

# HOSPITALITY AND TOURISM MARKETING

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Lecture 9: Pricing objectives and approaches

# Course outcomes

At the end of this lecture, you will be able to:

- Explain clearly **factors to consider when setting prices** for hospitality and tourism products/services
- Describe **correctly pricing objectives and approaches** for hospitality and tourism products/services

# Price

- price is the amount of **money** charged for a good or service.
- More broadly, price is the **sum of the values consumers exchange for the benefits of having or using the product or service**



Theworldnote, (2020), 5000 Rwandan franc note & bill\_FRw 5000, [https://encrypted-tbn0.gstatic.com/images?q=tbn:ANd9GcQria3dxhK\\_gAXBGDULUaQ1nH4y1D6evDLR9Q&usqp=CAU](https://encrypted-tbn0.gstatic.com/images?q=tbn:ANd9GcQria3dxhK_gAXBGDULUaQ1nH4y1D6evDLR9Q&usqp=CAU)

# Price (cont')

- ❑ Marketers and managers must have an understanding of price.
- ❑ Charging **too much chases away potential customers.**
- ❑ Charging **too little can leave a company without enough revenue** to maintain the operation properly.

# Factors to Consider When Setting Prices

- ❑ **Internal and external** company factors affect a company's **pricing decisions**.
- ❑ Internal factors include the company's **marketing objectives, marketing mix strategy, costs, and organizational considerations**.
- ❑ External factors include **the nature of the market, demand competition, and other environmental elements**.

# Internal versus External Factors



Kotler and Armstrong, (2006), Principles of Marketing (activebook 2.0 ): Chapter 11,  
[http://www.laukamm.de/fomweb/elearning/marketing/pricing/kotl\\_price\\_setting-Dateien/abkotler10\\_11\\_01.gif](http://www.laukamm.de/fomweb/elearning/marketing/pricing/kotl_price_setting-Dateien/abkotler10_11_01.gif)

# Internal Factors Affecting Pricing Decisions

- **Marketing Objectives**

- ❑ Before establishing price, a company must select a **product strategy**.
- ❑ If the company has selected a target market and positioned itself carefully, its marketing mix strategy, including **price**, will be more precise

## Marketing Objectives (cont')

- For example, **Four Seasons** positions its hotels as **luxury hotels** and charges a room rate that is **higher** than most.
- Motel 6 and Formula One have positioned themselves as **limited-service motels**, providing rooms for **budget-minded travelers**



Marina, (2021), Benefits & Features of a Luxury Hotel ,  
[https://hotelenglishpoint.com/blog/wp-content/uploads/2021/05/DJI\\_0949-Edit-768x395.jpg](https://hotelenglishpoint.com/blog/wp-content/uploads/2021/05/DJI_0949-Edit-768x395.jpg)

## Example of companies' objectives

- Survival objectives
- Current Profit Maximization objectives
- Market- share leadership objectives
- Product-Quality leadership objectives
- Other objectives

# Marketing Mix Strategy

- ❑ Price must be coordinated with **product design, distribution, and promotion decisions** to form a consistent and effective marketing program.
- ❑ Decisions made for other marketing mix variables may affect **pricing decisions**.

# Costs

- ❑ Costs set the **floor** for the price a company can charge for its product.
- ❑ A company wants to charge a price that covers its costs for **producing, distributing, and promoting the product.**
- ❑ Beyond covering these costs, the price has to be **high enough to deliver a fair rate of return to investors.**

## Cost (cont')

- Costs take two forms, **fixed and variable**.
- **Fixed costs (also known as overhead)** are costs that do not vary with production or sales level.
- a company must pay bills each month for **rent, interest, and executive salaries**.
- Variable costs vary directly **with the level of production**
- a salad, rolls and butter, the main course, a beverage, and a dessert>< all are example of variable cost
- **Total costs are the sum of the fixed and variable costs for any given level of production.**

# Organizational Considerations

- Management must decide **who** within the organization should set prices.
- Companies handle pricing in a variety of ways.
- In **small companies, top management**, rather than the marketing or sales department, often sets the prices.
- In **large companies**, pricing is typically handled by a **corporate department or by regional or unit managers** under guidelines established by corporate management.

## Organizational Considerations (cont')

- Many corporations within the hospitality industry now have a **revenue management department** with responsibility for pricing and coordinating with other departments that influence price.
- **Airlines, cruise lines, auto rental companies, and many hotel chains** have developed revenue management departments.

# External Factors Affecting Pricing Decisions

- **Market and Demand**

- ❑ Although costs set the lower limits of prices, the market and demand set the **upper limit**.
- ❑ Both consumer and channel buyers such as tour wholesalers balance the product's price against the benefits it provides

# Analyzing the Price–Demand Relationship

- Each price a company can charge leads to a different **level of demand**.
- The demand **curve** illustrates the relationship between price charged and the resulting demand.
- In the normal case, **demand and price are inversely related**; that is, the higher the price, the lower the demand

# Price versus Demand

Figure 1

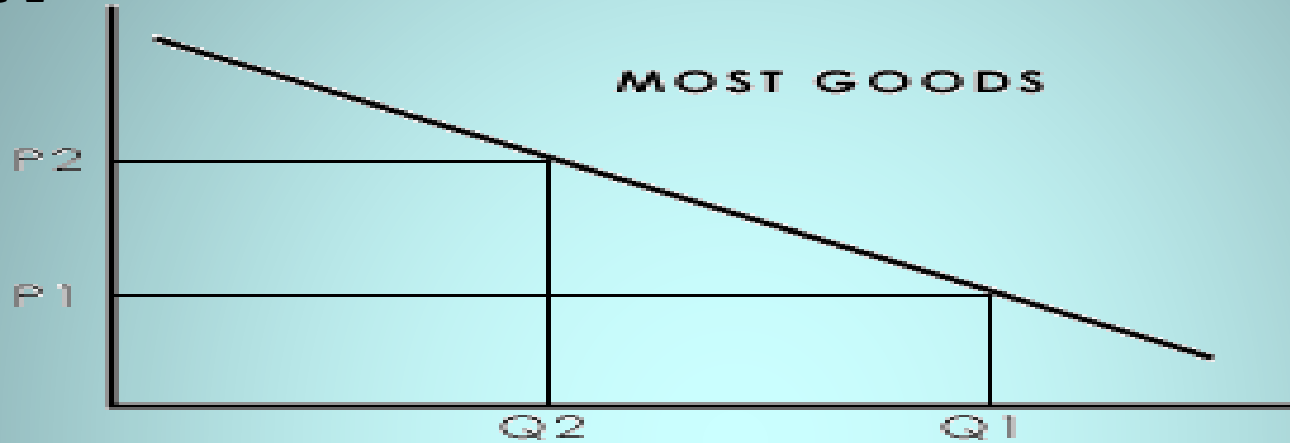
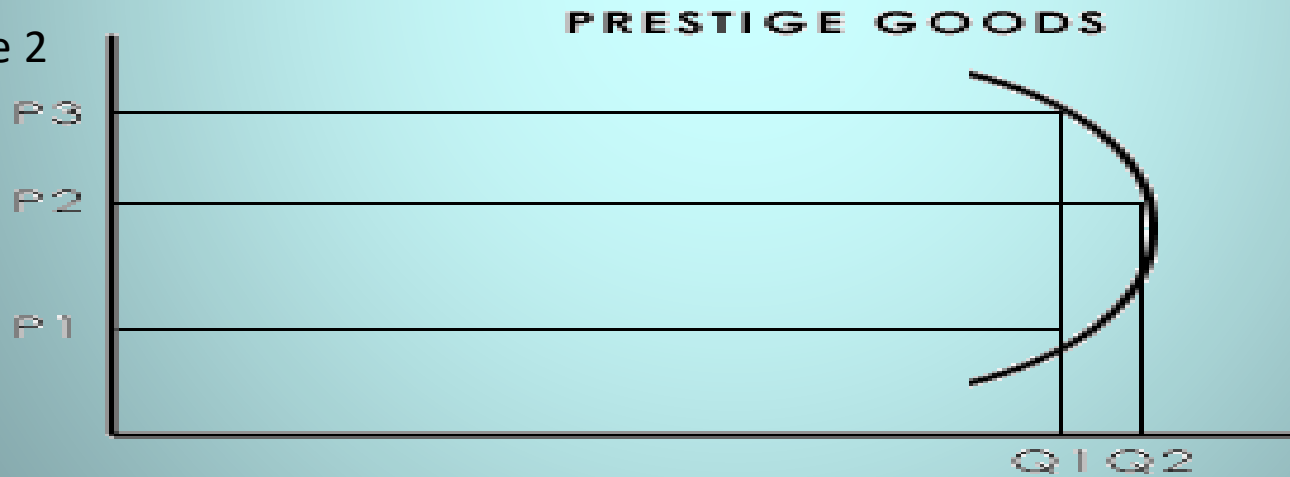


Figure 2



Copyright Prentice Hall, 1996

# Price Elasticity of Demand

- Marketers also need to understand the concept of price elasticity, how responsive demand will be to a change in price. Consider the two demand curves in previous slide. In Figure 1, a **price increase from P1 to P2 leads to a small drop in demand from Q1 to Q2.**
- In Figure 2, however, the same price increase leads to a **large drop in demand from Q1 to Q2.**

# Factors Affecting Price Sensitivity

- unique value effect
- Substitute Awareness effect
- business expenditure effect
- end-benefit effect
- total expenditure effect
- Price Quality effect

# Price-Rate Compression

- ❑ During periods of **weak demand** very few competitors escape the effect of a weak market
- ❑ Price (rate) compression occurs when the difference between room rates for three to four and five-star properties **is not significant.**
- ❑ This occurs when higher priced hotels **lower** these rates to maintain occupancy and **become direct competitors to lower-rated hotels.**

## Other External Elements

- ❑ When setting prices, the company must also consider other factors in the external environment.
- ❑ Economic factors such as **inflation, boom, or recession and interest rates** affect pricing decisions.

# Consumer Perceptions of Price and Value

- ❑ In the end, it is the consumer who **decides** whether a product's price is **right**.
- ❑ When setting prices, management must consider how consumers **perceive price and the ways that these perceptions affect consumers' buying decisions**.
- ❑ Like other marketing decisions, pricing decisions must be **buyer oriented**.

## Consumer Perceptions of Price and Value(cont')

- ❑ **“We can’t see the value of our product,”** explains Carlos Talosa, senior vice president of operations at Embassy Suites.
- ❑ **“We can only set price. The market value is set by our customers and our ability to sell to it.”**
- ❑ According to Talosa, **“Even in recessionary times, consumers aren’t necessarily buying the cheapest options, but they are demanding value for their dollars and rightly so. If you aren’t value-selling, then you are giving away precious assets.”**

# Consumer Perceptions of Price and Value(cont')

- ❑ Pricing requires **more than technical expertise.**
- ❑ It requires **creative judgments and awareness of buyers' motivations.**
- ❑ Effective pricing **opens** doors.
- ❑ Marketers must try to look at the consumer's reasons for **choosing** a product and set price according to consumer perceptions of its value.

## **Consumer Perceptions of Price and Value(cont')**

- **Consumers tend to look at the final price and then decide whether they received a good value.**
- For example, two people dining in a restaurant receive their bill and see that it is \$80.
- The diners then decide whether they were **satisfied during the post-purchase evaluation.**
- Rather than going over each item on the menu individually and judging its value, **they judge the entire dining experience against the cost of that experience.**

# General Pricing Approaches

- ❑ The company must consider **competitors' prices** and **other external and internal factors** to find the **best price** between these two extremes. Companies set prices by selecting a general pricing approach that includes one or more of these sets of factors.
- ❑ We look at the following approaches: **the cost based approach** (cost-plus pricing, break-even analysis, and target profit pricing), **the value-based approach** (perceived-value pricing), and **the competition-based approach** (going rate).

# Cost-Based Pricing

- ❑ The simplest pricing method is **cost-plus pricing**, adding a standard **markup** to the cost of the product.
- ❑ **F&B managers** often use the cost-plus method to decide wine prices.
- ❑ For example, a bottle of wine that costs \$14 may sell for \$42, or three times the cost.
- ❑ Cost as a **percentage** of selling price is another commonly used pricing technique in the restaurant industry

# Break-Even Analysis and Target Profit Pricing

- ❑ Another cost-oriented pricing approach is **BE pricing**, in which **the firm tries to determine the price at which it will break even.**
- ❑ Some firms use a variation of **BE pricing** called **target profit pricing**, which targets a certain **ROI.**

# Break-Even Analysis and Target Profit Pricing (cont')



Gvickig, (2010), Break-even Analysis and Target Profit Pricing,  
[http://1.bp.blogspot.com/\\_1uFFV8Qgk8/TF-bHzuUTcl/AAAAAAAAAAc/PDW9cttf7YE/s1600/break+even+point.bmp](http://1.bp.blogspot.com/_1uFFV8Qgk8/TF-bHzuUTcl/AAAAAAAAAAc/PDW9cttf7YE/s1600/break+even+point.bmp)

# Break Even Point Formula

$$\text{Break Even Point} = \frac{\text{Fixed Costs}}{\text{Total Sales Revenue} - \text{Cost to Make Product}} \text{ (Contribution Margin)}$$



Bermanevansretail, (2018), Calculating Your Break-Even Point,  
<https://blog.hubspot.com/hubfs/Picture1-20.png?t=1524593965401>

# Value-Based Pricing

- ❑ Value-based pricing uses the **buyers' perceptions of value, not the seller's cost, as the key to pricing.**
- ❑ Value based pricing means that the marketer cannot design a product and marketing program and then set the price.
- ❑ The company uses the nonprice variables in the marketing mix to build perceived value **in the buyers' minds, setting price to match the perceived value.**

## Value-Based Pricing (cont')

- ❑ Any company using perceived-value pricing must **learn the value in the buyers' minds for different competitive offers.**
- ❑ Sometimes researchers ask consumers how much they **would pay** for each benefit added to the offer.

## Value-Based Pricing (cont')

- ❑ A successful guest price mix depends on careful study of the **behavior profiles of major guest segments**.
- ❑ For most hospitality companies, this begins with a separation of guests **into leisure and business segments**. Sub segmentation of each category may occur, providing greater information about these major guest categories.

## Competition-Based Pricing

- ❑ A strategy of **going-rate pricing** is the establishment of price based largely on those of **competitors**, with less attention paid to costs or demand.
- ❑ The firm might charge **the same, more, or less than its major competitors.**
- ❑ Some firms may charge a bit more or less, but they hold the amount of difference constant.

## Competition-Based Pricing (cont')

- ❑ For example, a limited- service hotel chain may charge \$10 more than Motel 6 in markets where they compete.
- ❑ This form of pricing is quite popular.
- ❑ When elasticity is hard to measure, firms feel that the going price represents the collective wisdom of the industry concerning the price that will yield a fair return.
- ❑ They also feel that holding to the going price will **avoid harmful price wars**

# References

1] Kotler ,.B (2014) Marketing for Hospitality and Tourism Industry, p 314-330, <https://www.pdfdrive.com/marketing-for-hospitality-and-tourism-6th-edition-e178412795.html>

2] Carlos, et al, (2021), Price Strategy, Market Orientation, and Business Performance in the Hotel Industry, [https://www.researchgate.net/publication/348127604 Price Strategy Market Orientation and Business Performance in the Hotel Industry](https://www.researchgate.net/publication/348127604_Price_Strategy_Market_Orientation_and_Business_Performance_in_the_Hotel_Industry), DOI:10.4018/JGIM.2021010105

Thank you!

Next lecture: Pricing strategies

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