.s. Money

"Spend a little **time** and enjoy C&D's lemonade”

Time v.s. Money

"Spend a little **money**, and enjoy C&D's lemonade"

Time v.s. Money

"Enjoy C&D's lemonade."

Time, feeling, personal connection…

“How we spend our **time** says so much more about **who we are** than does how we spend our money.”---Cassie Mogilner

"Because a person's experience with a product tends to foster **feelings of personal connection** with it, referring to **time** typically leads to more favorable attitudes—and to more purchases,”– Jennifer Aaker, Professor of marketing at Stanford Graduate School of Business

Maybe retailers can draw more insights from these research and apply to retail pricing strategies ….

Reference

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