Introduction

Price is the amount paid by consumers for a product. Price is a vital component of the marketing mix as it impacts on the consumer demand for the product.

The pricing level will also:

- determine the degree of value added by the business to bought-in components
- influence the revenue and profit made by a business due to the impact on demand
- reflect the marketing objectives of the business and help establish the psychological image and identity of a product.

Get the pricing decision wrong and much hard work in market research and product development can be put at risk.

Factors determining the price decision

There are a number of factors that will determine the pricing decision for a product:

1 costs of production
2 competitive conditions in the market
3 competitors' prices
4 marketing objectives
5 price elasticity of demand
6 whether it is a new or an existing product.

The significance of these is discussed in this chapter.

Pricing strategies

COST-BASED PRICING

The central idea is that firms will assess their costs of producing or supplying each unit, and then add an amount on top of the calculated cost. There are a number of different methods of cost-based pricing that may be adopted.

Cost-plus pricing

KEY TERM

cost-plus pricing adding a fixed mark-up for profit to the unit price of a product

This method is often used by retailers, who take the price that they pay the producer or wholesaler for a product, and then just add a percentage mark-up. The size of the mark-up usually depends upon a combination of the strength of demand for the product, the number of competitors and the age and stage of life of the product. Sometimes it also depends on traditional practice in the industry.

Example 1:
Cost of bought-in materials: $40
50% mark-up on cost = $20
Selling price: $60

H HIGHER LEVEL

Marginal-cost pricing

KEY TERM

marginal-cost price basing the price on the extra cost of making one additional unit of output

If an airline has an empty seat on a particular flight, to gain additional (marginal) customers it could offer a price lower than the average cost as long as it at least covered the marginal cost of carrying an extra passenger. As long as this 'special promotional price' did not become universally known – in which case all customers would demand it – this pricing method could increase sales and market share. Not all customers can be offered special deals that just cover the marginal cost – total revenue must at least cover total costs for a profit to be made.

Contribution-cost pricing

KEY TERM

contribution-cost pricing setting prices based on the variable costs of making a product in order to make a contribution towards fixed costs and profit

A product makes a contribution to fixed costs and profit if selling price is greater than variable costs. The business calculates a unit variable cost for the product and then adds an extra amount – this becomes the contribution to fixed costs. If enough units are sold, the total contribution will be enough to cover the fixed costs and to return a profit. This is widely used by:

- multi-product businesses that would find it almost impossible to allocate or divide fixed costs accurately between different products
- firms that want to attract new orders from potentially important customers
- businesses that want to sell off stock to make way for new inventories.

Example 2: A product has a variable cost of $2 per unit. The business sets a price of $3, perhaps to remain competitive, which includes a contribution to fixed costs of $1. If the firm sells 40 000 units in the year, then a total contribution of $40 000 is made. If the business allocates fixed costs of $40 000 to this product, then it will start to make

a profit after 40 000 units have been sold. If the firm sells 60 000 units, then the fixed costs will be covered and there will be $20 000 profit made.

A product that makes a positive contribution to fixed costs should, generally, continue to be produced so long as there is spare capacity in the firm. There are many firms that have excess capacity and use contribution pricing to attract extra business which will absorb the excess capacity. Examples are train companies, for which there is substantial excess capacity except in the morning and evening rush hours. It is also widely used in making one-off decisions – such as a price for a special order and the assumption is that no additional fixed costs will be incurred.

Example 3: A business makes a single product design with a variable cost per unit of $4. The annual fixed costs or overheads are $80 000. The firm decides on a contribution of $2 per unit sold. Therefore, the selling price is $6. If the business sells 50 000 units in one year, the total contribution to fixed costs becomes 50 000 × $2 = $100 000. A profit of $20 000 has been made. This firm would have to sell at least 40 000 units per year in order to break even.

H

Full-cost (or absorption-cost) pricing

KEY TERM

full-cost/absorption-cost pricing setting a price by calculating a unit cost for the product (allocated fixed and variable costs) and then adding a fixed profit mark-up

This is similar in principle to cost-plus pricing. It is often used by firms making a single type of product. For multi-product firms, full-cost pricing involves the allocation of fixed costs to different products and the calculation of the 'full cost' for each one.

Example 4: A business produces DVDs. One of its products is a range of industrial training DVDs. The annual overheads or fixed costs allocated to this product are $10 000. The variable cost of producing each training DVD is $5. The business is currently producing 5000 units per year. The total costs of this product each year are:

$$\$10\,000 + (5000 \times \$5) = \$35\,000$$

The average or unit cost of

$$\text{making each DVD} = \frac{\$35\,000}{5000} = \$7$$

The business will have to charge at least $7 each in order to break even on each unit. If the firm now adds a 300% profit mark-up, then the total selling price becomes $28.

Competition-based pricing

An example of competition-based pricing is price leadership.

KEY TERMS

competition-based pricing a firm will base its price upon the price set by its competitors

price leadership one dominant firm in a market sets a price and other firms simply charge a price based upon that set by the market leader

This often occurs in oligopolistic markets – dominated by a few firms. In petrol retailing, for example, all prices charged tend to move in line with each other – following the market leader. Is this a result of illegal collusion between the companies? This is very difficult to prove in practice. It might just be because one major player in the market, often with lowest average cost, leads a price change and the others feel obliged to follow.

H HIGHER LEVEL

Predatory or destroyer pricing

KEY TERM

predatory pricing deliberately undercutting competitors' prices in order to try to force them out of the market

This is an illegal pricing strategy in the European Union as it favours the strong, established companies unfairly compared to new entrants. In practice, it is very difficult to prove – businesses often claim that they are just adopting a loss-leader strategy – see below.

H

Going-rate pricing

KEY TERM

going-rate pricing the price charged is based upon a study of the conditions that prevail in a certain market and the prices charged by major competitors

The internet has made going-rate pricing more common because of the greater transparency that now exists as result of this global information base. Consumers can quickly compare prices of, for example, DVDs or computers, and purchase from the cheapest supplier. More firms are therefore being forced to lower their prices to the 'going rate', especially if they cannot add value to it in the form of special customer service which might have justified higher prices.

See Table 27.1 for a summary of pricing strategies.

Methods	Advantages	Disadvantages
Full-cost pricing (also applies to cost-plus)	• Price set will cover all costs of production. • Easy to calculate for single-product firms where there is no doubt about fixed cost allocation. • Suitable for firms that are 'price makers' due to market dominance.	• Not necessarily accurate for firms with several products where there is doubt over the allocation of fixed costs. • Does not take market/competitive conditions into account. • Tends to be inflexible, e.g. there might be opportunities to increase price even higher. • If sales fall, average fixed and average total costs rise – this could lead to the price being raised using this method.
Contribution-cost pricing	• All variable costs will be covered by the price – and a contribution made to fixed costs. • Suitable for firms producing several products – fixed costs do not have to be allocated. • Flexible – price can be adapted to suit market conditions or to accept special orders.	• Fixed costs may not be covered. • If prices vary too much – due to the flexibility advantage – then regular customers might be annoyed.
Competition-based and going-rate pricing	• Almost essential for firms with little market power – price takers. • Flexible to market and competitive conditions.	• Price set may not cover all of the costs of production. • May have to vary price frequently due to changing market and competitive conditions.
(H) Price discrimination (one method of market-based pricing)	• Uses price elasticity knowledge to charge different prices in order to increase total revenue.	• Administrative costs of having different pricing levels. • Customers may switch to lower priced market. • Consumers paying higher prices may object and look for alternatives.

Table 27.1 *Summary of main pricing methods*

MARKET-BASED PRICING STRATEGIES

These are normally split into two different approaches depending on the marketing objectives of the business.

Penetration pricing

KEY TERM

penetration pricing setting a relatively low price often supported by strong promotion in order to achieve a high volume of sales

Firms tend to adopt penetration pricing because they are attempting to use mass marketing and gain a large market share. If the product gains a large market share, then the price could slowly be increased.

Market skimming

KEY TERM

market skimming setting a high price for a new product when a firm has a unique or highly differentiated product with low price elasticity of demand

This aims to maximise short-run profits, before competitors enter the market with a similar product, and to project an exclusive image for the product. If rivals do launch similar products, it may be necessary for the price to be reduced over a period of time. An example of this is pharmaceutical firms, who are often given a legal monopoly for a certain number of years for new drugs. They are able to charge high prices in order to recoup their considerable investments in research and to make high profits. It is not uncommon for them to lower their prices in the last year of their legal monopoly in order to hold their market share when other companies enter. This is a typical example of market-skimming price strategy – see Figure 27.1.

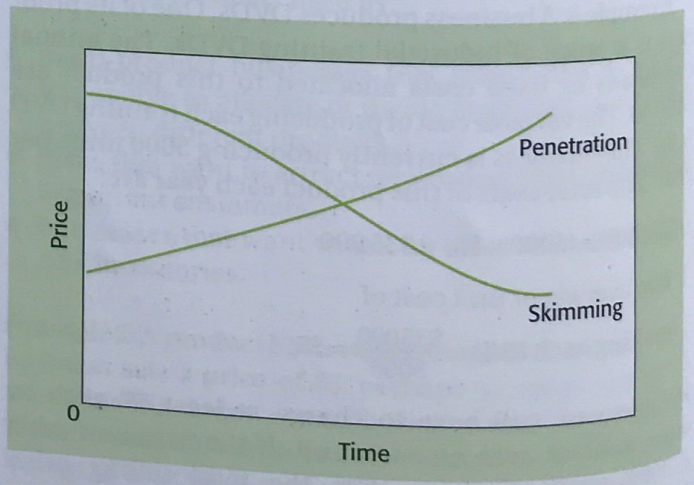

Figure 27.1 *Market-skimming and penetration pricing strategies*

H HIGHER LEVEL

Price discrimination

This takes place in markets where sub-groups of consumer exist and it is possible to charge different consumer groups different prices for the same product. An example of this would be airline operators who charge many different rates for the same journey. Firms can price discriminate if there are different groups of consumers with different elasticities of demand (see page 288). Also the firm must avoid resale between the groups and it must not cost too much to keep the groups of consumers separate. Other examples of price discrimination include selling train and bus tickets more cheaply to children or the elderly and setting different prices for products in different export markets.

Loss leaders

KEY TERM

loss leader product sold at a very low price to encourage consumers to buy other products

Loss leaders are widely used by supermarkets. Selling milk or bread at very low prices – perhaps below cost price – will encourage consumers into the stores to buy other goods on which the supermarket makes a higher profit margin. Is this fair on smaller retailers of milk and bread who cannot buy in supplies as cheaply as the large supermarkets? Other examples include computer printers sold for $40 – but the replacement ink cartridges can cost $30 each.

Psychological pricing

KEY TERM

psychological pricing setting prices that take account of customers' perception of value of the product

This has two aspects. First, it is very common for manufacturers and retailers to set prices just below key price levels in order to make the price appear much lower than it is. Therefore, $999 is used instead of $1001, and $1.99 not $2.01. In addition, psychological pricing also refers to the use of market research to avoid setting prices that consumers consider to be inappropriate for the style and quality of the product. A very low price for cosmetics or perfume, even though the costs of production may not be high, will not create the status and exclusive image that the firm is trying to portray. Potential consumers may be put off by the fact that too many people can now afford the product and the quality may not be as high as they originally believed. Similarly, prices can be so high that they exceed consumer perceptions of the quality and image of the product, and sales will be damaged as a result.

Promotional pricing

KEY TERM

promotional pricing special low prices to gain market share or sell off excess stock – includes 'buy one get one free' (see Chapter 28, pages 296 and 298)

A very widely used pricing strategy, it tends to operate for limited periods only to boost sales at times of low demand or to support the opening of a new store.

ACTIVITY 27.1

Read the case study below and then answer the questions that follow.

Car prices to rise in China?

Although Volkswagen has denied the rumour of 'general price hikes in April' for its cars in China, business analysts are predicting substantial car price rises. Due to rising costs of production – steel and other raw materials and higher labour costs – the cost of making each car in China increased on average by $400 in 2009. Can manufacturers resist these cost pressures? By how much are they prepared to cut their profit margins to stay competitive?

However, the fierce competition in China's car market has deterred many manufacturers from putting up prices. In recent years, due to increased numbers of cars being made in China and more manufacturers exporting to China, competitive pressures have put car prices on a downward trend, but that could change now that costs are rising so fast.

To avoid consumer resistance to price increases, manufacturers are increasing their profit margins in other ways. Dealers are promising quick delivery of cars to customers if they order expensive accessories and luxury items – such as leather seats. The profit margin on these decorative accessories can be as high as 30–40%, which helps to

make up for very low margins on the cars themselves. So, indirect price increases could be the solution to the very small profit margins on selling basic car models.

Source: ChinaBizIntel.com (adapted)

16 marks, 28 minutes

1 Explain why increasing costs usually lead manufacturers to raise prices to consumers. [4]

2 Why, in this case, are car manufacturers reluctant to raise prices? [4]

3 Analyse how car manufacturers such as BMW or Mercedes might still sell cars profitably in a competitive market. [8]

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ACTIVITY 27.2

Read the case study below and then answer the questions that follow.

Does the price fit?

Hartwood Hats manufactures caps for sportswear companies. The caps cost $3 each for materials and labour – the only variable costs. Last year, a total of 400 000 caps were produced and sold to two big sports firms. The fixed costs of the business amount to $200 000 per year. The marketing manager has to decide on pricing levels for the coming year and is uncertain whether to use full-cost or contribution pricing. Last year a price of $6 was set. The firm was left with spare capacity of around 100 000 caps.

15 marks, 25 minutes

1 What does contribution mean and what was the contribution per cap last year? [4]

2 What price would be charged if full-cost pricing was used and 100% mark-up added to the unit cost? [3]

3 Refer to your answer to question 3. Advise the firm on what factors it should consider before fixing the price at this level. [4]

4 If there were a 50% increase in variable costs and the contribution was lowered to $2, what profit would be made if sales remained unchanged? [4]

ACTIVITY 27.3

Read the case studies below and then answer the questions that follow.

Prices rise – but for different reasons

Case 1 Florida's theme parks increase prices

Universal Orlando is raising its one-day, one-park adult ticket prices from $63 to $67 just days after Disney World also raised its prices. A Universal spokesman refused to comment on whether the price rise was in response to Disney's announcement. Disney has raised its ticket prices twice this year. The latest increase takes an adult ticket to $67 – Universal has set exactly the same price.

Case 2 Carib Cement price adjustment

Caribbean Cement Company Limited has announced that from July the price of cement products would be adjusted by an average of 15%. The company blamed significant increases in input costs, such as electricity and oil prices. A spokesperson said, 'The price rises were inevitable as when costs rise, our profits will decline unless prices are increased too.' The company claims that its prices are still among the lowest in the region.

Case 3 Growing demand allows ethanol producers to increase prices

Growing demand in the USA for the corn-based fuel, ethanol, has boosted prices for this environmentally

friendly alternative to petrol. The supply of ethanol is limited due to no spare capacity in the industry, but 33 new plants are being planned for the USA. Currently, ethanol fuel is now no cheaper than ordinary petrol.

18 marks, 23 minutes

1 Identify the different pricing methods used in case 1 and case 2. [2]

2 In case 1, explain **two** potential benefits to Universal of the company *not* increasing its prices following the decision by Disney World to increase its entry fee. [6]

3 Under what circumstances might you recommend to the managing director of Carib Cement that the company should *not* increase its prices, despite higher costs. Explain your answer. [6]

4 Explain what might happen to the price of ethanol in the USA when the 33 new plants start producing it. [4]

H HIGHER LEVEL

Supply and demand

In a free market, the market or equilibrium price is determined by supply and demand. The prices of most of the world's commodities, such as agricultural goods, oil, copper, lead and so on, are determined by the forces of supply and demand. This applies to foreign currency exchange rates – have you ever noticed how frequently these change? Supply means the quantity that producers are willing to sell at the existing market price. If supply *increases* for a product, such as cocoa, then the world price is likely to *fall*. Factors that determine supply and could cause an increase in the supply of cocoa include:

- good harvest conditions
- more growers entering the market
- government subsidies to growers
- release of unsold stocks on to the market.

Demand means the quantity that customers are willing and able to buy at the existing market price. An *increase* in demand for cocoa is likely to *increase* the world price for it. Factors that could increase demand for cocoa include:

- increasing consumer incomes
- more advertising for chocolate
- increased prices of non-chocolate-based confectionery
- rising population.

PRICE ELASTICITY OF DEMAND (PED)

The quantity demanded for most products increases as the price of them falls. This can be shown on a demand curve – look at Figures 27.2 and 27.3. Notice that D_2 has a steeper gradient than D_1. What impact does the slope or gradient of the curves have on the demand levels for these two products when prices are changed? You will notice that, when the price of both products is increased by the same amount, the reduction in demand is greater for product B than it is for product A. This could be very important information for the marketing manager because the total revenue (total revenue = price × quantity) for product A has actually increased, but for B it has fallen, as can be seen by the size of the shaded areas.

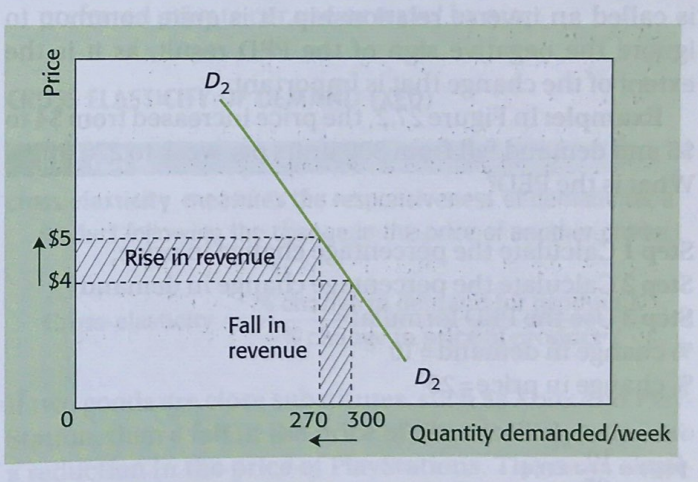

Figure 27.2 Demand curve for product A

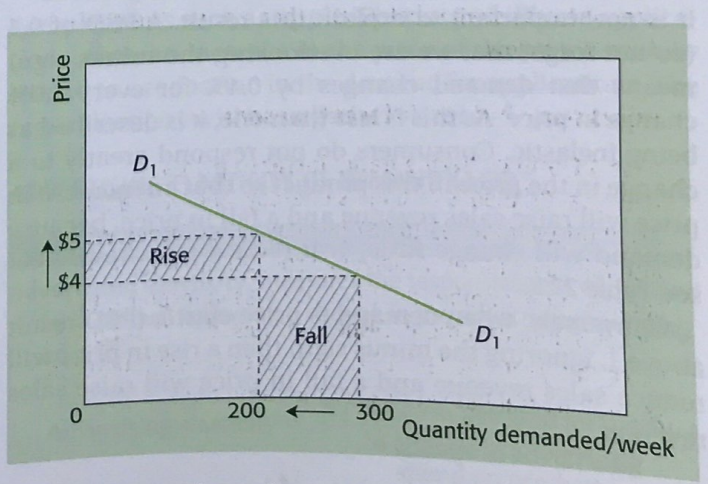

Figure 27.3 Demand curve for product B

This relationship between price changes and the size of the resulting change in demand is known as price elasticity of demand.

KEY TERM

price elasticity of demand measures the responsiveness of demand following a change in price

This concept can be demonstrated on demand curves as shown above – product A's demand is less elastic or less responsive to a price change than product B. This idea can also be measured mathematically. The formula for price elasticity of demand (PED) is:

$$\frac{\text{percentage change in quantity demanded}}{\text{percentage change in price}}$$

The value of PED is normally negative because a fall in price (–ve) usually results in a rise in demand (+ve). This is called an inverse relationship. It is quite common to ignore the negative sign of the PED result, as it is the extent of the change that is important.

Example: In Figure 27.2, the price increased from $4 to $5 and demand fell from 300 units per week to 270 units. What is the PED?

Step 1 Calculate the percentage change in price.
Step 2 Calculate the percentage change in demand.
Step 3 Use the PED formula:
% change in demand = 10
% change in price = 25

$$\text{PED} = \frac{10}{25} = 0.4$$

It is now important to explain this result. A PED of 0.4 (do not forget that we are overlooking the minus sign) means that demand changes by 0.4% for every 1.0% change in price. As this is less than one, it is described as being inelastic. Consumers do not respond greatly to a change in the price in this product so that an increase in price will raise sales revenue and a fall in price, because demand will change little, will reduce sales revenue – see Table 27.2.

Conversely, when demand is price elastic (PED result above 1, ignoring the minus sign) then a rise in price will reduce sales revenue and a fall in price will raise sales revenue.

ACTIVITY 27.4

6 marks, 10 minutes

1 Using the information in Figure 27.3, calculate the PED following the rise in price of product B. [2]

2 Comment on the likely impact on sales revenue as a result of this price increase. [4]

Value of PED	Classification	Explanation and impact on sales revenue
Between 0 and 1	Inelastic demand	The percentage change in demand is less than the percentage change in price. If a firm faces this elasticity of demand, it can raise the price, not lose much demand and increase sales revenue. However, this cannot keep happening. As the price continues to rise, demand will become more elastic.
Unitary	Unit elasticity	The percentage change in demand is equal and opposite to the percentage change in price, so any price change will lead to an equal change in demand. Total sales revenue will remain constant.
Between 1 and infinity (∞)	Elastic demand	The percentage change in demand is greater than the percentage change in price. If a firm faces this elasticity of demand, then it can lower the price, pick up a lot more demand and increase sales revenue.

Table 27.2 *Price elasticity of demand and its effects on sales revenue (minus sign not shown)*

Factors that determine price elasticity of demand

- How necessary the product is.
- The number of similar competing products or brands.
- The level of consumer loyalty to the brand.
- The price of the product as a proportion of consumers' incomes.

ACTIVITY 27.5

Read the case study below and then answer the questions that follow.

The *Daily Times*

The *Daily Times* newspaper editor is concerned about falling circulation (sales). He believes that newspaper readers are mainly influenced by price when making their decisions over which papers to buy. He decided to cut the price of the paper from $1.50 to $1.20. In the following week, circulation increased by 150 000 copies to 1 650 000. After four weeks, however, sales had fallen back to their original level. The owner was confused about the possible reasons for this and wondered whether he should cut the price again to $1.

25 marks, 45 minutes

1 From the information above, calculate the PED in the first week after the price reduction. [4]

2 Comment on your result in terms of the apparent price elasticity of this product. [2]

3 Calculate the newspaper's daily sales revenue before and after the price cut. Comment on your results. [5]

4 Explain **two** possible reasons why demand fell back to the original level some weeks after the price reduction. [6]

5 Discuss the action the newspaper's owner should now take to increase sales. [8]

ACTIVITY 27.6

A firm sells three products. The price elasticity of demand is estimated to be:
A –3, B –0.5, C –1

12 marks, 21 minutes

1 Explain what these results mean. [6]

2 Explain what the effect on (a) sales and (b) sales revenue will be for each product if all prices rise by 10%. [6]

INCOME ELASTICITY OF DEMAND (YED)

KEY TERM

income elasticity measures the responsiveness of demand for a product following a change in consumers' incomes

Income elasticity of demand is calculated by the following formula:

$$\text{Income elasticity} = \frac{\%\text{ change in demand}}{\%\text{ change in income}}$$

- Normal products such as DVDs and airline travel will have positive income elasticity of demand. It is positive because if incomes rise, the demand for the product is likely to increase.
- Necessity goods are likely to have low income elasticity of demand – a 10% increase in consumers' incomes is unlikely to have much impact on the demand for salt.
- Luxury goods are likely to have a high income elasticity – the demand for Ferraris tends to increase at a faster rate than consumers' incomes during an economic boom.
- Inferior goods have negative income elasticity. As they have a preferred competing product, the demand for inferior goods falls as income rises. The demand for bus and rail travel has fallen greatly in the USA as consumers, with higher incomes to spend, have preferred private car use or travel by air.

CROSS ELASTICITY OF DEMAND (XED)

KEY TERM

cross elasticity measures the responsiveness of demand for a product following the change in the price of another product

$$\text{Cross-elasticity} = \frac{\%\text{ change in demand for product X}}{\%\text{ change in price of product Y}}$$

If two goods are close substitutes, such as Xbox and PlayStation, then a fall in the price of Xbox is likely to lead to a reduction in the price of PlayStations. The cross elasticity is positive.

If two goods are often bought together, as they are complements such as Apple iPhones and iPhone applications, then an increase in the price of the phone is likely to lead to a reduction in the demand for applications. The cross elasticity will be negative.

ADVERTISING ELASTICITY OF DEMAND (AED)

KEY TERM

advertising elasticity measures the responsiveness of demand for a product following a change in the advertising spending on it

$$\text{Advertising elasticity} = \frac{\%\text{ change in demand for product}}{\%\text{ change in advertising spend on product}}$$

For many products, especially consumer goods, advertising elasticity will be high – demand is responsive to more advertising. However, this is not always the case if:

- rival firms are spending even more on advertising
- the campaign is expensive but poorly received by consumers
- other elements of the marketing mix are not working well – perhaps they are not integrated with the promotional campaign and consumers are getting mixed messages about the product
- industrial product sales are less responsive to advertising – product quality, after-sales service and delivery dates may be more significant.

Elasticity and the product life cycle

Table 27.3 explains the relationships between elasticity and the product life cycle.

EXAM TIP

When discussing the importance of these measures of elasticity it is important to make clear that nearly all elasticity results are estimates and depend very much on all other factors affecting demand remaining unchanged.

Stage of the product life cycle	Application of elasticity
Launch and growth	• PED likely to be low – consumers may be prepared to pay high prices. • AED likely to be high – informative advertising could lead to considerable consumer interest. • XED depends on number and closeness of substitutes – a unique new design will have very low XED as price changes of other goods will have little impact on demand for this unique product. • YED depends on whether the product is launched at a prestige niche market (high YED) or low-image mass market (low YED).
Saturation/ maturity	• PED might be increasing as new rivals come into the market and appear more attractive – business may have to lower prices. • AED likely to be low – most consumers will now be aware of the product. • XED – more competition and if prices of rival products are lowered, XED likely to be high and positive. • YED depends on nature of product.
Decline	• PED – prices may be lowered at this stage but PED might be low if consumers would really prefer a newer product. Time for an extension strategy? • AED – low unless advertising is used as part of a product re-launch extension strategy. • XED – high and positive as rivals' substitute products increase in number. • YED – the product may now become an 'inferior' good and YED could be negative.

Table 27.3 *Applying elasticity to a product life cycle*

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ACTIVITY 27.7

'Levi claims Tesco cut-price jeans bad for brand image'

The maker of Levi's jeans has asked the European Court of Justice to prevent Tesco and Costco selling their jeans at knock-down prices. The manufacturer fears that its brand image and reputation will be damaged if its jeans are sold in supermarkets. Judges are being asked to decide if Tesco has infringed Levi's trademark rights by importing and selling branded jeans from outside Europe without consent.

The jeans come from the United States, Canada and Mexico. Levi stopped supplying Mexican wholesalers when it discovered that its jeans were being sold for export. Several years ago, Levi started legal action against Tesco. The retailer argued that it was entitled to buy jeans from abroad and sell them freely. Alan Christie, Levi's vice-president of public affairs, said that Tesco had undermined Levi's ability to control its own brand. He said: 'Tesco is trying to use our investment in our brand to build its own reputation, and it is doing so illegitimately. For a company that makes as much money as Tesco does, that is simply unacceptable.' Christie denied that Tesco was providing

a service to consumers by making branded products available at a cheaper price. 'We have retail criteria that describe the conditions under which we want our products to be sold. Tesco does not meet those criteria because it does not specialise in retailing clothing,' he said. 'People want to experience a premium brand like Levi's in the right environment.'

Source: Daily Telegraph, *17 January 2001 (adapted)*

12 marks, 21 minutes

Do you think Levi's is right to try to limit the sale of its clothing products at 'knock-down' prices? Justify your answer. [12]

THEORY OF KNOWLEDGE

Major supermarkets like Tesco and Asda say that low prices are good for consumers and therefore good for society. Others argue that low prices are bad for producers who supply businesses, lead to over-consumption and have a negative effect on the environment.

In groups, discuss to what extent supermarkets selling goods at very low prices is good for society.

OVER TO YOU

REVISION CHECKLIST

1 State **two** reasons why the pricing decision is such an important one.
2 Why should pricing decisions not be taken in isolation to other marketing mix decisions?
3 Define full-cost/absorption pricing.
4 Differentiate between skimming pricing strategies and penetration pricing strategies.
(H) 5 State the formula for price elasticity of demand.
(H) 6 A manager is reviewing the pricing levels of two products and, from past data, the PED for product X is –0.5 and for product Y –1.6. In which case would you advise the manager to consider increasing price and in which case would a price reduction seem to be more appropriate? Explain your answer with diagrams or calculations.
(H) 7 Explain one situation in which contribution-cost pricing would seem to be more appropriate than full-cost pricing.
(H) 8 What do you understand by 'psychological pricing'?
(H) 9 Under what circumstances would it seem to be relevant to use a loss leader strategy?
(H) 10 How could variations in the price of a product be used to extend its life cycle?
(H) 11 Using your knowledge of price elasticity of demand, explain why many businesses use a policy of price discrimination.
(H) 12 Would consumers benefit from a policy of predatory pricing? Explain your answer.