

What Goes into Fact-Based Pricing Decisions?



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U.S. companies, including those in the home improvement industry, continue to be challenged by increased globalization, new technology and industry-wide consolidation. In this highly competitive arena, a product's retail price plays an important role.

The purpose of this article is to describe several types of retail pricing information currently available in the home improvement industry and discuss how it can assist in your future pricing decisions.

It is widely held that price is one of the most powerful influences on a brand's sales and profitability. Given this importance in the overall marketing mix (i.e. price, product, promotion and place), a company's senior management should know if their prices are in sync with the marketplace and have a reporting mechanism to periodically check to see if that status have changed.

A product's price should be part of an overall pricing strategy, e.g. cost-plus, penetration, product line, etc. Regardless of the particular strategy a company has chosen and the premises on which it was founded, it is important for the company to have up-to-date pricing information on both their products and competitor's products.

When companies have a firm understanding of their current prices in the

marketplace, their comparison to competition and their relative price sensitivity (elasticity), they will be in a position to make future pricing and promotion decisions based more on fact than supposition.

The price a company sets is a function of many factors including what the market will pay and what the competitors charge. It should not be done in a vacuum. Therefore, companies should

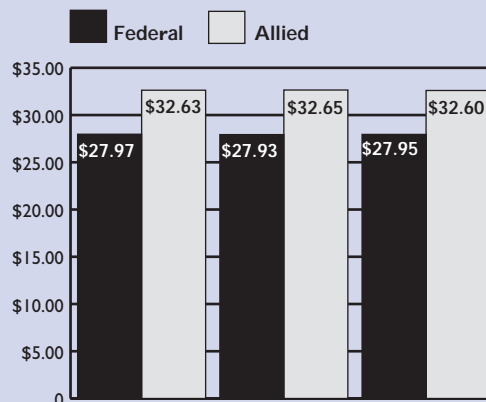
know how their products compare with their direct competitors—at the item level. Chart A tracks the Total U.S. retail price of two comparable items.

Allied is on target if its objective is to be 15 percent above Federal because of inherent product feature and quality differences. If, however, there are minimal differences and the objective is to be priced at parity with Federal, then Allied's pricing should be revised.

To make effective pricing decisions a company needs to understand its product's price sensitivity. In their book *The Marketing Revolution*, Clancy and Shulman made the following observations:

- The more consumers value any unique attributes that differentiate a product from competing products, the less sensitive they are to the product's price.
- Consumers are more sensitive to the price of one product when they are aware of substitutes.

Chart A 28 oz. Retail Price



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- The greater the expenditure, in both relative and absolute terms, the more sensitive consumers are to price.

- Consumers are less sensitive to the price of a product when they have made a large “sunk” investment in anticipation of its continued use—e.g. with an expensive camera, film becomes less important.

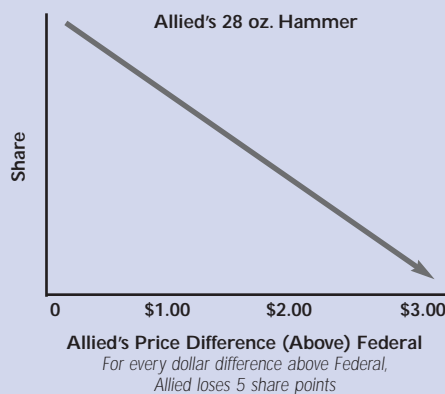
- Consumers are less sensitive to a product’s price when a higher price signals that the product is higher quality—e.g. image or exclusive products.

- Consumers are more price sensitive in the short term when they can hold inventories of a product and believe the current price is temporarily lower than it will be in the future.

The analysis of like items can be expanded by examining those occasions where the consumer has the opportunity of comparing the like items on the shelf. One can then determine on a store-by-store basis the difference in sales between the two items, when priced at parity, when priced above, and when priced below.

The item’s price elasticity can then be determined. By calculating the share of market done in each of the conditions (at parity, where Allied is \$1 above the competitive item, and where

Chart B Price Elasticity



Allied is \$2 above competition, etc.) the slope of the line can be determined. In Chart B, Allied loses 5 share points for every dollar it is priced above the comparable competitive product. This is important input to pending price and promotion decisions.

Information regarding a product’s current retail price, its comparison to competition and its elasticity are vital input to help companies sharpen their retail pricing decisions, thereby increasing their sales and profitability. It begs the question: what information is your company using in its pricing decisions?

To learn more about Vista’s information services, contact us at 847-253-6063 or visit our web site at www.vistainfoservices.com.

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MANUFACTURING NEWS

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“Manufacturing output in America is at the highest level in U.S. history and continues to support our economy. At the same time, manufacturers in the United States face unprecedented challenges—from rising energy and health-care costs and increased global competition to a serious shortage of skilled production workers, scientists and engineers that will intensify as the baby boom generation retires,” he said.

“The Facts book documents how manufacturing drives economic growth, productivity and innovation in America,” added Jerry Jasinowski, president of The Manufacturing Institute. The Facts book highlights six manufacturing pillars that support today’s U.S. economy:

- Manufacturing made the highest contribution (15 percent) of all sectors to real Gross Domestic Product (GDP) growth between 2001 and today.

- Manufacturing is the engine of American technology development and innovation, responsible for more than 70 percent of private sector R&D.

- Manufacturing’s high productivity rate—which determines real wage and benefit compensation—increased by more than 50 percent over the past decade and was far higher than for services.

- Manufactured goods make up more than 60 percent of U.S. exports, helping to pay for U.S. imports. While agricultural exports amount to about \$50 billion a year, manufacturers export that much each month.

- Manufacturing wages and benefits are approximately 25 percent higher than in non-manufacturing jobs.

- Manufacturing has a greater multiplier effect on the rest of the economy than does any other sector; each manufacturing dollar generates an additional \$1.37 in economic activity.