SOS POLITICAL SCIENCE AND PUBLIC ADMINISTRATION

MBA FA – 406(b) Optional Paper

SUBJECT NAME: FUNDAMENTALS OF RETAIL MARKETING

UNIT-IV

TOPIC NAME: Retail Pricing, Pricing Flexibility And Determining Pricing Strategy

Definition: A retail price is the cost paid for a good at retail stores. It is a term applied to the price that final consumers pay at retail outlets to differentiate from intermediate prices paid upward in the supply chain.

The retail price is the final price that a good is sold to customers for, those being the end users or consumers. That means that those customers do not buy the product to re-sell it but to consume it. Retail price is differentiated from manufacturer price and distributor price, which are prices set from one seller to another through the supply chain. In competitive, free markets, the final seller or retailer sets the retail price considering costs as well as supply and demand conditions.

When setting the price, the retailer will try to obtain an appropriate profit margin but at the same time to show an attractive price in comparison to competitors. Anyway, the manufacturer can recommend a retail price in order to have some influence in the decision and thus to guarantee a price aligned to the marketing strategy.

What is flexible pricing? Definition and examples

Flexible pricing is a business strategy in which a product's final price is open for negotiation. In other words, customers and sellers can get together and try to alter the price, i.e., either knock it down or push it up. Flexible pricing does not only apply to the price of goods but services too. It is, in fact, a very common strategy in tailor-made services.

The term may also refer to adapting one's prices more closely to market forces. Market forces are the forces of supply and demand. When demand rises or supply declines, prices go up. Conversely, when demand declines or supply increases, prices fall.

Flexible pricing – example

A carpenter, for example, charges the customer according to the amount of customization the customer requested. The carpenter also takes into account how much he believes the customer can afford.

Customers subsequently negotiate the price according to their understanding of the market.

Flexible pricing contrasts with fixed pricing. Fixed pricing is common among large corporations and retailers. If I go to a major supermarket chain, I cannot negotiate the price of goods for sale.

What is a pricing strategy?

A pricing strategy is the method of pricing a business uses to determine how much to sell their goods or services for. It's one of the most commonly overlooked and undervalued revenue levers in business. Carefully selecting the right pricing strategy takes a deep understanding of your product, your market, and your customers.

Cost plus pricing: The oldest and simplest (mostly) method of setting prices

Cost plus pricing is the simplest method of determining price, and embodies the basic idea behind doing business. You make something, sell it for more than you spent making it (because you've added value by providing the product), and buy something nice with the difference. In practice, a lot of companies calculate their cost of production, determine their desired profit margin by pulling a number out of thin air, slap the two numbers together and then stick it on a couple thousand widgets. It's really that simple. This method involves very little market research, and also doesn't take into consideration consumer demands and competitor strategies.

5 common pricing strategies

Pricing a product is one of the most important aspects of your marketing strategy. Generally, pricing strategies include the following five strategies.

Cost-plus pricing—simply calculating your costs and adding a mark-up

Competitive pricing—setting a price based on what the competition charges

Value-based pricing—setting a price based on how much the customer believes what you're selling is worth

Price skimming—setting a high price and lowering it as the market evolves

Penetration pricing—setting a low price to enter a competitive market and raising it later

Competitive based pricing: Essentially, ineffective plagiarism

Competitive based pricing is a lot like plagiarism - you decide not to do your homework, so you copy that of those who have already done some work (or that you're assuming have done some work). Obviously the market doesn't dole out suspensions for copying prices, but the processes of swiping an essay and competitor based pricing are pretty similar. Also called strategic pricing, this method involves looking at the prices set by other businesses in the same sector, and then adopting those numbers, plus or minus a few percent according to how your product looks that day. The dartboard gets smaller, because there's more data here, allowing you to rely on your competitors to do the work for you (as long as you trust they actually know what's going on in the market).

Competitive based pricing remains a simple, low risk way of quickly gauging prices, and in some cases it can be fairly accurate. Yet, it leads to enormously large missed opportunities,

because companies employing the strategy end up not assessing their true value and get caught in a race to the bottom through industry group think.

Value based pricing: It's all about the customer

A value based pricing strategy works to determine the true willingness to pay of a target customer for a particular product by utilizing customer data. Most common pricing strategies and methodologies forget about the customer, instead focusing on internal reasons and/or competitive metrics to justify prices. Yet, customers don't care how much something cost you to make or your competitors, they care how much value they're receiving at a particular price. By maintaining this customer focus, value based pricing provides real data, helps you develop higher quality products, and even improves customer loyalty. Simply put, you have the greatest amount of data to make an informed decision about your profit maximizing price. Thus, shrinking down the dartboard.

Of course, value based pricing isn't perfect. The process requires time and resources, along with consistent dedication, not just a "set it and forget it" mentality, especially because the willingness to pay differs for different customer personas, regions, and even offers. A 100% accurate prediction is impossible, but we can get pretty darn close.

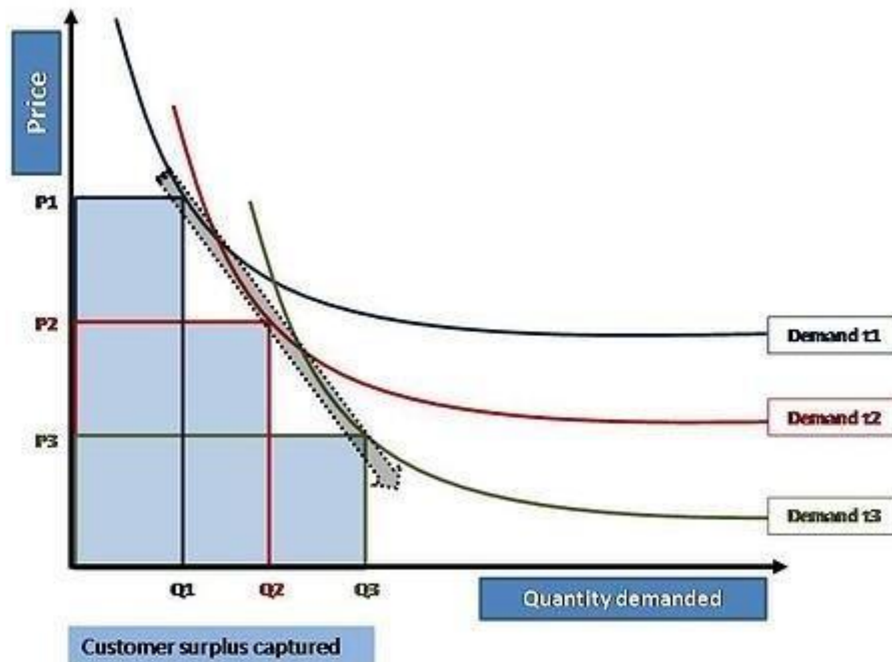
To summarize, almost everyone in the software and SaaS space will benefit from value based pricing. Even individuals in retail, media, etc. can benefit from the methodology. It takes dedication, but when done right, provides enormous benefits in terms of more profit, better and more competitive products, and customer oriented marketing and development.

Price skimming

Price skimming is the strategy of charging a relatively high price during the launch of a new, innovative product and then lowering the price over time to access different points on the demand curve.

How does Price Skimming Work?

Customers known as early adopters will pay steeper prices for a cutting edge product if it's marketed as a "must have", whether the price accurately reflects the value or not. Eventually, prices are lowered to follow the product demand curve and attract more price-sensitive customers. Theoretically, as each customer segment is "skimmed" off the top a company can capture some of the consumer surplus by charging the maximum price each segment is willing to pay.



"Theoretically" is the key word here, because although price skimming can effectively segment the market, it's almost impossible for the strategy to capture all of the consumer surplus. Price skimming is most effective when the product follows an inelastic demand curve, meaning the quantity demanded doesn't rise or fall drastically in response to a change in prices (for more on this, see our post on price elasticity). While necessities like gasoline and electricity are almost always inelastic, state-of-the-art products like the iPhone can potentially walk the same path. Let's uncover the pros and cons of price skimming before exploring the market characteristics that make the strategy a viable tactic for your business.

What is Penetration Pricing?

Penetration pricing is a pricing strategy that is used to quickly gain market share by setting an initially low price to entice customers to purchase from the company. Such pricing strategy is generally used by new entrants into a market. An extreme form of penetration pricing is called predatory pricing.

Rationale Behind Penetration Pricing

It is common for a new entrant to use a penetration pricing strategy to compete effectively in the marketplace. Price is one of the easiest ways to differentiate new entrants among existing market players. The overarching goal of the pricing strategy is to:

- Capture market share
- Create brand loyalty
- Switch customers from competitors
- Generate significant demand and utilize economies of scale

- Drive competitors out of the market

Situations where penetration pricing works effectively:

- When there is little product differentiation
- Demand is price-elastic
- Where the product is suitable for a mass market (utilizing economies of scale)