METHODS OF PRICING STRATEGIES

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Pricing Strategies

- Marketing Skimming
- Value Pricing
- Loss Leader
- Psychological Pricing
- Going Rate (Price Leadership)
- Tender Pricing
- Price Discrimination
- Penetration Pricing
- Cost Plus Pricing
- Contribution Pricing
- Target Pricing
- Marginal Cost Pricing
- Absorption Cost Pricing
- Destroyer Pricing
- Influence of Elasticity

Market Skimming Pricing

- High Price low volume
- Skim the Profit from the Market
- Suitable for the products that have short life cycle or Which will face competition at some point in future.
- Examples; Play Station, Digital Technology & DVD etc.

Value Pricing

- Based on consumer Perception.
- Price charged according to the Customers Perception.
- Price set by the company as per the perceived value.
- Example; Status Products/ Exclusive Products.

Loss Leader Pricing

- 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

- 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 Pricing

- 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

- 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 Pricing

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

Penetration Pricing

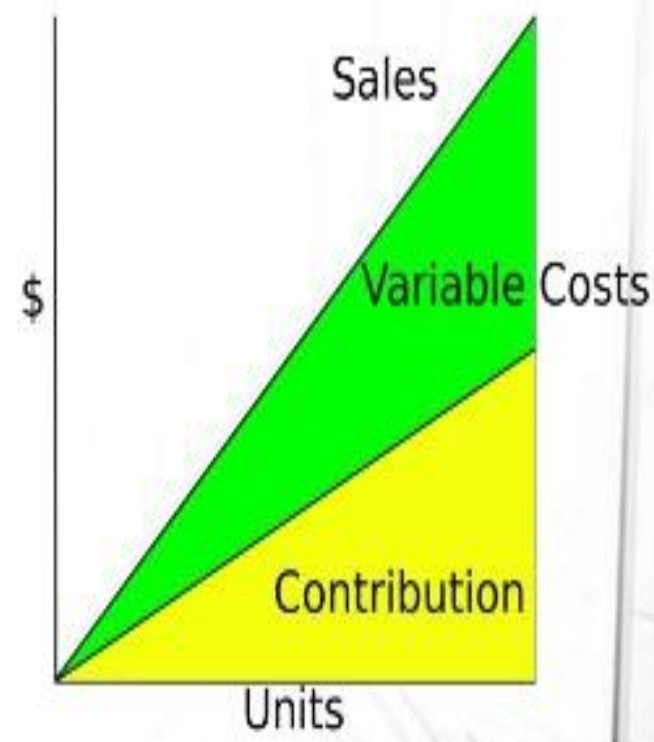
- Price set to 'penetrate the market'
- 'Low' price to secure high volumes
- Typical in mass market products – chocolate bars, food stuffs, household goods, etc.
- Suitable for products with long anticipated life cycles
- May be useful if launching into a new market

Cost Plus Pricing

- Cost-plus pricing is a pricing strategy that is used to maximize the rates of return of companies.
- Cost-plus pricing is also known as mark-up pricing where cost + mark-up = selling price.
- In practice, most firms use either value-based pricing or cost-plus 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

- 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

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

$$MC = \frac{\Delta \, TotalCost}{\Delta \, Output} = \frac{\$80}{2} = \$40$$

Absorption 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

Destroyer 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