Reading Assignment

Chapter 16:
Pricing Objectives and Policies

Chapter 17:
Price Setting in the Business World

Suggested Reading

See information below.

Course Learning Outcomes for Unit VII

Upon completion of this unit, students should be able to:

1. Discuss the importance of determining value proposition to the consumer.
   1.1 Relate the importance of the value proposition to competitive advantage with respect to the promotional strategies of a company.

4. Explain how the marketing mix is used to reach the target market.
   4.1 Analyze whether a company maintains a competitive advantage in reaching its target market with respect to its promotional strategies.

7. Examine pricing strategies utilized in an organization.
   7.1 Explain how a company uses components of pricing to establish its overall pricing strategy.

Unit Lesson

Price as defined by Perreault, Cannon, and McCarthy (2015), is the amount of money that is charged for something of value. Obviously, price is controllable by the company and has a significant impact on the overall profitability. The reality of setting price levels is that the optimal situation is setting prices high in order to achieve the highest profit for the company. While this is outwardly true, a marketer needs to take a step back and establish what the market will bear. In other words, it needs to be determined how high a price the target market is actually willing to pay before they will move to the competition. This ties in directly with how valuable the product/service really is to the target market. Pricing has many elements, beginning with the flexibility of the overall pricing structure. For instance, are the prices the same for every consumer that purchases the product, or does each consumer have the opportunity to bid or negotiate the price level? With respect to the large retailer Macy's, prices are not flexible because pricing is established for every customer. Contrary to this example, a Ford dealership utilizes the flexible pricing model where consumers actually negotiate the final selling price of the automobile that they are about to purchase. Flexible versus not flexible pricing strategies tend to be somewhat aligned with industries, but not always.

Perreault et al. (2015) describe three pricing objectives: profit orientation, sales orientation, and status quo orientation. Beginning with the profit orientation, this suggests that the company is interested in obtaining a certain profit level. What this means is that the company will set the pricing level based upon achieving this pre-determined profit level. Companies that tend towards profit orientation are ones that might be looking to recoup high investment costs they have on their books. The second type of pricing objective is that of sales orientation. This strategy looks at increasing sales but not necessarily profits. This suggests that marketers might not be looking at the high costs of selling the product. The idea of this pricing strategy is to increase overall market share, which can create obvious long-term competitive advantages. The final pricing strategy is that of the status quo objectives which are

also dubbed the “don’t rock the boat” strategy. This suggests that the company will meet the competition but not attempt to under-cut or over-cut the competition. The idea behind this strategy is to avoid creating a pricing battleground that could ultimately have a negative impact on ALL players in the market.

Marketers also look at specific pricing tactics when establishing their pricing policies. The tactics listed below take on a demand orientation, meaning that they weigh factors like expected customer tastes and preferences more heavily than other factors.

- Skimming: This pricing tactic involves pricing higher than that of their competitors and then dropping the price after a certain period of time. A prime example of this might be Apple who tends to introduce their products at very high price points only to drop their prices sometimes less than a year later.
- Penetration: This pricing tactic involves pricing lower than that of their competitors to generate interest and then gradually raising prices. This is probably the technique that we see most often used.
- Prestige pricing: This pricing tactic involves purposely setting the price high and maintaining that price point. The quality of the product/service is perceived to be higher with the higher price point. This tactic tends to be used by high-end companies such as BMW or Nordstrom’s. If the prices were dropped, consumers might perceive that there is something wrong with the product.

Another approach is that of a more cost orientation, meaning that the firm is basing their pricing tactics on the overall costs of producing the product or service.

- Standard mark-up pricing: This pricing tactic involves establishing the price point based upon a certain fixed percentage being added to the cost of the item.
- Cost plus pricing: This pricing tactic involves simply adding a specific amount to the cost of the item. While both of these tactics will cover the company’s costs in producing the product, it does not take into consideration market fluctuations or target market preferences.

The third approach is that of a profit orientation, which suggests that the firm’s primary interest is in reaching a certain profit level.

- Target profit pricing: This pricing tactic suggests that the company is setting an annual profit target and prices are set based upon this.
- Target return on sales pricing: This pricing tactic is much like the above except that prices are based upon an established annual return on sales.
- Target return on investment: This pricing strategy is also similar to the above except that prices are set based upon an established return on investment.

These three strategies provide the benefit of ensuring that a company is reaching certain target levels, which is very favorable for publicly held companies. On the other hand, the obvious disadvantage is that this does not take into consideration the market and consumer fluctuations.

The final approach we will discuss is that of a competition orientation, which suggests that prices are set based upon what the competition is doing.

- Customer pricing: This pricing tactic is used when a company sets their prices solely on the pricing level of the competition.
- Above-the-market, at-the-market, or below-the-market pricing: This pricing tactic is practiced when a marketer makes a concerted effort to establish one of these levels with all the products within their company. This provides a certain *brand identity* with respect to pricing.

- Loss leader pricing – This pricing tactic suggests that marketers are setting prices low on one product in order to attract consumers to other higher priced products. Understand that this is not deceptive because the lower priced items are still available for purchase.

Other pricing strategies could include the use of discount policies or reductions from list prices. This could involve quantity discounts, seasonal closeouts, trade discounts, or simply sale prices. At the end of the day, consumers love to feel as if they have just received a good deal, which this strategy reinforces. Perception is half the game when it comes to establishing an effective pricing strategy for a company's target market.

References

Perreault, W., Jr., Cannon, J., & McCarthy, J. (2015). *Essentials of marketing: A marketing strategy planning approach* (14th ed.). New York, NY: McGraw-Hill.

Suggested Reading

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