

SOS POLITICAL SCIENCE AND PUBLIC ADMINISTRATION

MBA HRD 406 (B)

SUBJECT NAME: FUNDAMENTALS OF RETAIL MANAGEMENT(OPT.PAPER)

UNIT-IV

TOPIC NAME- MULTIPLE UNIT PRICING

When products have different values for different customers, profits can sometimes be enhanced by using multiple-unit pricing strategies. With multiple-unit pricing, all customers typically face the same pricing schedule, but the price paid is determined by the value to consumers of the total amount purchased. Unlike single-unit pricing, where all customers are charged a unit price that sets $MR = MC$, multiple-unit pricing can result in some combination of per-unit and “lump sum” fees. Like price discrimination, multiple-unit pricing strategies have proven an effective means for extracting consumers’ surplus for the benefit of producers.

Selling a product at a price lower than that of other products of the same category is called Multiple Unit Pricing. This is true, especially in case of bulk orders.

Let us breakdown the definition. A product is sold at a pre-decided price, which is equal or less than the maximum retail price or list price of the product. But to increase the sales of the product or to uplift the number of customers, retailers or even companies have offers and give freebies.

Usually, the free product is the same product which is purchased in bulk, and it comes at either lesser or free of cost — for example, One bar of soap-free on purchase of 4 bars of soap.

So one bar is priced at \$1.25, but customers can get 5 for \$5. This reduces the effective net price of the product per unit.

When should you use Multiple Unit Pricing?

Multiple Unit pricing is a pricing strategy which is used as a marketing strategy to push the sales of the product. Following are few of the times when Multiple Unit pricing is used:

#1. Higher Sales by Multiple Unit Pricing

The strategy of Multiple Unit Pricing is used either by organizations or retailers to push their product for higher sales. Higher sales are targeted to achieve higher market potential and higher conversion of the customers.

Usually, this is implemented during large sale days, which are coupled with festival days or other shopping days like Black Friday. The price is reduced with the bulk purchase, and the customer is shown about the drastic reduction in price and the price benefit which he will be achieving.

Higher sales are also a concern in the case of target achievement. When the target of the sales team is to be achieved, and the duration for Sales closing is very less, in such cases, high sales becomes a priority, and Multiple Unit Pricing is used.

#2. Exhausting existing stock

When the companies or the retailers have a stock lying for several days, which may border on expiry or be near expiry, in such cases the stock is tried to finish off within the given date, and multiple-unit pricing is used in such cases.

It is mandatory, especially in case of pharmaceutical products or other consumer care products that they should not be sold after expiry dates and in such cases, the stock should be thrown off or disposed of suitably, which will be invariably loss for everyone.

To avoid such losses, multiple-unit pricing is used, and the stock is liquidated by providing bulk offers.

#3. Market Penetration with new products

Most of the times when a product is launched, it has to face the competition of existing products. The existing products have been in the market for a long time and have a bigger and wider customer base.

Combating an established product in the market requires a penetration strategy which will not only increase the customer base but also increase sales of the product over competition and provide an edge over the competition by increasing the market share.

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#4. Customized Deals

Multiple unit pricing is also used in case of customized deals. When there are bulk orders and customized deals, the buyer expects a better price on the products. Few free units are coupled with the order in order to reduce the per product price, thereby implementing Multiple Unit Pricing.

Multiple unit pricing is used in customized deals in case of dealing with supplier-manufacturer deals. For example, the deal is that on purchase of 100 units of a certain product, the supplier will get ten units for free of cost, the buyer can propose a deal of buying 500 units of products at one time and request for 60 units free.

#5. Penetration with existing products

When organizations want to increase the existing share of the products, multiple-unit pricing is provided. This not only increases sales but also gets a number of customers and penetrates existing share of the products in the market.

Example, to increase the sale of Pantene Shampoo it will be coupled with offers of Buy 4 Get 1 Free or Buy 1 Get one free.

Multiple Unit Pricing Examples

Two-Part Pricing

Athletic clubs, time-share vacation resorts, golf courses, and a wide variety of “membership organizations” offer goods and services using two-part pricing. A common two-part pricing technique is to charge all customers a fixed “membership” fee per month or per year, plus a per-unit usage charge. In general, a firm can enhance profits by charging each customer a per-unit fee equal to marginal cost, plus a fixed fee equal to the amount of consumers’ surplus generated at that per-unit fee.

In the case of golf course memberships, for example, two-part pricing often consists of a large lifetime membership fee plus “greens fees” charged for each round of golf played. To illustrate how such a two-part pricing practice might prove profitable, assume that an individual avid golfer’s demand and marginal revenue curves can be written $P = \$100 - \$1Q$ and $MR = \Delta TR/\Delta Q = \$100 - \$2Q$ where P is the price of a single round of golf, and Q is the number of rounds played during a given year. For simplicity, also assume that the marginal cost of a round of golf is \$20, and that fixed costs are nil. This gives the following total and marginal cost relations:

$$TC = \$20Q$$

$$MC = \Delta TC/\Delta Q = \$20$$

As shown in Figure, the profit-maximizing single-unit price for a monopoly golf course is found by setting $MR = MC$, where

$$MR = MC$$

$$\$100 - \$2Q = \$20$$

$$2Q = 80$$

$$Q = 40$$

At the profit-maximizing quantity of 40, the optimal single-unit price is \$60 and total profits

$$\text{qual } \$1,600 \text{ because}$$

$$P = \$100 - \$1(40)$$

$$= \$60$$

$$\pi = TR - TC$$

$$= \$60(40) - \$20(40)$$

$$= \$1,600$$

Notice from Figure that the value of consumers’ surplus at a standard per-unit price is equal to the region under the demand curve that lies above the profit-maximizing price of \$60. Because the area of a such a triangle is one-half the value of the base times the height, the value of consumers’ surplus equals $\text{Consumers’ Surplus} = 1/2 [(40) \times (\$100 - \$60)] = \800 . In words, this means that at a single-unit price of \$60, such an individual will choose to play 40 rounds of golf, resulting in total revenues of \$2,400 and total profits of \$1,600 for the golf course.

The fact that consumers’ surplus equals \$800 means that the avid golfer in question would have been willing to pay an additional \$800 to play these 40 rounds of golf. This is an amount above and beyond the \$2,400 paid. The avid golfer received a real bargain.

As an alternative to charging a single-unit price of \$60 per round, consider the profits that could be earned using a two-part pricing scheme. To maximize profits, the golf course would choose to charge a per-unit price that equals marginal cost, plus a fixed fee equal to the amount of

consumers' surplus received by each consumer at this price. Remember, in Figure, that the value of consumers' surplus is equal to the region under the demand curve that lies above the perunit price. When the per-unit price is set equal to marginal cost, $P = \$20$ and $Q = 80$ because

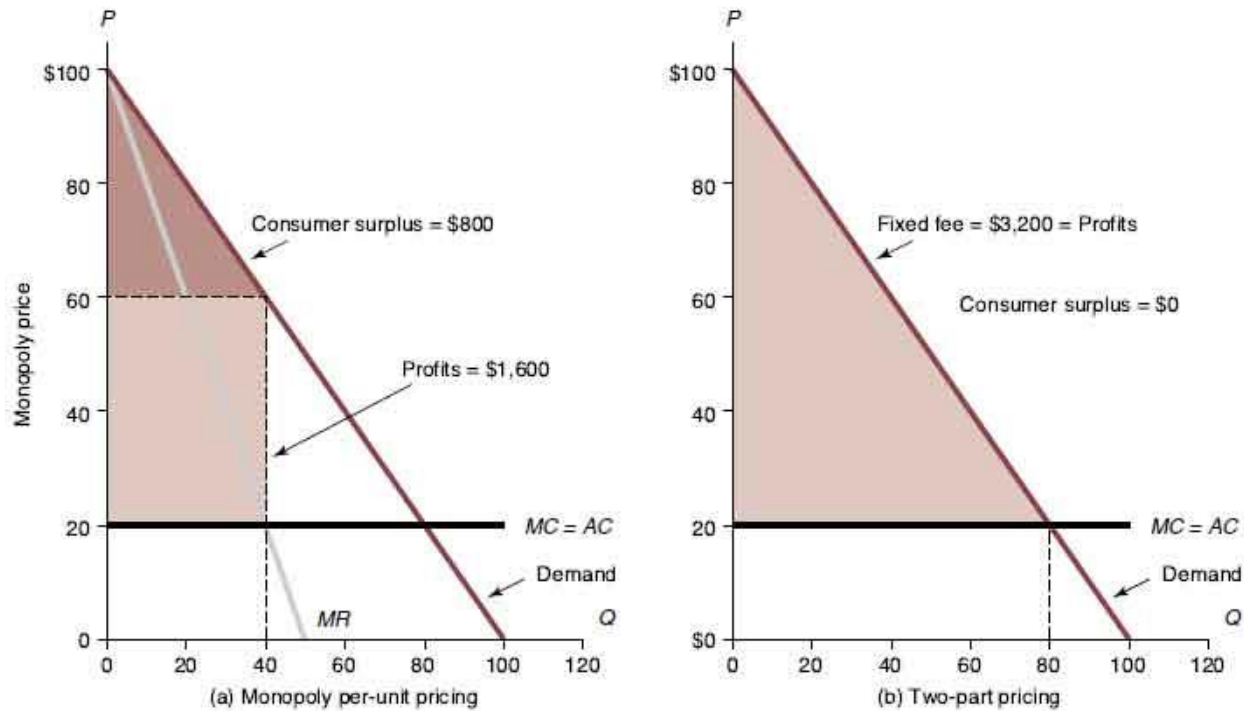
$$P = MC$$

$$\$100 - \$1Q = \$20$$

$$Q = 80$$

At the per-unit price of \$20 and output level of 80, the value of consumers' surplus equals

Monopoly Per-Unit Pricing Versus Two-Part Pricing



$$\text{Consumers' Surplus} = \frac{1}{2} [(80) \cdot (\$100 - \$20)] = \$3,200$$

Thus, \$3,200 is the maximum membership fee the golfer in question would pay to play 80 rounds of golf per year when modest additional “greens fees” of \$20 per round are charged. It follows that the profit-maximizing two-part pricing scheme is to charge each player an annual membership fee of \$3,200 per year plus “greens fees” of \$20 per round played. Total golf course revenues of \$4,800 represent the full value derived from playing 80 rounds of golf per year, cover marginal costs of \$1,600 ($= \$20 \cdot 80$), and result in a \$3,200 profit for the golf course.

Throughout this discussion it has implicitly been assumed that the seller must enjoy at least some market power in order to institute any two-part pricing scheme. Otherwise, competitors would undercut the amount of annual membership fees, and per-unit prices would converge on marginal costs. Therefore, it is unsurprising that high golf membership fees tend to be most common in urban areas where conveniently located golf courses are in short supply. In outlying or rural areas, where restrictions on the location of new golf courses are less stringent, large membership fees tend to be relatively rare.