

The psychology of pricing - How to arrive at the 'right' price for your products or services

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One of the most common challenges facing entrepreneurs, in general, is uncertainty around the correct strategy as far as the pricing of their products and services is concerned.



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This is not surprising, because unlike costing - which is a more precise and exact science - the psychology of pricing is murky and influenced by many factors.

These include the nature of the product or service, the target market, brand equity and positioning, distribution strategy, the scarcity or availability of the commodities in question, right down to factors such as packaging, product quality, originality and even current economic and inflationary trends.

In fact, the variables are so many and varied that it can feel like one needs to be a combination of the actuary, cost accountant, marketing guru, MBA and psychic to stand any chance of getting it right.

Frankly, it doesn't have to be that complicated. While we would caution against simply whacking 100% on your costs (as many do) to arrive at a selling price, if you follow a few fundamental truths, you should be able to derive a price that is right for you and your customers.

Know your costs

This is the bedrock of arriving at a sustainable pricing strategy. Simply put, if you do not know what a product or service costs you to make or deliver, you are not in a position to confidently set a price for it. Understanding your costs is fundamental to business success, not just as far as pricing goes but also in terms of managing production and input costs, identifying bottlenecks, maintaining healthy cash flow and optimum allocation of resources.

Add value

Studies have shown that many consumers do not view price as the most important element when deciding which product or service to choose.

A [recent report by McKinsey](#) found that across most of the Lifestyle Series Monitor (LSMs), insights show that although price is becoming a more important determinant as living costs spiral, a large percentage of consumers are still more concerned with value than price – in other words, people will pay the price asked as long as they feel they are getting value for their money.

So, your job is to find ways of adding value to the customer who buys your product or service. Some examples might be a five-year guarantee on the product, a loyalty programme (previously seen as the domain of the big brands only, but not anymore), competitions and giveaways, and any other activities that create the perception of 'good value for money'.

Discount strategically

One major Achilles Heel of the small business sector is the lack of a sustainable and well-thought-out discounting strategy, especially when just starting out. A strategy dedicated to how you discount may sound like overkill but consider this – if you offer your existing client base a discount of 10% on a product or service with a Gross Profit (GP) of 30%, you will need 50% more customers to make the same turnover as you are currently making. Let that sink in for a moment....

Our philosophy as far as discounting is concerned is a simple one; it has to be a two-way street. 'I give you a discount, and you give me something back in return' is a pretty good strategy to follow – perhaps that 'something' is a bigger order, a deposit to help with your cash flow, more favourable payment terms, a longer contract period or some form of brand exposure or promotion. The alternative is just taking money out of your own pocket.

Be ready to defend your price

When you enter a sales negotiation with a prospective customer, any buyer worth their salt will try and squeeze you for a better price. Be prepared by making sure you can defend your price when called upon to do so.

You do this in several ways – excellent product knowledge, an understanding of your competition and what they offer (and charge) for similar products and services, a clearly defined set of USPs (unique selling propositions – those unique, value-adding elements that make your product or service different or special).

Most importantly, the confidence and belief in your product or service to stand your ground when necessary. Rather lose a sale in the short-term, than be bullied into selling at an unsustainable price. We always encourage entrepreneurs to take a long-term view on pricing and to avoid too much short-term sacrifice unless it is strategic.

As we said at the outset, pricing is not an exact science. However, by blending a bit of confidence and common sense with

a more strategic approach, you can develop a pricing strategy that fulfils its primary aim – to make your business profitable.

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