**Does discount and cheap pricing work?**

**Abstract:** In this essay it is argued that the pricing of any product or service is a very difficult issue and should be based on good natural and social sciences. Giving a discount although may appear attractive, it not only unsustainable over the long term it is unethical. This essay is based on experience gained in the UK as well as in Sri Lanka.

**Selling and buying:** When we sell or buy products of services, we in general do that with the intension of profiting from those activities. Not all benefits are tangible, financial or material benefits, some is mental satisfaction to see the disadvantaged people benefiting from our donation, and the religious leaders conducting their business which is preaching, believing they will be rewarded in the afterlife, if there is one.

However, most of our day-to-day activities are based on obtaining some financial or material gain. There is also an established view that people will not respect and value anything that is given free or cheaply. Therefore, services and goods have to be priced correctly. The question is, how to price it correctly.

**Pricing**: Pricing has different dimensions, and how these affect the final price is discussed in this section. The key dimensions are, financial or accounting, customers’ needs and availability of the product or services, and also moral and ethical dimensions.

Pricing with respect to accounting, which is the prime dimension should take into account raw material costs, labour costs, fixed cost and the profitability of the activity or investment. If it is a private company and our objectives are growth and return on investment (ROI) then the profit margin has to be determined to make sure that the ROI is equal or above the interest rate which can be secured from a high-street bank.

The second dimension which is also important but not as much as the first dimension, is the need and availability of the products and services we are proposing to market. If there are no competitors, then the supplier theoretically can set the price as high as they like and the sales quantity will be determined by the demand and affordability. The achievable sales will come to an equilibrium to satisfy the supply and demand curves explained in all economic books. This is best explained by the fact that it is possible to buy an air ticket from London to Paris for as little as £15/= or as much as £185/= flying in a first-class cabin. The end result is that both passengers are transported from London to Paris roughly in the same time but the luxury and comforts are different.

The third dimension which is not discussed in many books are the moral and ethical dimensions. Given that there is a need and as a seller or a service provider, should they make as much profit as possible capitalising the needs of the buyer? The typical example was the people who smuggled petrol, parts for machines, and similar things to the areas where such items were banned during the civil war in Sri Lanka. There were a number of people who took items and made 1,000% profit by exploiting the needs of the people. The question is whether this is ethical or not. It can be argued either way as the smugglers risked their lives, so they need to be paid for their work.

Therefore, when it comes to pricing there is a basic dimension which is the total production cost and then the other two dimensions which are demand and ethical and moral issues.

The key issue to be addressed is whether discounting and cheap pricing works? The answer has to be no, because if it did, then we should all be able to go to Cargills Food City and negotiate their prices and ask for discount. The answer is no but at the same time we can go to the market or corner shop and ask for discounts and get them. Furthermore, the items in Cargills Food City are more expensive than in any other local shops but people still purchase items from Cargills Food City. Another example is the trains from the Jaffna to Colombo have 1st Class, 2nd Class and 3rd Class carriages, and the ticket prices are also in that order, but the availability of tickets is in the reverse. The tickets for 1st Class is always booked first and then the 2nd Class and finally tickets are always available for 3rd Class. This and the business class air tickets costs indicate that although price is a factor it is not the key factor.

**Does price discount work?** It does not work for the following reasons. First of all, if we are prepared to give a discount then our initial price was too high, and we were trying to make an excessive profit. By agreeing to a discount, we are admitting that we tried to cheat the customer first by trying a higher price and attempted to extract as much money from you as possible, but they managed to see through us to reduce our price. The seller is also making a statement “I managed to cheat all those people who paid the asking price”. It does not matter how much the petrol price is increased people still use vehicles.

Another point is, even after giving a discount, the seller is making a profit. No seller is going to agree a sale at a loss. Therefore, the sellers will also be grinning in his mind that they still managed to get a profit after tempting the buyer with a small discount.

The even worse, both parties will feel sad after agreeing a discount for the following reasons. The buyers will feel that had they tried a bit harder, they could have secured a better deal. The sellers will be unhappy with the deal because they will feel they have given too much discount. Once the concept of discount is agreed, both parties will not feel happy with the deal as they will feel they could have got a better one.

Another major negotiation technique used by big companies and contractors is bulk buying. It is simple mathematics which shows that if we sell 100 units at £10/= profit per unit, we will get a total profit of £1,000/=. If we can sell 1,000 units with £1/= per unit we can get £1,000/= profit. Therefore, even if we give 50% discount for bulk buying say for 1,000 units, then we can make 1,000 x £5 = £5,000/=. This is very attractive. Let us look at the moral and ethical aspects of these deals.

A contractor who has a need for 1,000 units drives in a flashy car or a pickup truck and says I am a contractor, and I can buy 1,000 units each year so give me 50% discount. When the seller looks at the quantity it is very attractive. If he agrees, he sells the units at 50% but as before, both parties will be unhappy as they could have obtained a better deal. Then a widow comes with three school aged children and counts her money in her purse and says I can only purchase 2 items and the seller says, ‘no discount’, the widow has to pay the full amount. Where is the morality and ethics of the salesperson?

Another scenario is, the contractor buys 1,000 units at 50% discount and resells them with 40% discount of the sellers’ price then the contractor is “steeling” the business from the producer. This is a difficult concept to follow. This is the reason why companies introduced the concept of Recommended Retail Price (RRP) which does not work. Even if we go to the corner shops in Sri Lanka, they are happy to show the RRP and say that they can sell it at a price a couple of rupees less than the RRP.

In the early 70s there was a price war between Tesco the supermarket chain and Heinz baked beans. Tesco managed to purchase Heinz baked beans at a considerably low price and started to sell them below the RRP. The local small grocery shop keepers complained to Heinz. Heinz then formally instructed Tesco not to sell their baked beans below their RRP. Tesco was forced to sell them at the RRP. Teso retaliated by selling them at the RRP and put a big notice in every Tesco outlets and on the Heinz bean shelf saying we (Tesco) wanted to sell these cans of beans below the RRP, but Heinz forced us to sell them at a higher price. Heinz had no option but to backdown and allowed Tesco to sell whatever price they choose. The local corner shops have to stop selling Heinz baked beans.

The author of this article was the business manager responsible for selling consultancy service in the UK, where he made a firm statement that no discount of any form would be given for the simple reason that if he agrees to give a discount then his original price was wrong, and he tried to extract as much profit as possible from his customers. He made the statement that he could not live with that kind of behaviour which was to “try and get as much as he could from his customers”. Customers really appreciated it and accepted the fact and his prices.

The same concept was introduced at InnoBlocks in Puthukkudiyiruppu where all staff who are responsible for selling CSEB blocks initially felt they should be able to give some discount now feel that trying to set the price high and giving a price discount is the wrong thing to do.

Finally, the concept of Sri Lankan government departments to go for the lowest bidder in any tender is fundamentally flawed. This is because most contractors will submit a very low price which they all know is not sufficient, but they will appoint a good Quantity Surveyor and a good site project manager who will start adding additional items and delays and push the project cost at least twice the original contract price. If the contractor is incapable of doing it and ends up with a price twice as much as the quotation, the contractor is not worth appointing. An alternative way which is practiced in some companies in the UK, is to ask the contractors to submit the proposals in two parts, the technical and the commercial parts. The contractor who submitted technically superior tender will be selected, and the price and the scope of work will then negotiate the contract price.

Therefore, setting the sales price artificially high trying to negotiate the appropriate discount is not a smart philosophy to follow. Price is not a major factor in selection criteria because if it is then Cargills Food City will have to be closed.

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