Chapter Objectives

To define the terms price and price planning
To demonstrate the importance of price and study its relationship with other marketing variables
To differentiate between price-based and nonprice-based approaches
To examine the factors affecting pricing decisions

Considerations in Price Planning

Evans & Berman
Chapter 20

Price Planning

Through price planning, each price places a value on a good or service. Price represents the value of a good or service for both the buyer and seller. Pricing can involve both tangible and intangible factors.

Value and Pricing

- Where does value come from?
- How is value shaped?
- How is value integrated with consumer behavior with regard to pricing?
- How is value integrated into new strategic marketing and management plans?

These are major marketing considerations relative to the increased importance of pricing strategies over the past thirty years.

Value Added and Pricing

- Firms benefit by increasing the value added at any/each stage of an item’s production.
- The food industry adds value by processing products to save consumers time.
- Carrots/lettuce—when washed, cut, and packaged—have significant value added for consumers.

Examples of Value-Added Products

Each of these products has differential advantages that lead to greater company control over prices and improved profits:
- Variety and types of bread, milk, and vegetables
- Unique restaurants
- Convenience stores
- Trendy fashions
- Sports equipment
**Value Subtractors**

Value may also be diminished at any stage of an item's production or distribution, such as with processed food—which will adversely affect a firm:

- Contaminated products, such as meat, or any questionable issues may become prime value subtractors.
- Negative PR, ads, and independent media reports on other issues, such as human rights, insider trading, and discriminatory actions, may result in severe consequences.

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**The Role of Price in Balancing Supply and Demand (1)**

![Supply and Demand Graph](chart)

**The Role of Price in Balancing Supply and Demand (2)**

At equilibrium ($P_E$, $Q_E$), the quantity demanded equals the supply.

At price $P_1$, consumers demand $Q_1$ of an item. However, at this price, suppliers will make available only $Q_2$. There is a shortage of supply of $Q_1 - Q_2$. The price is bid up as consumers seek to buy greater quantities than offered at $P_1$.

At price $P_2$, suppliers will make available $Q_3$ of an item. However, at this price, consumers demand only $Q_2$. There is a surplus of supply of $Q_3 - Q_2$. The price is reduced by sellers in order to attract greater demand by consumers.

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**Price-Based and Nonprice-Based Approaches**

- **Price-Based Approach**—Sellers influence consumer demand primarily through changes in price levels.
- **Nonprice-Based Approach**—Sellers downplay prices as a factor in consumer demand by creating a distinctive good or service via promotion, packaging, delivery, customer service, availability, and other marketing factors.

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**Consumer Perception and Price**

- Consumer behavior is often based on the individual's perception and other psychological characteristics.
- The more unique a product offering is perceived by the consumer, the greater a firm's freedom to set prices above competitors.

Perception: two faces or a vase? What the consumer perceives affects value.
In a price-based strategy, sellers influence consumer demand through price changes. This strategy is easy to copy. It is flexible and quick. Government monitors pricing strategies.

With a nonprice-based strategy, the more unique an item is, in the consumer’s eyes, the less driven he/she is by price. Other marketing factors influence demand. Prestige items can maintain higher prices.

A company operating at $P_1Q_1$ may increase sales by lowering its prices to $P_2$. This increases demand to $Q_2$. A firm relying on a price-based approach must lower its prices to increase sales.

Through a nonprice-based approach, the firm shifts the consumer demand curve to the right by successfully differentiating its products from competitors. This enables the firm to: (a) increase demand from $Q_1$ to $Q_2$ at price $P_1$, or (b) raise the price from $P_1$ to $P_2$ while maintaining a demand at $Q_1$.

The law of demand states that consumers usually purchase more units at a low price than at a high price. When demand is high and supply low, prices rise. If supply is high and demand is low, prices fall.

Price elasticity explains consumer reaction to price changes. It indicates the sensitivity of buyers to price changes in terms of quantities they will purchase. Demand may be elastic, inelastic, or unitary. Unitary demand exists if price changes are exactly offset by changes in quantity demanded, so total sales revenue remains constant.
Demand Elasticity Is Based on

Availability of substitutes and the urgency of need.
- Brand loyal consumers do not want to settle for less than the most desirable attributes of a particular product.
- Price shoppers want the best deals possible.

Elastic Demand

- Occurs if relatively small changes in price result in large changes in the quantity demanded.
- Consumers perceive there to be many substitutes and/or have a low urgency of need.
- With elastic demand, total revenue goes up when prices are decreased and goes down when prices rise.

Inelastic Demand

- Occurs if price changes have little impact on the quantity demanded.
- Consumers perceive there are few substitutes and/or have a high urgency of need.
- With inelastic demand, total revenue goes up when prices are raised and goes down when prices decline.

Economy Car = Elastic Demand

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Luxury Car = Inelastic Demand

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NYC Subway Pricing: Elastic Or Inelastic?

Price increases in NYC subway fares:
- Availability of substitutes?
- Urgency of need?
Government Actions Affecting Price Decisions

- Price Fixing Regulations
  * Horizontal
  * Vertical

- Price Advertising

- Prohibitions Against Price Discrimination Among Channel Members

- Unfair Sales Acts
  * Predatory Pricing
  * Loss Leaders

- Unit Pricing Laws

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Robinson-Patman Act

- This act prohibits manufacturers and wholesalers from price discrimination in dealing with different channel-member purchasers of products with "like" quality if it injures competition.
- Included are prices, discounts, rebates, premiums, coupons, guarantees, delivery, warehousing, and credit rates.

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Unit Pricing

- State laws often allow consumers to compare price per quantity for competing brands and for various sizes of the same brand.
- Food stores are most affected by unit-pricing laws; they often must show price per unit of measure, as well as total price.

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Price Advertising

- FTC guidelines specify standards of conduct in several areas of price advertising.
  - Firms cannot claim or imply a price reduction unless items were previously offered to public.
  - Comparative prices must be verifiable.
  - Bargain offers, "free, buy one, get one free," and "half price sale" are considered deceptive, if terms are not disclosed.
  - When running a sale, suggested list or pre-marked prices cannot be advertised as original prices unless products were actually at those prices.
  - Bait-and-switch advertising is an illegal practice.

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The Competitive Environment of Pricing

- Market-Controlled
  - Price War

- Type of Pricing Environment
  - Company-Controlled
  - Government-Controlled

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Chapter Summary

- The chapter defines the terms price and price planning.
- It demonstrates the importance of price and described its relationship with other marketing variables.
- It differentiates between price-based and non-price-based approaches.
- It examines the many factors affecting pricing decisions.