



Price

- Price means different things to different people:
 - **Buyers**
 - Price is the **opportunity cost**
 - **Sellers**
 - Price represents revenue, and so affects profits
 - **Government**
 - Changes in price affect inflation
- Therefore, in business studies we define price as:

*“The amount of money for which something is exchanged
IRRESPECTIVE of its value or worth”*





Pricing Strategies

● There are two main types of pricing strategies

SHORT-TERM

Usually used for promotional or tactical reasons

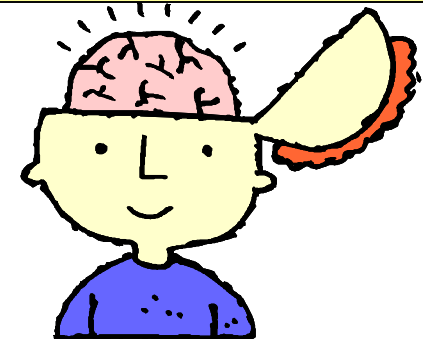
- Penetration Pricing
- Market Skimming
- Discounts & Sales
- Loss-Leader Pricing



LONG-TERM

Usually used for strategic reasons

- Demand-Based Pricing
- Cost-Based Pricing
- Competition-Based Pricing
- Psychological Pricing





Short-Term Pricing Policies

- There are a number of short-term policies which are often used for promotional reasons:
 - **Penetration Pricing**
 - Charging an initially low price
 - Used to establish a new product, to encourage retailers to stock it and consumers to try it
 - **Market Skimming**
 - Charging a high price when a product is unique i.e. mobile phones
 - Maximises revenue whilst consumers have no alternative
 - **Discounts & Sales**
 - Used to sell discontinued or unfashionable products
 - **Loss Leader Pricing**
 - Used commonly by retailers to attract customers into their store in the hope they will then make further purchases
 - Also used with games consoles





Demand-Based Pricing

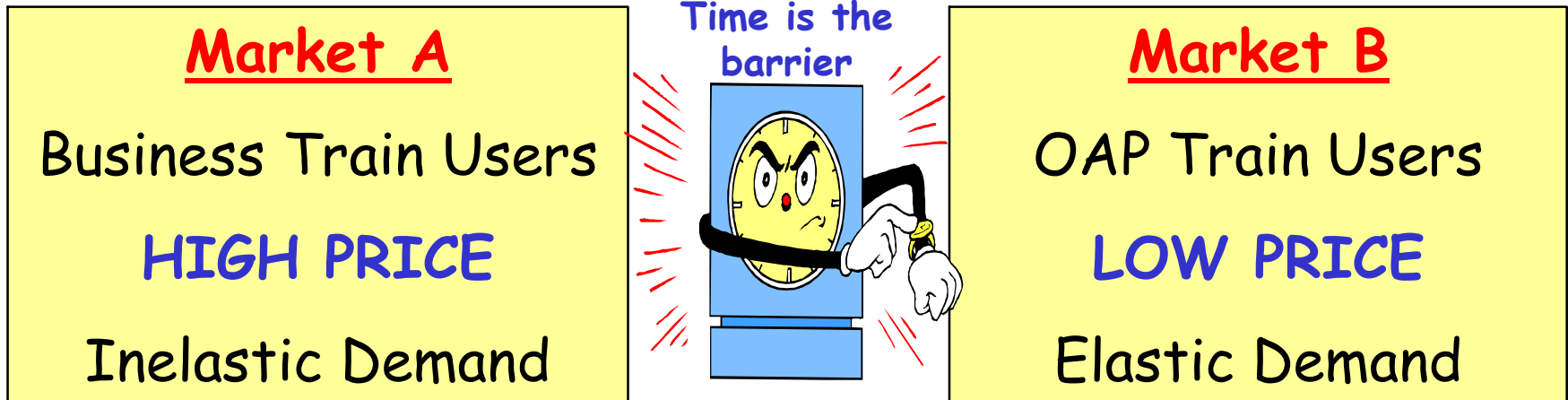
- Where this method is used, a high demand leads to a high price
- This pricing method has 2 main advantages
 - It allows **price discrimination** to be used
 - The price is determined naturally by market forces
- However, it has 1 main disadvantage
 - Unit costs will remain the same irrespective of the price, thus firms run the risk of making losses
- Demand-based pricing is therefore only used for selected products, mainly where discrimination can take place





Price Discrimination

- This is where a firm can charge different **market segments** different prices for an **IDENTICAL** product
- Three conditions **MUST** hold if price discrimination is to be used:
 - The firm must have significant **market power**
 - The firm must have more than one market, with a **barrier** between them
 - **Elasticity** in the different markets must be different
- E.g.:





Cost-Based Pricing

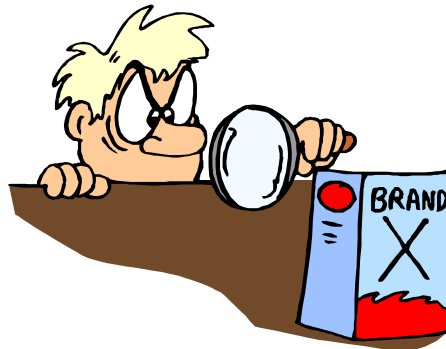
- This is where firms set prices on the basis of production costs
- There are 3 main methods:
 - **Cost-Plus Pricing (Mark-up)**
 - Here a % profit is added to the average cost per unit
 - Simple and ensures revenue is greater than costs
 - Does not account for market conditions
 - **Absorption/Full Cost Pricing**
 - Here the firm allocates indirect costs to particular products e.g. heating costs
 - Ensures that revenue is greater than costs
 - Inflexible and more complex to calculate
 - **Marginal/Contribution Pricing**
 - Here the firm allocates direct costs & required contributions
 - More flexible - less successful products can make less contribution
 - Can be very complex to calculate





Competition-Based Pricing

- This method considers competitors prices
- Used where goods are **homogeneous** and competition is fierce (e.g. **Oligopolistic markets**)
- There are 4 main types:
 - **Price Leadership**
 - Used by market-leaders to set prices that others are likely to follow
 - **Going Rate Pricing**
 - Used by non-leading firms trying to avoid a price war
 - **Destroyer Pricing**
 - Used to eliminate competition by setting very low prices
 - **Close Bid Pricing**
 - Used when firms have to tender bids for a contract





Psychological Pricing

- Where firms set prices to influence consumer thinking
 - e.g. at £99.99 firms can claim that a product is “less than £100 pounds” in their promotional literature
- Sometimes this is used to affect consumer perceptions of their products
 - e.g. many people believe that more expensive means better quality, so a high price could be charged to create a high quality image

