

Chapter 26 Pricing Strategies

Section 26.1 Basic Pricing Policies



Real-World Application Policy Analysis

Directions Read the article below, and then answer the questions that follow.

Costco—A Warehouse Retailer with Low Prices

With a combination of low markups, bare bones design, and a wide merchandise mix, the warehouse retailer Costco is able to offer customers low prices daily. Costco stores are the epitome of no frills. They are warehouses with merchandise stacked to the rafters.

While Costco carries only a few brands and sizes, it offers an impressive range of products, from groceries to household products, from clothes, books, and music to furniture and even luxury items. Fresh food accounts for 10 percent of Costco's annual sales. Costco customers can get their photos processed in the hour it takes to pick up fresh salmon, Waterford crystal, and motor oil. Customers can also get an eye exam and have glasses made, and at some locations they can fill up with gas that is up to 25 cents a gallon cheaper than retail gas stations.

Costco relies on a predictable pricing strategy. It keeps markups between 10 and 14 percent above cost, well below the minimum 25 percent for most retailers. And Costco avoids selling items at cost to attract customers, instead relying on a low markup to ensure that prices on all items stay low. In addition, Costco charges all its customers a membership fee: \$45 for business owners and the general public, and \$100 for executive memberships with added features.

Costco does not have as many stores as Sam's Club, a major competitor. There are about 300 Costcos compared with around 530 Sam's Clubs (a subsidiary of Walmart). Another competitor is BJ's Wholesale Club, with around 150 locations. Regardless of number of locations, Costco manages to generate greater annual sales per store—\$112 million—which is significantly higher than the \$63 million per store for Sam's Club and \$46 million for BJ's Wholesale Club.

1. How does Costco demonstrate cost-oriented, demand-oriented, and competition-oriented pricing?

Copyright © by The McGraw-Hill Companies, Inc. All rights reserved. Permission is granted to reproduce this page for classroom use.

Chapter 26 Pricing Strategies

Section 26.1 Basic Pricing Policies



Real-World Application

Policy Analysis *(continued)*

2. Is Costco's pricing policy more representative of a one-price policy or a flexible-price policy? Explain your answer.

3. How is Costco able to keep its prices so low and still be profitable?

4. Why do you think Costco's annual sales per store exceed those of its competitors?

Chapter 26 Pricing Strategies

Section 26.1 Basic Pricing Policies



Study Skills Learning New Vocabulary

Directions Use the following tips to help improve your vocabulary. Then match each definition with the correct term from the Word Bank.

Learning New Vocabulary
<ul style="list-style-type: none"> • When performing a matching exercise, match the easiest, most recognizable words first. The amount of choices left may make finding the remaining pairs much easier. • Think about synonyms and antonyms to new vocabulary or to key words in their definitions. How closely do the synonyms or antonyms relate to the key term? • Once you learn a new word, try to use it right away—either verbally in a conversation or on paper in a sentence.

Word Bank		
bundle pricing	cost-plus pricing	discount pricing
EDLP	flexible-price policy	markup pricing
penetration pricing	prestige pricing	promotional pricing
seasonal discounts	skimming pricing	trade discounts

- _____ 1. The price of a new product is set very high to capitalize on the high demand during its introductory period.
- _____ 2. Prices are reduced for a short period of time.
- _____ 3. The seller offers reductions from the usual price.
- _____ 4. These price breaks are offered to buyers who are willing to buy in advance of the customary buying season.
- _____ 5. The initial price for a new product is set very low in order to encourage as many people as possible to buy it.
- _____ 6. A company sets prices consistently low with no intention of offering discounts in the future.
- _____ 7. Prices are higher than average to suggest status and an upscale image to the consumer.
- _____ 8. Some manufacturers quote prices to wholesalers and retailers in this way.
- _____ 9. Arriving at a price by adding a dollar amount to the cost of an item.
- _____ 10. This permits customers to bargain for merchandise.

Copyright © by The McGraw-Hill Companies, Inc. All rights reserved. Permission is granted to reproduce this page for classroom use.