Pricing Strategies

Factors Influencing the Pricing

There are many factors that influence the pricing of the products like consumers' perceptions, product life cycle stages, quality, branding etc. they can be grouped together into external and internal factors as shown in the following table. We will discuss in detail some of the important factors that affect price of any product.

Internal factors

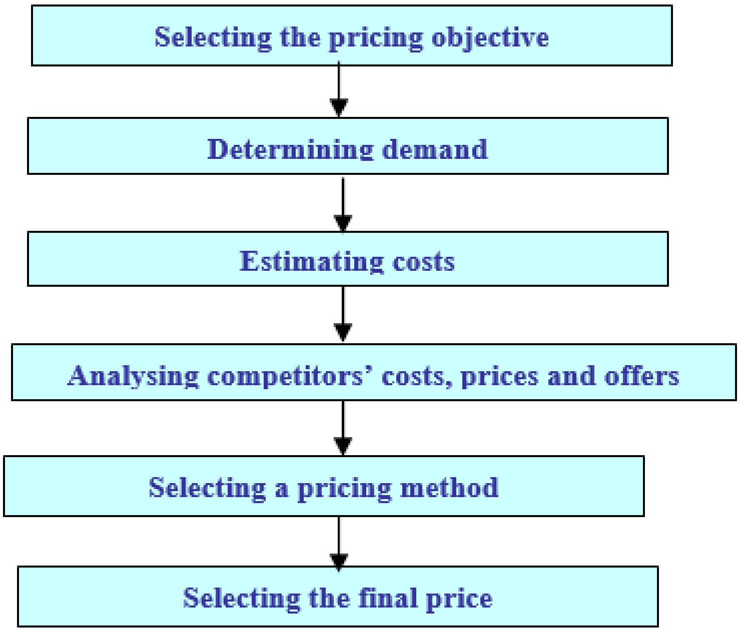
- Business and marketing objectives
- The image that business wants to build in the market (branding)
- The nature and characteristics of the product. (Quality)
- Cost of production and marketing
- Price elasticity of demand
- Product line and its composition
- The stage of product in the life cycle
- The extent to which the product is distinct in the market
- Other elements of marketing mix

External Factors

- The demand in the market
- The customers and their bargaining power
- Buyer behaviour in respect of the product
- The competition and competitor's pricing policy
- The suppliers and their bargaining power
- Government controls
- Legal norms

Setting the Price

Having stated various pricing positioning strategies, the major issue for a company is to consider many factors while setting its pricing policy. The 6-step procedure for setting pricing policy is as follows:



Step 1 - Selecting the pricing objective:

The company first decides where it wants to position its market offering. The clearer a firm's objectives, the least it is to set price. A company can have any of following 5 major pricing objectives

Survival: It is applicable if the company is facing problem of overcapacity, intense competition or changing customer wants. Profits are less important than survival. As long as prices cover variable costs and some fixed costs, the company survives in the business. This is short-run objective. In long run, the company must learn how to add value or face extinction.

Profitability: The company may set a price to maximize current profits. The companies estimate the demand and costs associated with alternative prices and choose the price that produces maximum current profit, cash flow or rate of return on investment. This strategy assumes that the company has knowledge of demand and cost function which in reality very hard to estimate. This strategy emphasizes current financial performance and sacrifice long-run performance by ignoring the effects of other marketing-mix variables, competitors' reactions and legal restraints on price.

Return on investment: The objective of pricing products of an organization can be to attain a specified return on their investments. Usually, data used to arrive at the returns on investment is not available (\t the time when prices are set. Therefore, organization adopts a trial and error method wherein the company arrives at the best pricing alternative to leverage the maximum return on investment.

Status quo: Organizations can maintain status quo as their pricing objective. Finns adopt a status quo approach to pricing to maintain a certain level of stability in its prices or to maintain the market share. Maintaining status quo helps the company to reduce potential threats in the form of competition by stabilizing the demand for the company's products.

Product quality: Firms try to set the prices of their products to reflect the product's quality leadership in the market. Finns set high prices for their products so as to cover the high R&D costs incurred in improving the quality of the product. It is also important for marketers to communicate the product quality to the intended audience, as customers will be inclined to pay a high price only when they are assured of the product quality. When the company increases the price of the product, it is also important to improve the relative quality of the product.

Market share: Some companies want to maximize their market share. They believe that a higher sales volume will lead to lower unit costs and higher long run profit. This strategy of setting a low price works well when:

- The market is highly price sensitive for which low price stimulates market growth
- The production and distribution costs fall with accumulated production experience
- The low price discourages actual and potential competition

Nirma uses this kind of *market penetration pricing*

Skimming: Many companies like Intel and Sony favor setting high prices to “skim” the market. This strategy is applicable in following conditions:

- A sufficient number of buyers have a high current demand
- The unit costs of producing a small volume are not so high that they cancel the advantage of charging what the traffic will bear
- The high initial price does not attract more competitors to the market
- The high price communicates the image of a superior product
- The company thus can enjoy product-quality leadership

Except this, non-profit and public organizations may adopt other pricing objectives. A university aims for partial cost recovery, knowing that it must rely on private gifts and public grants to cover the remaining costs. A non-profit hospital may aim for full cost recovery in its pricing. A social service agency may set a social price geared to the varying incomes of clients

Step 2 - Determining demand:

The relation between alternative prices and the resulting current demand is captured in a demand curve.

Price sensitivity: There are 9 factors that affect the price sensitivity:

- ***Unique value effect*:** Buyers are less price sensitive when the product is more distinctive
- ***Substitute-awareness effect*:** Buyers are less price sensitive when they are less aware of substitutes
- ***Difficult-comparison effect*:** Buyers are less price sensitive when they cannot easily compare the quality of substitutes

- ***Total expenditure effect*:** Buyers are less price sensitive the lower the expenditure is as a part of their local income
- ***End-benefit effect*:** Buyers are less price sensitive the smaller the expenditure is to the total cost of the end product
- ***Shared-cost effect*:** Buyers are less price sensitive when part of the cost is borne by another party
- ***Sunk-investment effect*:** Buyers are less price-sensitive when the product is used in conjunction with assets previously bought.
- ***Price-quality effect*:** Buyers are less price sensitive when the product is assumed to have more quality, prestige or exclusiveness
- ***Inventory effect*:** Buyers are less price sensitive when they cannot store the product

<u>Estimating demand curves</u>: The companies use different methods to measure the demand curves:

- First method involves statistically analysing past prices, quantities sold and other factor to estimate their relationship. The data can be longitudinal over time or cross-sectional for different locations at the same time. Building the appropriate model and fitting the data with the proper statistical techniques requires high skill.
- Second method is to conduct price experiments. One example is to vary the prices of several products sold in a discount store and observed the results. An alternative approach is to charge different prices in similar territories to see how sales are affected.
- The third approach calls for asking buyers to state how many units they would buy at different proposed prices.

<u>Price elasticity of demand</u>: The Price elasticity of demand (PED) is the responsiveness of changes in the quantity demanded to changes in the price. It is calculated using the following formula

% Change in Demand / % Change in Price

The calculation of the PED will produce a value. This value will indicate the characteristics of the PED. For instance;

- Zero (perfectly inelastic): Quantity demanded does not change at all as price changes.
- Between zero and one (inelastic) - quantity demanded changes by a smaller percentage than price
- One (unitary elasticity): Quantity demanded changes by exactly the same percentage as the change in price
- Between one and infinity (elastic): Quantity demanded changes by a larger percentage than does the change in price
- Infinity (perfectly elastic): Buyers are prepared to purchase all they can obtain at a given price, but none at a higher price.

Step 3 - Estimating costs:

Demand sets a ceiling on the price the company can charge for its product. Costs set the floor. The company wants to charge a price that covers its cost of producing, distributing and selling the product, including a fair return for its effort and risk.

A company's costs can be of two forms such as

- Fixed costs or overhead: The costs that do not vary with production or sales revenue. For example, the land cost remains same whatever amount you produce
- Variable costs: These costs vary directly with the level of production. For example, the cost of raw material varies with the amount you produce.

Total costs can be calculated as the sum of fixed and variable cost for any given level of production whereas the average cost is the cost per unit at given level of production. Average cost falls with accumulated production experience. It is called experience curve or learning curve. The risks of experience-curve pricing are:

- Cheap image
- Wrong assumption of weak competitors who are unwilling to fight

- Lower cost technology adoption by the competitors

Step 4 - Analysing competitors' costs, prices and offers:

Within the range of possible prices determined by market demand and company costs, the firm must take the competitors' costs, prices and possible price reactions into account. There could be 3 possibilities:

- If the firm offers inferior product than its competitors, then the firm should offer a price less than competitors
- If the firm offers similar product as that of its competitors, they have to price same or close to the competitors' prices
- If the firm's offer is superior, the firm can charge more than the competitor.

For example, Akai has introduced its low priced CTVs whereas Sony stuck to its high value premium offer strategies.

Step 5 - Selecting a pricing method:

While selecting the final price, the companies must decide 3 factors commonly known as ***3 C***'s

- Cost function: It sets a floor price
- Competitors' price: It provides orienting point
- Customers' demand schedule: It establishes the ceiling price

There are several methods of pricing. Each of them is appropriate for achieving a particular pricing objective or a combination of pricing objectives. Following are the various methods of pricing.

1) Cost Based (or Cost-plus or Cost-driven) Pricing

a) Mark-up pricing/cost plus pricing

b) Absorption cost pricing/full cost pricing

c) Target pricing/rate of return pricing

d) Marginal cost pricing

2) Demand or Market Based (or Market-driven) Pricing

a) "What the traffic can bear" pricing

b) Skimming pricing

c) Penetration pricing

3) Competition Oriented Pricing

a) Premium pricing

b) Discount pricing

c) Parity pricing/going rate pricing

4) Product line oriented pricing

5) Tender or sealed bid pricing

6) Affordability-based pricing

7) Differentiated pricing

8) Perceived-value pricing

9) Value pricing

10) Sealed-bid pricing

11) Prestige pricing

12) Psychological pricing

13) Value based pricing

14) Price discrimination

15) Loss-leader pricing

1) Cost based pricing: In this method, pricing a product is based on all the costs involved in various processes like production, promotion, distribution and overheads. The various cost based pricing methods are:

a) <u>Mark-up pricing/cost plus pricing:</u> Here the prices of products are fixed by adding a margin to the cost price. The mark up or margin differs from product to product depending upon the unit cost of the product and other factors. Higher the unit cost higher the mark up and vice versa. Faster the turn round of the product, the smaller the mark up and vice versa.

The assumption under this method is that demand cannot be known accurately, but costs can be known. A reasonable mark-up is added to the costs. The objective is to maximize profits in the short run without sacrificing sales due to excessive prices. This method is preferred by those firms who do not have any manufacturing of their own.

The method is to add a standard mark-up to the product's cost.

The mark-up price can be found as:

(Variable cost per unit + fixed cost/unit sales) / (1-desired return on sales)

For example, let a manufacturer has following costs and sales expectations:

Variable cost per unit = Rs. 30

Fixed cost = Rs. 7,50,000

Expected sales in units = 50,000

Desired return on sales = 10%

So, unit cost = variable cost per unit + fixed cost/unit sales

= 30 + 7,50,000/50,000 = 30+15 = 45/-

Hence, the mark-up price=unit cost/(1-desired return on sales) = 45/(1-0.1) = 45/0.9 = 50/-

Mark-ups are generally higher on seasonal items (to cover the risk of not selling in non-seasonal time), specialty items, slower moving items, items with higher storage and handling costs and demand-inelastic items (such as prescription drugs)

Mark-up pricing has following advantages:

- Determination of cost is much easier

- When all the companies in an industry use this method, price tends to be similar and price competition is minimized unlike pricing method based on demand
- Buyers may feel this method is fairer to them as this method does not take advantage during the time of high demand.

This method has some disadvantages:

- Ignoring demand level, perceived value and competition do not lead to determination to actual level of pricing
- High-mark-up strategy may turn out to be fatal for the company if the competitor offers low price.

b) <u>Absorption cost pricing/Full cost pricing</u>: This method calculates the variable and fixed costs involved in producing, selling and administering the product. This is the total cost of the product to which profit margin is added which becomes the price of the product. This is similar to mark-up pricing. This is mostly followed in manufacturing organizations.

Firms preferring great amount of safety in their pricing method follow this method of pricing because as long as the market can absorb the production at the determined price, the firm is assured of its profits without any risks.

The most positive aspect of this pricing is that as long as the market can absorb the production at the determined the firm is assured about its profits with no risks at all. That is why this pricing method is followed by the firms which prefer safety over other things. On the negative side, this pricing method does not consider the demand factors which also might affect prices. This method also relies on the normal or assumed level of production and sales and this method will fail if there is any change in the assumed level of production. This method does not consider the change in cost of input that might occur during the phase of production and sales. From the time the absorption cost was work out to the actual time of production there might be changes in the costs of the organization. Thus this method is not a dynamic method of pricing.

c) <u>Target/Rate of return pricing</u>: This method is similar to that of absorption cost pricing but is different in the sense that mark-up is arbitrary in case of absorption cost pricing but in case of rate of return pricing it is decided based on return on investment criteria of the firm. In other words rate of return on the funds employed is a function of mark-up.

In this method, the company determines the price that would yield its target Return On Investment (ROI).

Target-return price is obtained as:

((Variable cost per unit + fixed cost/unit sales) + desired return* invested capital)/ total unit sales

For example, let a manufacturer has following costs and sales expectations:

Variable cost per unit = Rs. 30

Fixed cost = Rs. 7,50,000

Expected sales in units = 50,000

Invested capital = Rs. 10,00,000

Desired ROI = 10%

Unit cost = Rs. 45 (as found out in previous example)

Then, Target-return price = unit cost + (desired return* invested capital)/unit sales

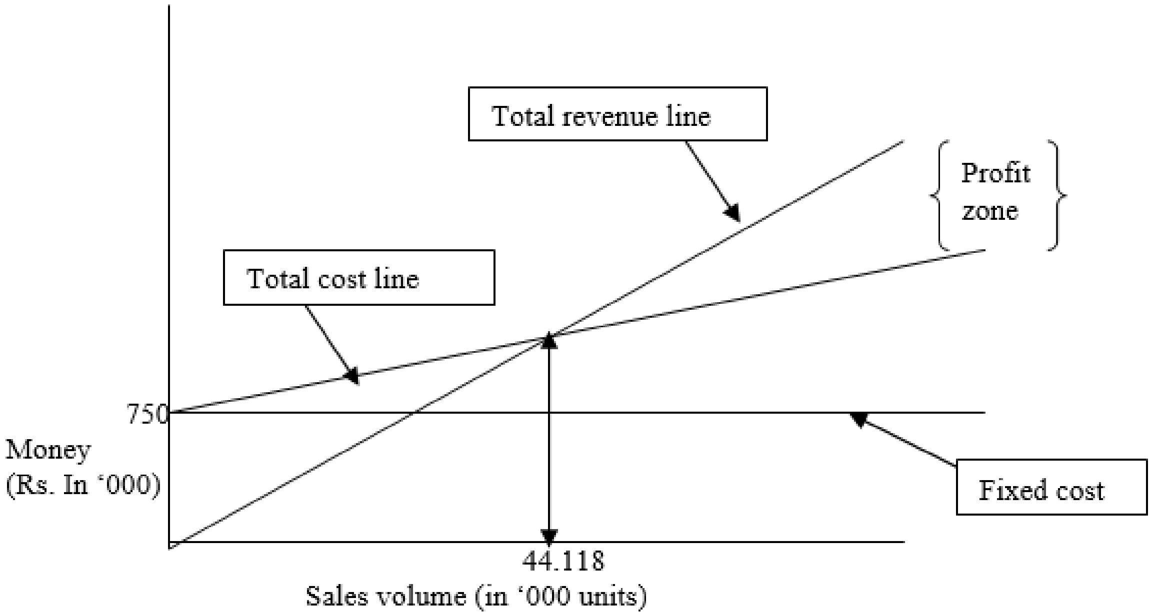
= 45 + (0.1*10,00,000)/50,000

= 45 + 1,00,000/50,000 = 45 + 2 = 47/-

But what happens if the company can achieve the sales of 50,000 units as expected. The manufacturer can prepare a break-even chart to learn what would happen at other sales levels. In this case, fixed costs are Rs. 7,50,000 regardless of sales volume. Variable costs rise with the volume. Thus total cost curve is drawn as sum of fixed cost and variable cost. The total revenue curve starts at zero and rises with each unit of sale. The break-even volume is obtained as fixed cost/ (price-variable cost per unit).

In this case, break-even volume = 7,50,000/(47-30) = 7,50,000/17 = 44,118 units

Graphical illustration of beak-even analysis



This method is an improvement over the absorption cost method as it uses a rational basis for arriving at the mark up. The rate of return on the funds employed is a function of the mark up as well the turnaround of capital employed. This tells a firm that there are two routes of profits, improvement in the capital turnover and increase in the mark up. The main demerit of this method of pricing is that the rate of return is calculated on the level of production and sales assumed. Any change in these figures will change the rate of return also.

d) Marginal cost pricing: This is a method of pricing where direct variable costs are realized fully and a portion of the fixed costs is also realized. This method aims at maximizing the contribution towards fixed cost. The difference between absorption cost pricing and marginal cost pricing is that in case of absorption cost pricing full variable and fixed costs are recovered. But in marginal cost pricing, a part of fixed costs may remain unrecovered depending upon the market situation. It also gives the flexibility to recover a larger share of the fixed cost from certain customers and a smaller share from others.

In spite of being a cost based method it takes into consideration the demand factor also. So this method is more useful under competitive market conditions. On the other hand this method makes certain assumptions regarding costs and revenue behaviour that might turn out to be incorrect for some cases. This method ignores the third kind of cost called mixed cost apart from fixed and variable costs. This method can be employed only in short run and under specific circumstances.

2) Demand/Market based pricing: The basic feature of all these demand-based methods is that profits can be expected independent of the costs involved, but are dependent on the demand. This pricing method differs from Cost-driven pricing in that it starts by asking at what price the market will be prepared to pay for the product and works back to the level of profit and costs, which that price will afford to the organization.

a) "What the traffic can bear" pricing: Under this method the seller charges maximum price, which the customers are willing to pay for the product under the given circumstances. This method brings high profits in the short-run but is not safe in the long run as chances of errors in judgment are very high and involves trial and error method. This method is used more by retail traders and wherever monopoly or oligopoly conditions exist and demand is quite inelastic.

b) Skimming Pricing: This method aims at high price in the early stage of marketing the product. As the word skimming indicates, this method literally skims the market in the first instance through high price and subsequently settles down for a lower price. This method profitably taps those segments of the market, which do not bother much about the price. This method is more useful in pricing new products that have a luxury or specialty element. As the product has novelty and as if is aimed at the affluent sections, the quantity that can be sold is not affected by the price level. It helps the firm to feel the market for the product and then make appropriate decisions on pricing.

Once the innovation has taken off, interest might begin to wane and in order to reach a wider spectrum of potential purchasers, prices are lowered at the first skim, which brings in more innovator categories or different social groups. This process proceeds continuously until the final skim. Demand thereafter tends to reflect replacement demand.

c) Penetration Pricing: This method seeks to achieve greater market penetration through relatively low prices. It is the opposite of skimming pricing. This method is useful in pricing new product that is not a luxury item and there is no price insensitive segment backing it, but is capable of bringing in large volume of sales. This method brings large size sales at a reasonable price before competitors enter the market with a similar product. Such products are highly price sensitive even in the introductory stage and this method helps the firm in obtaining a good coverage of the market and keep competition out for quite some time. For these products large sales may be necessary for break-even and penetration method helps in getting large sales.

A low initial penetration price attracts a mass market at the outset. Demand takes off exponentially during introduction and pattern shown by the typical product life cycle concept hardly applies. The notion is particularly appropriate for products with strong demand elasticity where unit cost reductions can be achieved through mass production at the beginning. An abundant sales volume must be assured from the outset to keep production levels high, in order to continue to realize these economies of scale. Marketing's task is to ensure that interest is maintained during the life of the product and the concept remains 'fresh' in the eyes of consumers.

3) Competition Oriented Pricing: The methods under this category rest on the principle of competitive parity in the matter of pricing. Three policy alternatives are available to the firm under this pricing method.

a) Premium Pricing: It means pricing the product above the level adopted by competitors.

b) Discount Pricing: It means pricing the product below the level adopted by competitors.

c) Parity Pricing/going rate pricing: It is pricing the products equal to that of competitors. Where supply is more than adequate to meet demand and the market remains competitive in a stable manner and where the channel and consumers are well aware of their choices, parity pricing may be the answer. Similarly when a market leader has established a market price with the intention of stabilizing the price the smaller firms in the industry may have to go for parity pricing.

4) Product Line Pricing: When the firm manufactures and markets a large variety of products that can be grouped into a few product lines, this method of pricing can be adopted. As the products in a given product line are related to each other, sales of one influence the sales of others and they have inter related manufacturing and distribution costs. In such situations the firm aims at fixing the price of each product in such a manner that the entire product line is priced optimally resulting in optimal sales of all the products in the line put together and optimum total profits from the line, instead of fixing optimal price for each product independently. The total cost of the entire line and the total profit expected from the entire line is taken into consideration for pricing. A firm may also fix tentative prices for various products in the line adjusted later based on competitors' prices for these products and the demand reactions at different prices. In this method there is the problem of joint costs and joint revenues and price of a product cannot be altered without considering the line effect.

5) Tender Pricing: It is a special type of pricing which is mostly applicable to industrial products and products purchased by industrial customers. Such customers usually go by competitive bidding through sealed tenders or by quotations. It is a competitive oriented method of pricing. Customers seek the best price consistent with the minimum quality specifications. In this method, the firm bases its price on expectation of how competitors will price rather than on a rigid relation to the firm's costs or demand. The firm's objective will be to get the best possible price under the circumstances and to bag the order. The problem faced here is to find a price that is consistent with costs, profits and company objectives and also low enough to get the bid. Another problem is that of avoiding regrets of having missed a better price and profits due to over anxiety in securing the order and wrong estimation of the competitors bid.

6) Affordability-based pricing: This method is relevant in respect of essential commodities, which meet the basic needs of all sections of people. The idea here is to set prices in such a way that all sections of the population are in a position to try and consume the products to the required extent. The price is set independent of the costs involved, often an element of state subsidy is involved and the items are distributed by the public distribution system. It is also referred as social welfare pricing.

7) Differentiated Pricing: Some firms charge different prices for the same product in different zones/areas of the market. Sometimes, the differentiation in pricing is made on the basis of customer class rather than marketing territory, which is more common for services; for example, railways and airlines offer concession for senior citizens (age above 60). Sometimes, the differentiation is made on the basis of volume, when the products are offered at variable prices with bulk or regular purchases; the examples are economy-sized packs of detergents.

8) Perceived-value pricing: Many companies base price on the customer's perceived value. They use the other marketing-mix elements especially promotion tools such as advertising and publicity to build up perceived value in buyers' minds. The best examples are luxury goods such as Ferrari sports cars or Rolex diamond studded watches that charge exorbitant prices cashing their high prestige values. The key element of this pricing is to determine the market's perception of the offer's value accurately. Market research is necessary to establish the market's perception of value as a guide to effective pricing.

9) Value pricing: In this method, companies charge a fairly low price for a high-quality offering so that price represents a high value to the consumers. An important type of value pricing is Every Day Low Pricing (EDLP) that takes place at the retail level. A retailer who holds to an EDLP pricing policy charges a constant, everyday low price with no temporary price discounts. These constant prices eliminate week-to-week price uncertainty and can be contrasted to the "high-low pricing of promotion oriented competitors. In high-low pricing, the retailer charges higher prices on an everyday basis but then runs frequent promotions in which prices are temporarily lowered below the EDLP level. Retailers adopt EDLP for following reasons:

- Constant sales and promotions are costly and have eroded consumer confidence in the credibility of everyday shelf prices.
- Consumers have less time and patience for such time-honored traditions as watching for supermarket specials and clipping coupons.

10) Sealed-bid pricing: Competitive oriented pricing is common where the firms submit sealed bids for jobs. The firm bases its price on expectations of how competitors will price rather than on a rigid relation to the firm's costs or demand. The firm wants to win the contract, and winning normally requires submitting a lower price bid. At the same time, the firm cannot set its price below cost.

11) Prestige pricing: As a purchasing motivation, 'prestige' is rarely openly admitted. Many buyers do not realize that this might be their prime motivation for wanting to possess a particular item. At best, they might see the motive, as the desire to possess something that is exclusive and such exclusivity is often associated with a high price. This is associated with what we term 'psychological pricing'.

12) Psychological pricing: It is now acknowledged that there are psychological price brackets for certain categories of products (ladies clothes are a particularly good illustration) in which price increases or reductions have little effect. When prices are reduced or raised to the next psychological price band, then demand will increase or decrease in a step-like manner. An obvious example of this is the high pricing to suggest product quality or exclusivity. Closely linked to this is the notion of odd/ even pricing' where a price of Rs. 9,990 means that there is a little change from Rs. 10,000, but psychologically it is a 4-digit figure. Anything 5-digit i.e. over Rs. 10,000 is in the next psychological band, which consumers perceive as being much more expensive than it actually is. 'Price lining' is also linked to psychological pricing and here retailers like Bata shoes sell all of their products in a limited number of price bands of Rs. 49.95, Rs. 89.95 and Rs. 129.95. The psychological pricing also exists in bulk-buy prices used mainly by discount stores like Big Bazaar that offer apparently exciting discounts that may not exist in practice thus prompting huge (and often unnecessary) purchases.

13) Value based pricing: This is where a producer bases prices on the perceived value that the customer has of the product or service. It uses purchasers' price perceptions rather than costs as the principal measure. The marketing mix is manipulated so that non-price variables are accentuated and price perception is implanted in the minds of buyers. Price is then set to match the perceived value of the product or service. Cost-based price is accounting constrained using costs and the ultimate product as the basis for the pricing decision. Value based pricing is where the company establishes a target price, based on customer perceptions of the value that the product holds for them. If this turns out to be too high, the company must then reduce price and settle for a lower profit margin.

14) Price discrimination: Different prices are sometimes charged to certain categories of customers and this is termed 'price discrimination'. Discount structures operate in many industrial companies and 'trade discounts' apply for bona fide members of certain skilled professions. Volume discounts are also a feature in such circumstances and discounts are frequently offered as a promotional tool to encourage larger individual orders. Discounts are often used as an inducement to pay by a stipulated time or to bolster sales of slow moving lines. Quite often price discrimination is applied to attract certain market segments that the company wishes to target. A current example is cheap initial loan rates, for a short period, offered by banks and building societies to attract first time homebuyers in the expectation that they will remain loyal to the lender.

15) Loss-leader pricing: This is widely used in retailing to encourage traffic in the store, when a few well-known brands are marked down to allure consumers.

In case of B2B markets, some tactics differ from consumer markets, as the customers are the professional buyers or purchasers form different organizations. The prices for these markets will be quoted differently considering ex-works (this price excludes transport and is suitable for customers who will collect on their own), or cost and freight (price including delivery) or product price and delivery costs shown separately. Some companies purchase on the basis of tenders, where the competitors make bids against each other, not possibly knowing what their rivals' prices are likely to be. In industrial marketing, the practice of haggling (bargaining) for discounts is very much common especially in case of volume or regular purchases or to the customers who pay either in advance or promptly upon invoice. Sometimes the quoted price list may be the starting point from which both the buyers and sellers start negotiating for the best deal for their own organizations.

Step 6 - Selecting the final price:

Pricing methods narrow the range from which the company must select its final price. In selecting that price, the company must consider some additional factors that are described below:

Psychological pricing: Many consumers use price as an indicator of quality. Price and quality perceptions of products interact. Higher-priced products such as cars are perceived to possess high quality and vice versa. When alternative information about true quality is available, price becomes a less significant indicator of quality. When this information is not available, price acts as a signal of quality. If you see the price of a Mercedes Benz car costs Rs. 5 lakhs only, you will not consider it as a highly prestigious car. When looking at a product, the buyers carry in their minds a reference price formed by noticing current prices, past prices or the buying context. Sellers often manipulate these reference prices. For example, a seller can situate its product among expensive products to imply that it belongs in the same class. Hence, when Hyundai launched its SUV Terracan, its price was positioned in the segment of cars dominated by Chevrolet Forrester, Ford Endeavour and Mitsubishi Pajero. Department store will display women's apparel in separate departments differentiated by price; dresses found in the more expensive department are assumed to be of better quality. If highly priced designer clothes are placed among the mass apparel, you either will not notice it or will not be motivated to buy. Reference-price thinking is also created by stating a high manufacturer's suggested price or by indicating that the product was priced much higher originally or by pointing to a competitor's high price.

- Company's pricing policies: The price must be consistent with the company pricing policies. Many companies set up a pricing department to develop policies and establish or approve decisions. The aim is to ensure that the salespeople quote prices that are reasonable to customers and profitable to the company.
- Impact of price on other parties: Management must also consider the reactions of other parties to the contemplated price. How will the distributors and dealers feel about it? Will the sales force be willing to sell at that price? How will the competitors react? Will suppliers raise their prices when they see the company's prices? Will the government intervene and prevent this price being charged?

- The influence of other marketing-mix elements: The final price must take into account the brand's quality and advertising relative to competition. Farris and Reibstein examined the relationships among relative price, quality and advertising and found the following:
  - Brands with average relative quality but high relative advertising budgets were able to charge premium prices. Consumers apparently were willing to pay higher prices for known products than for unknown products.
  - Brands with high relative quality and high relative advertising obtained highest prices. Conversely, brands with low quality and low advertising charged the low prices.
  - The positive relationship between high prices and high advertising held most strongly in the later stages of PLC for market leaders.