DEPARTMENT OF COMMERCE (CA)

NON MAJOR ELECTIVE II - MARKETING (Semester-VI)

III-UG **Sub Code-18BCA6EL**

UNIT – III

Pricing – Objectives – Pricing policies – Different pricing methods

Pricing

Pricing is the process whereby a business sets the price at which it will sell its products and services, and may be part of the business's marketing plan. In setting prices, the business will take into account the price at which it could acquire the goods, the manufacturing cost, the marketplace, competition, market condition, brand, and quality of product.

Objectives of pricing

- Maximize long-run profit
- Maximize short-run profit
- Increase sales volume (quantity)
- Increase monetary sales
- Increase market share
- Obtain a target rate of return on investment (roi)
- Obtain a target rate of return on sales
- Stabilize market or stabilize market price: an objective to stabilize price means that the marketing manager attempts to keep prices stable in the marketplace and to compete on non-price considerations. Stabilization of margin is basically a cost-plus approach in which the manager attempts to maintain the same margin regardless of changes in cost.
- Company growth
- Maintain price leadership
- Desensitize customers to price
- Discourage new entrants into the industry
- Match competitor's prices
- Encourage the exit of marginal firms from the industry
- Survival
- Avoid government investigation or intervention
- Obtain or maintain the loyalty and enthusiasm of distributors and other sales personnel
- Enhance the image of the firm, brand, or product
- Be perceived as "fair" by customers and potential customers
- Create interest and excitement about a product
- Discourage competitors from cutting prices
- Use price to make the product "visible"
- Help prepare for the sale of the business (harvesting)
- Social, ethical, or ideological objectives

Pricing Policies
Pricing policy refers to how a company sets the prices of its products and services based on costs, value, demand, and competition. Pricing strategy, on the other hand, refers to how a company uses pricing to achieve its strategic goals, such as offering lower prices to increase sales volume or higher prices to decrease backlog.

- **Cost-Based Pricing**

Cost-based pricing involves the determination of all fixed and variable costs associated with a product or service. After the total costs attributable to the product or service have been determined, managers add a desired profit margin to each unit such as a 5 or 10 percent mark-up. The goal of the cost-oriented approach is to cover all costs incurred in producing or delivering products or services and to achieve a targeted level of profit.

- **Value-Based Pricing**

Value prices adhere to the thinking that the optimal selling price is a reflection of a product or service's perceived value by customers, not just the company's costs to produce or provide a product or service. The value of a product or service is derived from customer needs, preferences, expectations, and financial resources as well as from competitors' offerings. Consequently, this approach calls for managers to query customers and research the market to determine how much they value a product or service. In addition, managers must compare their products or services with those of their competitors to identify their value advantages and disadvantages.

- **Demand-Based Pricing**

Managers adopting demand-based pricing policies are, like value prices, not fully concerned with costs. Instead, they concentrate on the behaviour and characteristics of customers and the quality and characteristics of their products or services. Demand-oriented pricing focuses on the level of demand for a product or service, not on the cost of materials, labour, and so forth.

- **Competition-Based Pricing**

With a competition-based pricing policy, a company sets its prices by determining what other companies competing in the market charge. A company begins developing competition-based prices by identifying its present competitors. Next, a company assesses its own product or service. After this step, a company sets it prices higher than, lower than, or on par with the competitors based on the advantages and disadvantages of a company's product or service, as well as on the expected response by competitors to the set price. This last consideration—the response of competitors—is an important part of competition-based pricing, especially in markets with only a few competitors. In such a market, if one competitor lowers its price, the others will most likely lower theirs as well.

Pricing Method

Pricing method can be seen as the process of ascertaining the value of a product or service at which the manufacturer is willing to sell it in the market. The cost, market competition and demand are the three significant factors which influence a product's price.

Pricing of products or services is a crucial decision-making strategy of the firm. Since it has a long-lasting impact over the business and its existence. Hence, a suitable pricing method needs to be adopted for this purpose.

Different Pricing Methods

1. Cost-Oriented Methods
    - Cost Plus Pricing
    - Mark-up Pricing
    - Marginal Cost Pricing
    - Target Return Pricing
    - Break-Even Pricing
    - Early Cash Recovery Pricing
2. Market Oriented Methods
    - Going Rate Method
    - Sealed Bid Pricing Method
    - Customer-Oriented Method
3. Other Pricing Methods
    - Market Skimming Pricing
    - Limit Pricing
    - Peak Load Pricing
    - Bundle Pricing
    - Psychological Pricing
    - Internet Pricing Models

1. Cost-Oriented Methods

These are the traditional methods of product pricing. The major factors which influence the product price are the fixed cost, variable cost and other overheads incurred in manufacturing the products.

- **Cost Plus Pricing**

Cost-plus pricing is one of the simplest ways of price determination. A certain percentage of cost is added as a profit margin to the value of the product to acquire the selling price.

- **Mark-up Pricing**

It is a form of cost-plus pricing, but here the profit margin is presented as a percentage of expected return on sales.

- **Marginal Cost Pricing**

The primary aim of the company adopting this pricing method is to meet its marginal cost and overheads. The marginal costing method is suitable for entering the industries which are dominated by giant players, posing a fierce competition for the organization to sustain in the business.

- **Target Return Pricing**

The pricing objective in target return method is to attain a certain level of ROI (Return on Investment).

- **Break-Even Pricing**

This method is similar to break-even analysis, where the company needs to price the products such that it generates profit after recovering the fixed and variable costs. The selling price should be equal to or more than the break-even price (the point at which the sales revenue matches the cost of goods sold).

- **Early Cash Recovery Pricing**

When it comes to rapidly growing technological products or the ones with a short life cycle, the cost needs to recover as early as possible. This method is very similar to target return pricing; the only difference is that it considers a high value of return on investment owing to a short recovery period.

2. Market-Oriented Methods

In a highly competitive market, the company cannot survive with cost-oriented pricing. Hence, it needs to price its products according to the market demand and competitor's pricing strategy.

- **Going Rate Method**

'Follow the crowd' method is based on market competition, where the company price its product similar to the competitor's product price. If the market leader reduces the price of its product, the organization also needs to decrease its product price, even if the latter's cost of production is high.

- **Sealed Bid Pricing Method**

When it comes to industrial marketing or government projects, the supplier needs to bid specific product price, which he/she assumes to be the lowest, in a sealed quotation.
In other words, the organization needs to fill a tender, which indicates its costing and competitiveness. The pricing should be done smartly by estimating the profit margin at different price levels and enclosing the most competitive price.

- **Customer-Oriented Method**

This method is also called perceived value pricing. It is demand-based pricing where the company determines the product price on value perception in terms of consumer demand for the particular goods or service. This perceived value is based on the following constituents:

  - **Acquisition Value**: The acquisition value is based on the opportunity cost of a product or service, which is estimated through the comparison of the perceived benefit and the perceived sacrifice.
  - **Transaction Value**: The comparison of the customer's reference price (assumed or quoted price) with the actual price paid for the product or service is the transaction value.

3. Other Pricing Methods

There are specific other methods for determining the price of a product or service, other than considering the cost or market competition as the basis. These are explained in detail below:

- Market Skimming Pricing

The skimming method is usually implemented in case of speciality, luxury or innovative products.
Here, the company avails the profit opportunity in the initial stage of marketing by selling the products at a high price in a non-price-sensitive market segment. Later, the prices are dropped down gradually to sustain in the market.

- Limit Pricing

This is a defensive pricing strategy. The company price its products immensely low (and this price is known as entry forestalling price), to retain the monopoly in the market. It is done to discourage the entry of competitors by presenting the business as unattractive and non-profitable.

- Peak Load Pricing

The peak load method is demand-based pricing, where the companies charge high prices in the peak seasons or period when the demand for the product is quite high. However, in the off-peak time or season when the demand falls, the prices are kept low.
It is applied for seasonal product pricing, airline travel pricing, tourism package pricing, etc.

- Bundle Pricing

Bundling refers to compiling two or more products together and selling it as a single product. The company prices the complete bundle at a single price known as the offer price.
An organization can either opt for pure bundling, where the products in a bunch are strictly not available individually. Or it may go for a mixed bundling, i.e. the products in a bundle can be sold separately but at a higher price.

- Psychological Pricing

This pricing method aims to influence the consumers mentally by posing a low product price.
Here, the product is priced slightly less than a round figure, for instance: a product is priced at ₹99 instead of ₹100 or 1.98$ instead of 2$. This makes the consumer assume that the product price lies within the range of ₹100 or 2$ and therefore it is worth buying.

- Internet Pricing Models

Internet is a modern communication platform and therefore, provides vast scope for carrying out marketing activities. The different pricing methods for internet services (as a product) are as follows:

Priority Pricing: The consumer's priority for service quality determines the price of internet services; thus, the price increases with the quality of internet service.

Flat-Rate Pricing: The consumer is charged a fixed amount for availing the internet services for a defined period irrespective of the sage.

Usage-Sensitive Pricing: The utility tariff is divided into two sections, the provider first charges for the service connection and then for the usage in terms of price per unit (bit).

Transaction-Based Pricing: Here, the price is first charged for service connection and then each transaction is separately chargeable.

Precedence Model: The pricing here, is based on the security provided to the existing customers by setting up the priority of different applications. Data packets are formed based on network preference and are given different precedence numbers. In case of congestion, the packets are sent in the sequence of their assigned precedence numbers.

Smart Market Mechanism Model: This model is purely dependent on network congestion. It functions through a dynamic bidding system where the bit price fluctuates with the level of congestion or traffic in the network. The bidder with the highest bit or unit price wins the deal. Every business organization has a different objective; not all the companies aim at profit-making. Some may look forward to capturing the market and others may focus on long term existence.

Thus, these organizational goals determine the pricing methods to some extent. However, the prevailing market trends or industry type also influence these decisions massively.

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