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TACTICS AND STRATEGIES IN GREAT DEAL OF DETERMINING PRICE

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Abstract: There is no limit to the number of variations in pricing strategies and tactics. The wide variety of options is exactly what enables entrepreneurs to be so creative with their pricing. This paper will examine some of the more commonly used tactics under a variety of conditions. Pricing always plays a critical role in a firm's overall strategy; pricing policies must be compatible with a company's total marketing plan.

Most business owners approach, setting the price of a new product with a great deal of apprehension because they have no precedent on which to base their decision. If the new product's price is excessively high, it is in danger of failing because of low sales volume. However, if its price is too low, the product's sales revenue might not cover costs. When pricing any new product, an entrepreneur must satisfy three objectives:

1. *Get the price accepted.* No matter how unusual a product is, its price must be acceptable to the company's potential customers.
2. *Maintain market share as competition grows.* If a new product is successful, competitors will enter the market, and the small company must work to expand or at least maintain its market share. Continuously reappraising the product's price in conjunction with special advertising and promotion techniques helps the firm acquire and retain a satisfactory market share.
3. *Earn a profit.* Obviously, a small company must establish a price for the new product that is higher than its cost. Managers should not introduce a new product at a price below cost because it is much easier to lower the price than to increase it once the product is on the market. Pricing their products too low is a common and often fatal mistake for new businesses; entrepreneurs are tempted to underprice their products and services when they enter a new market to ensure their acceptance.

Business owners have three basic strategies to choose from in establishing a new product's price: penetration, skimming, and sliding down the demand curve.

Penetration. If a business introduces a product into a highly competitive market in which a large number of similar products are competing for acceptance, the product must penetrate the market to be successful. To gain quick acceptance and extensive distribution in the mass market, a company introduces the product at a low price. In other words, it sets the price just above total unit cost to develop a wedge in the market and quickly achieve a high volume of sales. The resulting low profit margins may discourage other competitors from entering the market with similar products.

In most cases, a penetration pricing strategy is used to introduce relatively low-priced goods into a market in which no elite segment and little opportunity for differentiation exist. The introduction is usually accompanied by heavy advertising and promotional techniques, special sales, and discounts. Entrepreneurs must recognize that penetration pricing is a long-range strategy; until a company achieves customer acceptance for the product, profits are likely to be small.

Another danger of a penetration pricing strategy is that it attracts customers who know no brand loyalty. Companies that attract customers by offering low introductory prices must wonder what will become of their customer bases if they increase their prices or if a competitor undercuts them. If a penetration pricing strategy works, however, and the

product achieves mass-market penetration, sales volume increases, economies of scale result in lower unit cost, and the company earns adequate profits. The objective of the penetration strategy is to achieve quick access to the market in order to realize high sales volume as soon as possible.

Skimming. A skimming pricing strategy often is used when a company introduces a new product into a market with little or no competition. Sometimes a company uses this tactic when introducing a product into a competitive market that contains an elite group that seems willing and is able to pay a premium price. The firm sets a higher-than-nor-mal price in an effort to quickly recover the initial developmental and promotional costs of the product. Product development or start-up costs usually are substantial, owing to intensive promotional expenses and high initial costs. The idea is to set a price well above the total unit cost and to promote the product heavily to appeal to the segment of the market that is not sensitive to price. This pricing tactic often reinforces the unique, prestigious image of a business and projects a quality picture of the product.

In cases in which development costs are extremely high, as in new high technology products, the skimming technique helps the firm recoup its research and development costs in a shorter time span. As sales volume increases with the broad acceptance of the new products, the firm can lower its price. When a company employs a skimming strategy, it always can lower the price to generate additional sales to increase the firm's total revenue.

Sliding Down the Demand Curve. One variation of the skimming pricing strategy is called sliding down the demand curve. Using this tactic, the firm introduces a product at a high price. Then technological advancements enable the firm to lower its costs quickly and to reduce the product's price sooner than its competition can. By beating other businesses in a price decline, the firm discourages competitors and, over time, becomes a high-volume producer. Computers, DVD players, and other electronic equipment are a prime example of products introduced at a high price that quickly cascaded downward as companies forged important technological advances.

Sliding is a short-term pricing strategy that assumes that competition will eventually emerge. But even if no competition arises, the firm almost always lowers the product's price to attract a larger segment of the market. Yet, the initial high price contributes to a rapid return of start-up costs and generates a pool of funds to finance expansion and technological advances.

Each of the following pricing techniques can become part of the toolbox of pricing tactics entrepreneurs use to set prices for established goods and services.

Odd Pricing. Although studies of consumer reactions to prices are mixed and generally inconclusive, many entrepreneurs use the technique known as **odd pricing.** They set prices that end in odd numbers (frequently 15,49; or 99) because they believe that an item selling for 19,90 appears to be much cheaper than an item selling for 20,00. Psychological techniques such as odd pricing are designed to appeal to certain customer interests, but their effectiveness remains to be proved.

Price Lining. Price lining is a technique that greatly simplifies the pricing function. Under this system, the manager stocks merchandise in several different price ranges or price lines. Each category of merchandise contains items that are similar in appearance, quality, cost, performance, or other features. For example, most music stores use price lines for their CDs to make it easier for customers to select items and to simplify stock planning. Most lined products appear in sets of three-good, better, and best-at prices designed to satisfy different market segment needs and incomes.

Leader Pricing. Leader pricing is a technique in which the smaller retailer marks down the customary price (i.e., the price consumers are accustomed to paying) of a

popular item in an attempt to attract more customers. The company earns a much smaller profit on each unit because the mark-up is lower, but purchases of other merchandise by customers seeking the leader item often boost sales and profits. In other words, the incidental purchases that consumers make when shopping for the leader item boost sales revenue enough to offset a lower profit margin on the leader.

Geographic Pricing. Small businesses whose pricing decisions are greatly affected by the costs of shipping merchandise to customers across a wide range of geographic regions frequently employ one of the geographic **pricing** techniques. For these companies, freight expenses constitute a substantial portion of the cost of doing business and often cu deeply into already narrow profit margins. One type of geographic pricing is zone **pricing,** in which a company sells its merchandise at different prices to customer's located different territories. For example, a manufacturer might sell at one price to customer's earn of the Constanța and at another to those wests of the Romania. The small business must be able to show a legitimate basis (e.g., difference in selling or transportation costs) for the price discrimination.

Another variation of geographic pricing is the **uniform delivered pricing,** a technique in which the firm charges all of its customers the same price regardless of their location, even though the cost of selling or transporting merchandise varies. The firm calculates the proper freight charges for each region and combines them into a uniform fee. The result is that local customers subsidize the firm's charge for shipping merchandise to distant customers.

A final variation of geographic pricing is **F.O.B. seller** in which the small company sells its merchandise to customers on the condition that they pay all shipping costs. In this way, the company can set a uniform price for its product and let each customer cover the freight cost

Opportunistic Pricing. When products or services are in short supply, customers are willing to pay more for products they need. Some businesses use such circumstances to maximize short-term profits by engaging in price gouging. Many customers have little choice but to pay the higher prices. Opportunistic pricing may backfire, however, because customers know that a company that charges unreasonably high prices is exploiting them (e.g. costs of lamb in the Easter's time).

Discounts. Many small businesses use discounts, or markdowns, reductions from normal list prices, to move stale, outdated, damaged, or slow-moving merchandise. A seasonal discount is a price reduction designed to encourage shoppers to purchase merchandise before an upcoming season. For instance, many retail clothiers offer special sales on winter coats in midsummer. Some firms grant purchase discounts to special groups of customers, such as senior citizens or students, to establish a faithful clientele and to generate repeat business. It is very common for students to find merchants located near their schools who offer student discounts on all purchases. Such a strategy can be quite successful in developing a large volume of student business. Large retailers commonly offer a percentage discount to all seniors or they have a certain day of the month set aside for senior shopping with special discounts.

Multiple Unit Pricings. Multiple pricing is a promotional technique that offers customers discounts if they purchase in quantity. Many products, especially those with a relatively low unit value, are sold using multiple pricing. For example, instead of selling an item for 0,50 , a small company might offer five for 2.

Bundling. Many small businesses have discovered the marketing benefits of bundling, grouping together several products or services, or both, into a package that offers customers extra value at a special price. For instance, many software manufacturers bundle several computer programs (such as a word processor, spreadsheet, database,

presentation graphics, and Web browser) into "suites" that offer customers a discount over purchasing the same packages separately. The tourism industry has discovered a large market for travellers who want their entire vacation bundled into a one-price experience.

Optional-product pricing involves selling the base product for one price but selling the options or accessories at a much higher percentage mark-up. Automobiles are often sold at a base price with each option priced separately. In some cases, the car is sold with some of the options "bundled" together as explained previously.

Captive-product pricing is the grand-daddy of marketing pricing tactics when the base product is not functional without the appropriate accessory. King Gillette, the founder of Gillette razors, taught the business world that the money is not in the razor (the product) but in the blades (the accessory). Today we see the same pricing strategy used by Nintendo and other electronic game manufacturers that have a low margin on the product but a substantially high margin on the game cartridges.

By-product pricing is a technique in which the revenues from the sale of by-products enable a firm to be more competitive in its pricing of the main product. For years, sawmills thought that bark chips were a nuisance. Now they are packaged and sold to gardeners who use the bark chips for ground cover.

Suggested Retail Prices. Many manufacturers print suggested retail prices on their products or include them on invoices or in wholesale catalogs. Small business owners frequently follow these suggested retail prices because doing so eliminates the need to make a pricing decision. Nonetheless, following prices established by a distant manufacturer may create problems for the small firm. For example, a haberdasher may try to create a high-quality, exclusive image through a prestige pricing policy, but manufacturers may suggest discount outlet prices that are incompatible with the small firm's image. Another danger of accepting the manufacturer's suggested price is that it does not take into consideration the small firm's cost structure or competitive situation. A manufacturer cannot force a business to accept a suggested retail price or require a business to agree not to resell merchandise below a stated price because such practices violate legislation.

Follow-the-Leader Pricing. Some businesses make no effort to be price leaders in their immediate geographic areas and simply follow the prices that their competitors establish. Entrepreneurs wisely monitor their competitors' pricing policies and individual prices by reviewing their advertisements or by hiring part-time or full-time comparison shoppers. But then these entrepreneurs use this information to establish a "me too" pricing policy, which eradicates any opportunity to create a special price image for their businesses. Maintaining a follow-the-leader pricing policy may not be healthy for a small business because it robs the company of the opportunity to create a distinctive image in its customers' eyes.

Below-Market Pricing. Some small businesses choose to create a discount image in the market by offering goods at below-market prices. By setting prices below those of their competitors, these firms hope to attract a sufficient level of volume to offset the lower profit margins. Many retailers using a below-market pricing strategy eliminate most of the extra services that their above-market-pricing competitors offer. For instance, these businesses trim operating costs by cutting out services such as delivery, installation, credit granting, and sales assistance. Below-market pricing strategies can be risky for small companies because they require them to achieve high sales volume to remain competitive.

Adjustable or Dynamic Pricing. For most of the history of business, price was set through face-to-face bargaining. Merchants knew their customers and their price sensitivity and bargaining skills. The result was that the final price for identical merchandise or services could vary significantly. In the mass marketing era of the latter half of the

twentieth century when individual identity became blurred, the trend became to have an established "fixed" price for the goods or service.

With the Internet, the marketplace is beginning to see the reemergence of adjustable or **dynamic pricing.** Computer software is blending the disciplines of microeconomics, mathematics, and psychology into programs capable of analyzing a customer's price sensitivity based on that potential customer's previous purchasing behaviour. The airline and hospitality industries have been employing adjustable pricing for some time. For this reason, people on the same flight may have paid different prices for their tickets. Software firms all employ a blending of consumer data with sophisticated mathematical models to help retailers set prices in ways they believe will maximize profits.

Conclusions: In summary, there is a wide variety of pricing strategies or tactics and each has a set of specific situations in which it is most appropriate. Additionally, the pricing strategy selected must be both internally and externally compatible. Internally, the pricing strategy must be compatible with the firm's marketing objectives and the other components of the marketing mix, as well as the firm's cost structure. Externally, the pricing strategy must be consistent with the competitive realities of the market and the shifting forces of supply and demand. The forces that shape the pricing decision can change rapidly and, therefore, the pricing strategy is never completely fixed. Pricing decisions take into consideration the firm's cost, the special value the product or service creates for the buyer, as well as aggressively coping with the pricing tactics of competitors.

The underlying forces that dictate how a business prices its goods or services vary greatly among industries. In many instances, the nature of the business itself has unique factors that determine the pricing strategy.

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