

The influence of price on customer's purchase decision

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Abstract. *In modern times, especially with the appearance of the economic crisis, pricing is one of the main activities of each company. Companies should bear in mind that the price is element that surrounds every natural or legal person, depending on what kind of role the person is in, and that it is at all times in contact with their customers. The price is included in each segment of the company. It is not only important when selling a product or service; it is present in every phase of companies' lifetime. Also, it is important to note that the price can be seen as a mean of differentiation, and often for the customers price can be the only reason for buying certain product. Therefore, this paper will show how price influence the purchasing decisions of consumers. The paper is a result of the research established for writing final thesis of undergraduate study.*

Keywords. price, strategy, goals, purchase decision

1 Introduction

Since the price is present in every segment of the company, knowing its characteristics and its monitoring is of crucial importance for the company and for future management. It is necessary to determine the strategy that the company will use and maintain it throughout the business life cycle. And with quality and adequate pricing strategies, goals and politics, the company can greatly affect the business activities.

Hereafter we will explain the concept and characteristics of the price, price policy and why the pricing strategies are needed in the companies' operations. At the end of this paper we will present a results of research conducted for the purpose of writing final thesis, the results will show how respondents react to price changes and how it affects their purchasing decisions.

2 Concept and characteristics of the price

"The idea of the marketing mix and the "4P" (product, price, place and promotion) was presented and elaborated by McCarthy back in 1964." [12, 38] In modern times companies are faced with a changing environment especially because economic opportunities, all over the world, are changing every year. So, companies must make great efforts to keep up with such frequent changes [5, 1350].

Price is the most sensitive element of the market mix and also the only "element that produces income" [8, 665]. However, this element of the marketing mix can be manipulated; so many companies pay a lot of attention to it. Companies can change (increase or decrease) price much easier, while for the other elements of the marketing mix, it is considerably difficult to do the same. Thus, changing the characteristics of the product, the main suppliers of raw materials and products, change of permanent and main buyer, change in distribution channels is significantly more difficult. Therefore changes of other parts of marketing mix are associated with longer period of time. Since the price is directly related to the coverage of initial expenses and the ultimate cost, it directly affects income, which is ultimately converted into profit. Therefore, a small price change can cause a large reaction of consumers and it is important to mention that the reaction can be positive or negative [4]. So, pricing related decisions usually constitute the hardest and most sensitive set of decisions that each company have to make [9, 81] especially if we company takes into account the fact that the price is a key factor in most purchases [6, 467].

Kotler and associates [5, 665] define the price, in the narrower sense, as "the amount of money wanted for some product or service", while price, in the broader sense, is seen as "the sum of all the values that consumers are changing for the benefit of ownership or usage of certain product or service" [8, 665]. It should be noted that the price affects supply and demand of product or service. So, according to that, even a small increase of price can reduce demand for the product, because price represents what the consumer will lose in a transaction they make [6,

468]. Also, price is often considered as a measure of quality which can make the product or service more or less attractive to a potential buyer.

3 Price policies

Price policies and their goals are closely linked. In their interpretation we can't strictly determine what exactly the company must do to be successful. Price is a lengthy term that covers a large number of elements and each company is unique. Therefore, each company chooses pricing policies and strategies that suit them the best especially in this competitive market [11, 159].

Companies can set prices in different ways. In small businesses price is usually determined by the owner. While in big ones, high level managers or administration can determine the price, which usually depends on the goal they want to achieve or the tasks the price must fulfil [7, 433]. Therefore, price policy can be viewed as a philosophy of each individual company. There are three basic philosophies of pricing: pricing of new products, pricing of production mix and price adjustments. Each of these policies has a different impact on other elements of the marketing mix and it can be changed depending on the lifetime phase in which the product or service is.

When the company intends to launch a new product on the market, it must determine which strategy to follow. There are two basic pricing strategies for new products. The company can set the price in order to skim the cream (market-skimming pricing strategy), or to penetrate deeper into the market (marketing penetration pricing strategy) [8, 689]. On one hand, strategy aim of pricing for skimming the cream on the market is to determine the maximum production price which is gradually reduced. While on the other hand, penetration strategy aims to win as many of the market as possible on the basis of low cost of production and sale. [3, 194]

Pricing policy of production mix must take into account that it is the part of entire production mix, so the price has to be summed up. The production mix includes [5]: pricing for the product line, pricing for additional products, pricing for related products, pricing for ancillary products and pricing for product packages. Therefore, the product can be placed in a many different roles, which affects the price change.

In the case when customers initiate a change in demand for a particular product, there is a need to adjust prices due to the new situation in the market. Some strategies for price adjustment are: price discounts and allowances, discriminatory pricing, psychological pricing, promotional pricing, value pricing, geographical pricing, international prices and so alike [8, 693].

4 Price goals

According to price policies, companies must define the goals they want to accomplish in a given period of time. "Thanks to the fact that the price is extremely flexible and suitable for a variety of adjustment" [3, 186], the price goal may be different due to the vision that the company has. "The company that has clearly defined goals will set the price easier. Some examples of common goals are: survivals, current profit maximization, maximize market share and leadership in product quality." [8, 667]

It is important to set goals that are measurable, that are limited by a certain period of time, a goals that can be monitored and compared with those that are achieved. The survival of the company is considered as one of the main goals, especially if there is a great competition in the market and thus the fear of disappearing from the market. On the other hand, maximizing current profit can be very dangerous goal. "In the desire to maximize profits the companies are guided by economic legality, which states that the demand can be managed with different levels of prices." [12, 52] So, companies have two options. To determine the higher price of the product or service than their competitors. Or, if they already have a certain demand for the product or service, to determine a lower price and to expected that the increased of demand will influence higher profit. This raises the question of the companies' future, if the goal is just current profit maximization. With a desire to achieve the higher profits, the management board can make wrong decisions that company in the long-term will not benefit from. The company also can strive to the realization of a bigger market share. Then the company aims to create a habit of consumers using a product or service, provided that they are satisfied with the price of the product. In case a greater market share is grabbed, company creates safety for profit within a certain period of time, and thus the changes in price. But also in today's business a quality of the product is extremely important. So in practice, price of the product is often compared with its quality. Therefore major challenge for the company it to harmonize price and quality. It is possible that the customers, when the prices changes i.e. decrease, will think that the quality of products has decreased also. Of course this may not be the case. There are many certificates that provide quality confirmation. Customers are increasingly aware of the existence of norms and quality standards. Therefore, the companies must take over and use customers' awareness, and provide what the market demands. Norms and quality standards can be companies' advantage over competition [5, 1351]. If customers notice that the company works in their favor, they will be more satisfied with the products of the company. Therefore, the company must try to persuade customers to use quality product permanently and must sell quality, which is featured with a price. It is

necessary to convince the customer to purchase a product or service that is worth exactly the same monetary units. Neither more nor less. Because the price that is set can be a sign of product quality and a lower price can make potential purchase less consequential and vice versa [1, 80]. The most important for the each company is to take into consideration how can each customer behave. And customer behavior can be defined as "customers' actions of purchasing goods and services for household and individual uses in order to satisfy their basic needs, where the individuals are involved in the process of making decision and exchanging money for goods and services" [according to Serirt et al, 2000 in 13, 2081]. Analyzing customer behavior considers investigation the customers' pattern of purchasing, consuming, and using, both at an individual and organizational levels of consumers. And understanding the factors behind consumer choice and behavior has been central to developing marketing strategies and price policies since the birth of modern marketing [2, 50]. In order to comprehend the main pricing elements that influence purchasing of certain product and consuming it is important to examine make a research.

5 Elements affecting the change of price

There are numerous elements that can affect the price; they are divided into internal and external. Internal elements that affect the change of the price are: marketing and financial strategies of each company. External elements are: impact of the consumer and the market, and conditions in which determining the price was decided [3, 187].

In accordance with the decision of the company on execution of the price policy, they make decision on what marketing strategy to use. The company may have a number of different marketing goals that are satisfied through price. They can achieve specific goals, such as "they can set price so low as to prevent entry into the market to other competitors, or set price at competitive levels in order to stabilize the market" [8, 668]. Referring to the goals, the company must define a strategy of marketing mix with all its elements. The price per unit of a product must be in accordance with the other elements, with distribution related to a specific channel, the type of a product, its promotion, ect. Kotler and associates [8, 670] point out: "if the product is positioned around the elements that are not related to prices, then the decision about quality, promotion and distribution will strongly influence the price. If price is a key element in positioning, then the price will strongly affect decisions about other elements of marketing mix." The financial strategy of the company can also affect the price change. In other words, expenses, on which

essentially depends the price itself, are involved in every aspects of business. For example production in progress, distribution channels ect. A cost defining impacts the definition of the final product or service price. "If a company has a higher cost of production and sales than their competitors, they have to seek a higher price or they will make smaller profit, which puts them in a competitive disadvantage." [8, 671] For this reason the company must set up a clear management costs.

Market and demand, as external elements that are affecting the price, are sensitive on the reaction of price changes. "Generally speaking, consumers are most sensitive to the price of the product that is expensive or that they often buy. Normally, demand and price are inversely related: higher the price, lower the demand. In the case of luxury goods, the demand curve is sometimes tilted down." [7, 439] By analyzing the demand, company can explain the behavior and the causes of consumers' behavior in certain situations on the market. Before defining the price, the company must be familiar with the basic law of action of supply and demand in the market. Supply and demand do not depend only on the price; they depend on the numerous elements. Demand depends on: the average income of consumers, the price of substitutes and complements, market size, consumer tastes and preferences, and the special influences. While on the other hand, the offer may depend on: "the production cost which depends on the price of inputs and technological improvements, price of substitutes and complements, the politics of the state and the special influences" [10, 90-91]. Last, but not least, important external element that affects pricing is competition. Given the existence of a growing number of different companies in the market, management must have in mind management of the competition. It is necessary to know their costs and price of products or services in order to determine an appropriate price, which will depend on the goal that company sets. While the pricing can be affected by a numerous elements such as: prosperity or recession, inflation or interest rates, consumers perceptions of price and value of the product ect. [12, 680], their impact is lower and therefore in this work they are not explained in more detail.

6 Research

For the purpose of this work, quantitative descriptive survey was carried out, by examining customers in Croatia. The survey instrument was a questionnaire that has been created in the Google tool for online surveys. The survey was conducted through direct e-mail and social networks in the period from early July to late August 2014. Total number of 65 examinees fully responded to all questions in the questionnaire and statistical analysis has been conducted on their responses. This sample, because of its way of

contacting (through e-mail and social networks) should be viewed as a snowballing sample. The purpose of this research was: to determine the degree of price importance in the purchase, to detect customer reaction to price changes and to identify other elements that influence the purchasing decision. One part of the results obtained in this survey are shown hereafter.

At the beginning it is important to note that the sample is dominated by women with 72.3%. According to the age group young people are dominating. Respondents between 20 and 25 years (86.2% of respondents), while the least represented of the respondents were between 15 and 19 and between 31 and 35 years old (1.5%). The study included 80% of students, 18.5% of employees and 1.5% unemployed.

Furthermore, if we consider the frequency of purchasing of special (shopping) products (clothing, footwear, cosmetics, etc.), it can be pointed out that 41.5% of such purchase is performed once a month, 24.7% of them perform purchase several times a month, 20% of the purchase is done at the end of the season (summer-winter) and 12.3% of them buy special products on weekends. From these results it can be concluded that respondents do not buy special products so often.

When asked how often they look at prices when buying products, 86.2% of respondents said that they often or always look at the price when purchasing special products, while 4.6% of them rarely or don't at all look at the price, and 9.8% of respondents are undecided. On the other hand when it comes to follow up discount prices, 60% of respondents always or frequently follow promotional prices. 20% of respondents rarely or don't at all follow discount prices and also 20% of them neither follows, neither not follow discounts. To them the price is not crucial for the product purchase (Chart 1). Most of respondents (27.7%) follow discounts in catalogs, 24.6% of them follow discounts through the Web site, 20% directly in the store, while 15.4% of respondents follow discounts through social networks. Only 6.2% of them follow discounts verbally (friends, acquaintances) and 6.2% of them through other channels. Of the total number of respondents, 52.3% of them plan or always plan to which amount they will make a purchase, 24.7% of respondents rarely or do not at all plan the amount they will spent, while for 23% of respondents the purchase amount is not important, they nor plan it, nor do not plan it.

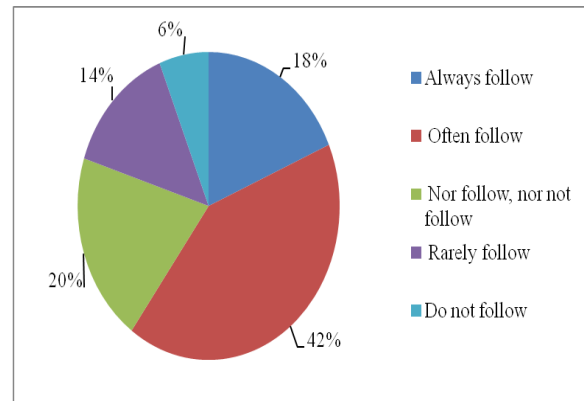


Chart 1. Following of discount when purchasing

When asked what is the most important elements while purchasing, 35.4% of respondents said that the quality is the most important element, 26.2% of respondents said that for them more important while purchasing is immediate need for the product, while only 13.8% consider the products design and 6.2% brand are the most important element while purchasing. Only 17% of respondents consider the price to be the most important element when purchasing. What puts the price on third place of most important elements that affects these respondents when purchasing products (Chart 2). But on the other hand, according to the given results, even 61.5% of respondents remain loyal to the company if the prices of the product changes.

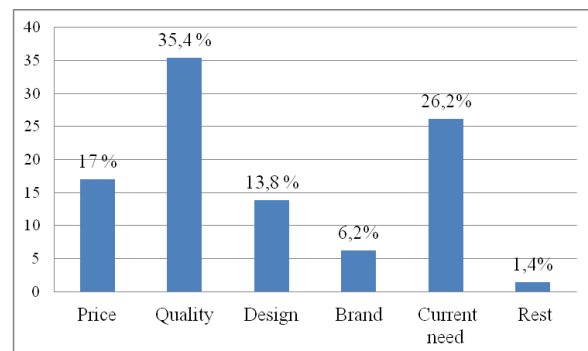


Chart 2. Elements that influence customers' purchase decision

When respondents were asked whether companies policy (way and working conditions) affects their purchasing decision, 23.1% of respondents said that companies policies often or always affects their decision to buy, 30.8% of respondents are undecided, they neither agree nor disagree with the statement that companies policy affects their purchasing decisions. While 45.5% of respondents said that the companies policy of individual companies rarely or do not at all affect their purchasing decisions.

On the basis of this study it can be concluded that people usually perform purchase once a month and that the purchase is usually planned. Price is only the

third most important element when making purchasing decisions, right behind the product quality and the need for product. Also it is important to point out that the changing of price usually does not affect the replacement of product with a substitute, and that the respondents are mostly loyal to the product, to brand, they normally buy.

This research has some limitations and the results of this paper must be interpreted in the context of its limitations. Primarily in the fact that it is based on a research conducted for a purpose of writing a final thesis of undergraduate study so this paper does not contain all the elements that the price affect on purchase decision each of the respondents. Also, limitation can be the fact that the research was based on mainly student population, and that we had only 65 examinees that fully responded to all the questions in the questionnaire and that statistical analysis has been conducted on that small number of responses. So, the findings may not be generalizable to situation beyond that specified group of respondents. Future studies could take into consideration all the price elements that influence on customer's purchase decision, wider group of respondents with different demographic characteristics and based on that include more statistical methods.

7 Conclusion

Price as an element of the marketing mix requires special attention. One of the reasons is that the price, unlike other marketing elements, affects on the income of consumers. The company as a legal entity must determine the goals that are to be achieved before determining the price. Taking into account the goals set by each company, the next upgrade is the pricing policy. Each policy has its advantages and disadvantages, and with the combination of different policies and knowledge of the current market situation, the company can make profit.

Although, traditionally customer's purchase decision mostly depends on price [6, 81], the conducted research has shown how important element for purchasing decision is price and how it can affect the company. The results also show how non-price elements have been gaining significance in purchasing decision over the past decades and that customers always follow the activities of company related to price and that they will continue to follow them. Therefore, companies must always keep in mind that consumers are the ones who should be in the center of their attention and that should always bear in mind their wishes, needs and preferences, but also their possibilities.

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