Retail Pricing Strategies

What Affects Pricing?

- Consumer Factors
  - Supply/Demand
  - Price Elasticity of Demand
    - Sensitivity of buyers to price changes
- Govt. Factors – FTC
  - Mfrs., Wholesalers, Suppliers
- Competition
- Strategy Variables
  - Target audience
  - Profits

Pricing Strategies

- Demand-oriented
- Cost-oriented
- Competition-oriented

Demand-Oriented

- Estimate how much customers will buy at various price levels
  - Set prices to achieve sales goals
- Determine prices acceptable to target market
  - Demand ceiling
  - Demand floor
- Psychological Pricing
  - Price/quality relationship
  - Odd pricing

Cost-Oriented

- Takes into account the cost of merchandise, retail operating expenses, and desired profits
- Markup covers operating expenses and profits
  - Markup = Selling price (retail price) – Cost of Goods

Zone Pricing:
"Refining companies actually map out areas and charge dealers different wholesale prices based on secret formulas that often factor in location, the area’s affluence or simply what the market will bear."

Wholesale Prices:
- CT.: Berlin $0.95
  - Greenwich 1.01
- NY: Albany $0.98
  - NYC 1.12
- Northern CA: Pleasanton $1.20
  - Palo Alto 1.35
Entrée Economics

- 300% solution: Many independently owned restaurants aim for an overall food markup of 300% or 4X the cost of the raw ingredients

- But, you might see a 500% markup on a grilled vegetable plate (and pay $9) and only a 200% markup on a tenderloin meal (and pay $25)

Pinot Bistro, Los Angeles
Grilled Pork Chop with white beans, pancetta, escarole, and assorted olives
Total Cost to Restaurant: $5.67
Menu Price: $19.95

Le Francais, Wheeling, Illinois
Trio of Lamb (mustard-crusted rack, cumin-dusted loin and braised shoulder with their own jus)
Total Cost to Restaurant: $16.81
Menu Price: $32.50

Pinot Bistro, Los Angeles
Persimmon Salad with grilled radicchio, crisp cress, and a red wine-cranberry vinaigrette
Total Cost to Restaurant: $2.42
Menu Price: $8.50

Charlie Palmer Steak, Las Vegas
New York bone-in shell
Total Cost to Restaurant: $8.33
Menu Price: $27.00

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Figuring Out the Tab

<table>
<thead>
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<th>Restaurant</th>
<th>Item Description</th>
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Cost Example

- Retailer buys a TV for $200 and wants to sell it for $300
  - Markup in $: $300 - $200 = $100
  - Markup % on Retail = 100/300 = 33%
  - Markup % on Cost = 100/200 = 50%

Markup

- Markup % (at retail)
  - \( \frac{\text{Retail Selling Price} - \text{Merchandise Cost}}{\text{Retail Selling Price}} \)

- Markup % (at cost)
  - \( \frac{\text{Retail Selling Price} - \text{Merchandise Cost}}{\text{Merchandise Cost}} \)

- Merchandise cost
  - What the retailer pays the mfr. (unit costs, freight costs, less discounts)

Initial Markup

- Initial value of merchandise less the cost of the merchandise

  Ex. A bike retails for $100 and costs the retailer $60
  - Initial markup is $40 (100-60)
  - 40% of retail (40/100)
  - 66% of cost (40/60)

Maintained Markup

- Based on the actual price received for the merchandise less the cost of the merchandise

  Ex. If the bike sells for $80, maintained markup is $20 (original retail price was $100)

  Maintained markup on retail is 20% (20/100)

How do you determine the initial markup?

- Initial Markup % (at Retail)
  - \( \frac{\text{Expenses} + \text{Profits} + \text{reductions}}{\text{planned sales} + \text{reductions}} \)

  Ex. A florist plans sales of $200,000, has operating expenses of $45,000, desires a profit of $35,000, and is expecting reductions of 20% of sales (or $40,000)

  \[
  \text{Initial markup} = \frac{45,000 + 35,000 + 40,000}{200,000 + 40,000} = \frac{50%}{100}
  \]

Maintained Markup %

- \( \frac{\text{Expenses} + \text{Profits}}{\text{Net Sales} \times 100} \)

  Florist:
  \[
  \frac{45,000 + 35,000}{200,000(100)} = \frac{40}{100} = 40\%
  \]
Florist Ex. (cont.)

- If flowers cost $8.00/dozen, what should the florist charge for the flowers (retail selling price)? Assume a 50% markup on retail.

\[
\text{Retail Selling Price} = \frac{\text{merchandise cost}}{1 - \text{markup}}
\]

So: $8.00
\[\frac{1}{1-.5} = 16.00\]

\[
\text{Retail Selling Price} = \text{Cost of Merchandise} + \text{Markup}
\]

Converting Markup from Retail to Cost

- \(\text{Markup \% on Cost} = \frac{\text{Markup \% on Retail}}{100\% - \text{Markup \% on Retail}}\)

Ex. If markup on retail is 18%, what is the equivalent markup on cost?

Answer: \(0.18\)
\[\frac{1}{1-.18} = 0.219\]

Converting Markup from Cost to Retail

- \(\text{Markup \% on Retail} = \frac{\text{Markup % on Cost}}{100\% + \text{Markup \% on Cost}}\)

Ex. If markup on cost is 36%, what is the equivalent markup on retail?

Answer: \(0.36\)
\[\frac{1}{1.36} = 0.26\]

What Should you Pay for Merchandise?

You are considering vendors for private label shirts. You would like the retail price of the shirts to be $25.00. Your markup objective is 45% on retail. What is the highest price you can pay to meet this objective?

\[
\text{Retail Selling Price} = \text{Cost of Merchandise} + \text{Markup}
\]

\[
\$25 = X + \$11.25
\]
\[100\% = 55\% + 45\%\]

So: 55% of $25 = $13.75

Determining the Most you Can Pay

- A buyer for men's clothing is seeking sport coats to retail for $125. The markup objective on retail is 48%. What is the most a buyer can pay a supplier for the jackets?

\[
\$125 (100\%) = X + (48\%)
\]
\[X = 52\%
\]

52% of $125 = $65.00

Setting the Retail Price

- A gift shop owner must pay a vendor $6.00 for a photo album and she wants to maintain a 60% markup on retail. What should she charge for the album?

\[
\text{Retail Selling Price} = \frac{\text{Merchandise Cost}}{1 - \text{Markup}}
\]

\[
\$6.00
\]
\[\frac{1}{1-.6} = \$15.00\]
Pricing Strategies

- Everyday Low Pricing
- High/Low Pricing
- Odd Pricing
- Leader Pricing
- Multiple Unit Pricing/Price Bundling
- Price Lining
- One-Price Policy

Markdowns

- Reduction in the initial retail price

\[
\text{Markdown as % of net sales} = \frac{\$ \text{ amount of markdown}}{\text{net sales}} \times 100
\]

Ex. You bought 100 sweaters and 80% sell at $50 each while the remainder sell at $30 each. Ans.: Markdown amount – 20 sweaters were marked down $20 each so $20 \times 20 = $400. Net Sales Revenue is (80 \times $50) + (20 \times $30) = $4600. Markdown % = $400 \div $4600 \times 100 = 8.69%

Advertising Markdowns to Consumers

\[
\text{Markdown % (of original retail value)} = \frac{\$ \text{ price reduction per unit}}{\text{original price per unit}} \times 100
\]

Ex. A sweater retails for $50 and is marked down to $30. What is the markdown %?

\[
\frac{20}{50} \times 100 = 40\%
\]