Calculating Markup: A Merchandising Tool

Pricing Strategies

Pricing strategies and policies are impacted by external environmental factors as well as internal company factors such as the company's objectives, resources, and management's philosophy. Some of the external factors affecting retail pricing include consumer, industry, and market trends; societal and cultural trends; economic trends (e.g., unemployment rates, interest rates, tax rates); political happenings; legislative regulations; and global sourcing trends. Another major external factor that affects retail pricing is that of the competition. Since many retailers carry the same brands and identical merchandise classifications, an astute buyer must price merchandise competitively. Customers usually do not pay higher prices at one store, when they can walk across the street to another store and buy the same merchandise at a reduced price from the competition.

There is a multitude of internal store components that the retailer must consider when deciding upon markup percent and pricing product. They include store type, channel of distribution, image, customer services, type of merchandise, etc. The *store type* and *channel of distribution* affect the price expectations of the consumer. Stores with a prestigious *image* can demand a higher price for their merchandise than those in the discount, off-price or mass merchant channel of distribution. In fact, the business models of discount stores are often based on sparse décor, high sales volume, and low markup. Additionally, the types and quantity of *customer services* provided by a store help to dictate the retail price of the product. For example, a more exclusive store with beautiful décor in a high rent area or a specialty store that offers specialized customer services must take higher markups on its merchandise assortment in order to meet profit goals, while providing exclusivity for the consumer.

The *type of merchandise* carried by the retailer has a major impact on retail pricing or establishing the markup on the product classification. As previously discussed, different types of merchandise classifications may carry higher markups than others. For example, many times *basic merchandise categories* carry a lower markup than expensive, *higher fashion seasonal products*. With trendy or high fashion seasonal merchandise, sometimes costly markdowns are required to sell the inventory. Therefore a higher markup must be planned in order to cover those reductions. Further, items such as fine jewelry or expensive designer goods have a higher risk of theft, need to be merchandised in a specific location in an exclusive setting, and/or demand high qualified sales associates to sell the goods. Thus, additional markup is needed to cover the operating expenses when pricing these goods. Also, the merchandise *brand* type (i.e., designer, national, private, licensed, store, generic) impacts the markup and thus the retail price of product. National branded products are usually sold at or near the same retail price by all retailers in the same geographic location, since these retailers more than likely paid the same wholesale cost and similar shipping costs for the goods.

In today's competitive market environment, major retailers are developing private label product for their stores. The private label merchandise more than likely will have a higher markup than the national brand since the retailer controls the entire development of the product, including pricing. However, some retailers may use private label to create store traffic, thus taking a lower markup on the brand in order to create value for the consumer. Or, these retailers may utilize private label to help position their store and/or product assortment in the marketplace in order to differentiate themselves from the competition.

Additionally, the *consumer's perception* of price is a major factor in retail pricing. The consumer often decides what value is desired for a specific price. Value may be a combination of price, product attributes and features, positioning of product in the marketplace, fashion level of the product, and image cues such as brand and packaging, along with other factors that the customer determines to be important. Most consumers want the most value for the lowest price. However, they will pay higher prices if they desire an exclusive or a specific brand of merchandise. For most retailers, there is a problem with meeting the consumer's perception of value, since every consumer has a different definition for the value/price equation. It is very difficult for the retailer to address all of the "value" definitions held by the various target consumers frequenting the store.

Lastly, when planning markup, the retailer must consider operational factors such as *promotional costs* needed to market the merchandise and store. Frequently during the selling season, the retailer must create traffic in the store in order to reach sales goals. On these occasions, the retailer may select specific merchandise classifications to sell at below or near wholesale costs. These products are called *loss leaders* and must be addressed by the retailer when determining initial markup.

Based on the above factors, the retailer must establish a realistic pricing strategy for his retail venue. No one strategy is appropriate for all store types, merchandise categories or geographical markets. The major **Pricing Strategies** include: a) new product pricing, b) consumer demand pricing, c) customer value based pricing, d) cost oriented pricing, and e) competitive pricing. All of these pricing strategies with their major types of pricing models will be discussed below in *Part 3: 3-2 pricing Types*.