PRICING PSYCHOLOGY and POLICIES

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Psychology of Pricing

One of the reasons commercial flower growers and other nurserymen are in the business of growing and marketing plants is to make money. The revenue equation is simply the selling price per unit multiplied by the quantity sold (sold, not just produced!), and the profit or net income equation is revenues minus the costs or expenses equal profit. Therefore, pricing often determines the volume of business and directly influences the net income of the business. Pricing is also used to move inventory, promote sales, and attract customers.

The key to successful pricing is to provide customers an option. Of value to the customer is the marketer's ability to justify the price. Obviously, a low or inferior quality justifies only a low or cheap price. Higher quality, new colors, new or exciting varieties and cultivars, novelties, bundled merchandise, or an aesthetic or pleasureful buying experience warrant higher prices.

The key economic principle is supply and demand, whereby as the market forces (landscaping and gardening needs, consumer purchasing power, influences of promotion and advertising, "you have it, I want it, I'm buying it!," etc.) increase demand, prices increase. After all, price rations the available supply of merchandise. Customers are either price sensitive and will shop around for a favorable price, or they are price insensitive and almost impulsive in their buying habits. Flowers and decorative plants are price insensitive items for which the purchase decisions are governed by quality, supply, sensory experiences (color, appearance, form, smell), and value.

Retail garden centers and commercial flower growers tend to price plant materials too low. There are at least three special problems associated with these markets: (a) they must cover the risks of perishable items; (b) they must earn a reasonable return on investment with a relatively slow inventory turn; and (c) they must cover the costs of creating demand for their plants and their business.

Pricing rules worth remembering include:

- ✔ Competitors' prices must not determine your own pricing policies.
- ✔ Buyers tend to tie price to quality.
- ✔ Innovative, better, different, bundled products command higher prices.
- ✔ The market establishes the price; let the customers have the pleasure of paying a fair price.
- ✔ It's less costly to do better marketing and promotion than to cut price.
- ✔ Some customer grumbling is to be expected if the products are priced appropriately.
- ✔ Adjust prices in increments, not all at once.

Pricing Policies and Methods

The question of pricing causes some headaches among commercial growers. The pocketbook tells you that prices are too low to cover the rising production costs, but your competitive instinct tells you that if you raise prices you are running the risk of losing customers and sales, especially if your target market is the retail and/or landscape trade. Where can you find relief? A successful pricing strategy includes an analysis of personal and business objectives, the competition, the market, and what customers are willing to pay.

Prices may be determined or based on cost, intuition, imitation, or any combination of the three. Cost-based prices are computed by adding a desired markup to the total cost (overhead or fixed costs plus variable or per unit costs) of growing and marketing the goods to represent profits. Cost-based pricing is the only one sure method of guaranteeing a profit to oneself. Intuition prices are based on what the marketer thinks the customers are willing to pay, and that takes luck, experience, and trial-and-error. Imitation-based prices are set either below, at, or above those of the competitors. Setting prices in relation to the competition's prices is dangerous because cost of production and marketing, including overhead expenses, are different for every grower and every operation. One grower may make a profit at a certain price, while another grower may lose money at that same price due to higher total costs. A successful pricing strategy should incorporate an analysis and implementation of all three pricing methods.

Pricing is a process that results in profits or losses. Costs, customers, and competition may change and prices must be adjusted as these changes occur. The first step is to gain a thorough knowledge of the total cost of each plant, product or service offered to sell. The second step is to determine whether a market exists for that plant, product or service at that price. If the market analysis reveals that adequate demand exists for the plants evaluated and at the prices necessary for the grower to achieve the stated goals and objectives of the business, then an appropriate inventory should be amassed by one's own production or buying in materials from other growers.

A three-way balance between selling prices, sales volume, and expenses is required. Low prices may generate a high sales volume, but may not produce enough income to cover expenses, let alone create a profit. High prices may not generate enough volume to cover expenses; recall the revenue equation. The overall objective is to produce the largest total profit for the business, not the largest profit per plant or item nor the largest sales volume.

Psychological Price Barriers at Retail

Price barriers are a series of check points customers use to determine the relative value of a product. Major price barriers exist at \$1, \$5, \$10, \$15, \$20, and so on, and are common to all customers.

Minor barriers exist at $1.50, $2.00, $3.00, $7.00, etc., and their importance varies depending on the customer's need for the product, desire for the product, and amount of discretionary income to pay for the product. The objective is to establish prices just below a price barrier. The following two tables provide an easy reference for determining prices using psychological price barriers.

Price Barriers in Green Goods:

Major Price Barriers	Minor Price Barriers	Suggested Plant Prices
$ 1.00		$ 0.99
	$ 1.50	1.49
	2.00	1.99
	3.00	2.99
5.00		4.99
	7.00	6.99
	8.00	7.99
10.00		9.99
	13.00	12.99
15.00		14.99
	17.00	16.99
	18.00	17.99
20.00		19.99
	23.00	22.99
25.00		24.99

Suggested Retail Prices for Green Goods:

Costs ($) From	Costs ($) To	Retail Price ($)	Maximum GPM (%)
0.00	0.44	0.99	–
0.45	0.58	1.29*	65
0.59	0.63	1.49*	70
0.64	0.76	1.79*	64
0.77	0.90	1.99	61
0.91	1.12	2.49*	63
1.13	1.35	2.99	62
1.36	1.80	3.99*	66
1.81	2.25	4.99	64
2.26	3.14	6.99	68
3.15	3.60	7.99	61
3.61	4.50	9.99	64
4.51	5.85	12.99	65
5.86	6.75	14.99	61
6.76	7.65	16.99	60
7.66	8.09	17.99	57
8.10	9.00	19.99	59
9.01	10.35	22.99	61

[Suggested retail prices based on a minimum gross profit margin (GPM) of 55%; and * indicates the suggested retail prices are between barriers for a competitive market.]

Variable Pricing

Hidden costs such as perishability and special handling requirements are often overlooked in pricing, resulting in lower than expected profit margin. When plants require special care or handling, or are very perishable, or are subject to greater than usual breakage, damage or death losses, then the base cost can be adjusted by adding allowances for hidden costs. The following example illustrates how to establish the "real" cost before pricing an unusual, difficult to maintain plant and a common, easily maintained plant that each cost $11.00.

Quality Differentiation

	Unusual Plant	Common Plant
Costs Incurred	$ 11.00	$ 11.00
Add: Perishability (10%)	1.10	0
Add: Special Care & Handling	0.50	0
Actual Cost	12.50	11.00
Selling Price With 55% GPM	28.00	24.45
Price Barrier Adjustment	29.99	24.99

A pricing strategy that merits consideration is to allow customers to buy the quality they can afford or want. Any block or shipment of plants contains plants of varying quality. If all the plants from one block or shipment are priced identically, the good quality will sell first and a selection of poorer quality plants that look overpriced will remain. Instead, a median price for each plant from that block or shipment can be calculated, and higher quality plants priced higher, medium quality plants priced at the median price, and lower quality plants priced lower than the median price. Customers than have the option of buying the price and quality combination they desire. Customers typically are not looking for the same high quality (and prices) of plants for use in a landscape mulch bed as would be used as foundation plantings or in flower boxes.

Penetration Pricing Versus Price Skimming

A skimming strategy is when prices are set artificially high initially, then gradually reduced. Customers who want the product will pay the higher price, leading to higher short-term profits. This strategy is most successful with a new or unusual product that is without direct competition. Many people associate quality with price and they may be more willing to pay higher prices because of perceived enhanced value. If the price is set too high, it can be lowered.

For penetration, prices are set deliberately low in an attempt to gain a large share of the market. Once the market share has been gained, prices will gradually be raised to maintain an adequate profit margin. Loss-leader pricing is similar in result but the intent of the loss-leader strategy is to grab the attention of the customers and draw them into the business. Impulse pricing using low prices to encourage sales for slow movers in the inventory. Likewise, the word "sale" attracts bargain hunters and price sensitive shoppers.