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Emerging Leaders and Entrepreneurs in Marketing, Finance, Hospitality and Management
Price is the monetary value of a product exchanged for the purpose of owning the product. Pricing may seem like a simple enough task; after all, your ultimate goal as a business is to price items so that you surpass your **break-even point** (the point at which your costs and expenses equal your revenue) and earn a profit. But there are, in fact, several pricing strategies—and several factors that may influence your choice to implement one over another.

Let’s consider the factors affecting pricing before we move on to pricing strategies. These include costs and expenses, supply and demand, consumer perceptions, and competition.

Costs and expenses refer to the money your business pays out. This includes the costs of goods that you will resell, shipping charges, supplies, rent, utilities, etc. You want to price your goods/services so that you earn more money than you have to pay out. This surplus or “net” income after you have paid all your other expenses is your profit. Suppose your SBE sells water bottles. You purchase your water bottles from a vendor, who you pay for both the cost of the water bottles and delivery of them to your school. If the cost of plastic increases, however, your vendor will have no choice but to raise the cost of the water bottles. To keep making a profit, your SBE will have to raise the price on the water bottles as well.

Supply and demand is the general principal that as the supply of an item increases, the demand for it decreases. Conversely, as the supply of an item decreases, the demand for it increases. Price is also tied to this concept. Perhaps your SBE sells school supplies. These are items every student in your school uses, so you must charge a reasonable price. If your prices for school supplies are too high, demand will go down because students can purchase their school supplies elsewhere for less. Your supply of school supplies will also go up, because you are not turning over the inventory as quickly as you would like. If your prices for the school supplies are too low, your stock (supply) will be quickly depleted as demand for the items goes up.

Consumer perceptions are preconceived notions about an item and its price. Your customers believe that the price of an item says something about it. For instance, some people will purchase an expensive handbag because they feel that its high price reflects its exclusivity.

Competition significantly affects pricing decisions. Consider the school supply example. While you need to consider supply and demand when pricing school supplies, your SBE must also consider the competition. If your school supply prices are too high, students will take their business to a local office supply store or grocery store where the items are less expensive.

Now that we’re familiar with the factors affecting pricing decisions, let’s consider the various pricing strategies.

**Product mix pricing strategies** are actually a group of several different pricing techniques:

- **Price lining** is the designation of different “lines” of products through their prices. A jewelry store might sell bracelets at price points of $50, $75, and $100. The customer views these differences in price as indicative of the quality of the items.
- **Optional product pricing** involves setting prices for accessories or options sold with the main product. This often occurs with electronics like computers; you can often buy additional benefits such as data storage space or insurance—but for a cost in addition to that of the computer itself.
A **captive product** is one that is made for use with another product. Consider perfume atomizers. While some old-fashioned atomizers are now collectibles, many atomizers are simply inexpensive containers meant to dispense perfume. The atomizer is unusable without perfume. The atomizer may be relatively inexpensive, but the high price of perfume refills makes up for this.

**By-product** pricing helps businesses get rid of excess materials used in making a product. A custom picture frame shop might offer discounts to a customer who chooses a molding already cut and in the shop as opposed to ordering a new molding from an outside vendor.

You may very well employ **bundle pricing** in your SBE. Bundle pricing involves grouping several products together for one set price. The price of the bundled products is less than that of all the products if they were to be purchased separately.

**Geographical pricing** refers to pricing products differently in different geographic locations due to the variable costs of shipping. One example of this is the fluctuations often seen in gasoline prices.

**International pricing** is a rather broad pricing strategy, for it must take into account several factors including costs, competition, laws, economic conditions, and exchange rates (among other things)—all of which can vary significantly from country to country.

**Segmented pricing** refers to setting different prices for a product, though there are no differences in the item's initial cost. The following four factors influence segmented pricing:

- **Buyer identification**—knowing who your customers are and how much they are willing to pay allows your business to set different prices for different groups of people. For example, theme parks often offer multiple “levels” of tickets. Each level is priced differently and awards the buyer of the ticket a different theme park experience. A lower priced ticket may be good for only one day and include no extra amenities, while a higher priced ticket may be good for multiple days’ entry into the park as well as meals.
- **Product design** affects a product’s price, though there often is no difference in cost between different versions of the same product. This is seen in products that are offered in different styles or colors—a cellphone case in a pattern or a standing mixer in a color will typically be more expensive than their plain counterparts.
- **Purchase location** will affect pricing, as in the purchase of items online from a standalone store in a faraway locale. Some famous restaurants offer their specialties to consumers throughout the country. Customers in Texas who purchase steaks online from a New York steakhouse will incur the costs of dry ice, packaging, and shipping that in-house diners will not.
- **Time of purchase** can affect pricing, too. Many high-end restaurants offer special early-bird prices to their patrons who dine with them before 6:00 PM, the start of the dinner rush.

**Psychological pricing** plays to the customer’s beliefs about prices and employs the following techniques:

- **Odd-even pricing** maintains that consumers “like” certain prices more than others. Retailers will often set the price of an item so that it ends in an odd number just under a round even number. The consumer sees the price of $19.99 and thinks they are getting a bargain because the price is not quite $20.00.
- **Prestige pricing** is the act of setting prices higher than average to suggest quality and luxury. The consumer believes that high price and high quality are directly related. Examples of prestige-priced products include designer shoes and handbags, jewelry, and high-end automobiles.
- **Multiple-unit pricing** involves setting prices for multiples of one particular item. For example, a supermarket might advertise that it sells two boxes of cereal for $5.00. Even if one box of cereal costs $2.50, “two for five” sounds more like a deal.
- **Everyday low prices** (abbreviated as EDLP) are just that—low prices offered to customers all the time. Offered at such big-box stores as Wal-Mart and Target, these prices are not often reduced for sales or promotions.
Promotional pricing is used during sales promotions and consists of the following techniques:

- **Loss leader pricing** refers to the markdown of a specific item below its cost. The idea is that, while the retailer will take a loss in revenue generated by the product, the product’s low price will “lead” customers into the store where they will make other purchases at full price.

- **Special-event pricing** is perhaps the most familiar of the promotional pricing techniques. You most likely hold special events in your SBE. You may run a holiday sale before the winter break and mark down all apparel and gift items in honor of this special event.

- **Rebates** are refunds given to the customer by the manufacturer. Usually a rebate requires the customer to send in proof of their purchase along with their receipt, for which they will receive payment from the manufacturer. Cell phone companies issue rebates for phone sales, often in the form of prepaid gift cards.

- Customers use **coupons** to buy products at reduced prices. Coupons are often printed on paper (in newspapers, magazines, etc.), but more and more manufacturers and retailers are distributing coupons via email that can be printed off or scanned from a consumer’s smartphone.

**Discounts and allowances** reduce the base price of an item, but they are typically given in return for a buyer (wholesaler, retailer, or consumer) doing something specific.

- **Cash discounts** are given to buyers (wholesalers or retailers) who pay their bills in full within a specified time period. Perhaps you’ve heard the term “2/10, net 30”—a common payment system. This means that the buyer must pay their bill within 30 days, but they will receive a 2% discount if they pay it within 10 days.

- **Quantity discounts** encourage buyers to purchase larger orders than they otherwise would. A vendor may offer several dozen of a product for an overall price that is less per individual item than if those items had been purchased in a smaller quantity.

- **Seasonal discounts** are offered on merchandise sold “out of season.” Retailers may sell snow gear like boots and gloves at significantly reduced prices toward the end of the winter season in order to make space for new spring inventory.

- **Allowances** refer to cash incentives given to consumers when they trade-in a used product and purchase a new one. This technique is most often employed in the automobile industry.

REFERENCES


CLASSROOM ACTIVITY

What pricing strategies do you employ in your school-based enterprise? Choose one to evaluate using the following questions:

1. Choose one product priced using this strategy. What is the product?
2. What is the cost of the product?
3. What pricing strategy did you choose for this product and why?
4. Does this product ever go on sale? Describe any promotional pricing strategies used.
5. How quickly does this product turnover? Do you think your chosen pricing strategy has been effective or should you consider pricing the item differently?
6. What have you learned from this activity that you will apply to future pricing decisions in your SBE?

CASE STUDY

Global companies tailor their businesses to the places and cultures in which they are located. The same products that sell well in one country may not sell as well in another. Because businesses’ product mixes vary from country to country, so too do their pricing strategies. This is true for one of the most successful American companies of the twenty-first century—Starbucks.

While many Americans still regard Starbucks coffee as an expensive alternative to coffee drinks they could purchase elsewhere for less or even brew at home, the Starbucks coffee shop is nonetheless a staple in American society. Its very ubiquity has worked to its advantage; three dollars for a grande latte at Starbucks may seem like a lot of money when compared to competitors’ prices, but those three dollars will also buy you convenience and trend conformity.

The success of Starbucks in America relies on the fact that America is a coffee society. Americans drink coffee at all hours of the day and for a variety of reasons. We drink it in the morning to wake up, in the afternoon to fuel our workouts, and in the evening over conversations with friends. China, on the other hand, is not a coffee society. The staple drink of the Chinese is tea, which they enjoy, like Americans do their coffee, at all hours and for all occasions. When it opened its first Chinese location in 1998, Starbucks realized that it needed to approach its business differently in China than it did in the United States. Marketing of Starbucks coffee as a casual and enjoyable-at-any-time type of beverage—and pricing it as such—would not lead to impressive sales in China as it had in the U.S. Starbucks, then, decided to market the experience of the coffee shop in its Chinese locations, as opposed to the convenience and trendiness so crucial to its American success. Starbucks in China feature dine-in service and culture-specific drinks, such as green-tea infused coffee. The sit-down Starbucks coffee experience is regarded not as an everyday occurrence, as it is in America, but as an exclusive event. A trip to Starbucks in China is not a quick stop for a coffee; it is an opportunity for a lingering indulgence. The “indulgence” of coffee is priced at a premium that further indicates its exclusivity. By pricing its beverages higher in its Chinese locations, Starbucks is effectively tailoring its pricing strategy to the cultures it serves. This builds goodwill for the brand which, in turn, translates to higher sales for the company.