BUSINESS STUDIES

GRADE 11

TERM TWO

CHAPTER TEN

BUSINESS OPERATIONS

MARKETING ACTIVITIES: PRICING AND DISTRIBUTION POLICY

TABLE OF CONTENTS

This chapter consists of 10 pages

CONTENT DETAILS FOR TEACHING, LEARNING AND ASSESSMENT PURPOSES

MARKETING ACTIVITIES: PRICING AND DISTRIBUTION POLICIES

Learners must be able to:

PRICING POLICY

- Define/Explain the meaning of price
- Discuss/Explain the importance of pricing.
- Outline/Mention/Explain/Discuss the following pricing techniques e.g.:
  - Cost-based/orientated pricing
  - Mark-up pricing
  - Customer/target based pricing
  - Competition based/orientation pricing
  - Promotional pricing
  - Penetration pricing
  - Psychological pricing
  - Bait pricing
  - Skimming prices
- Identify the above-mentioned pricing techniques from given scenarios/statements. Quote from the scenario to support your answer.
- Outline/Mention/Explain/Discuss factors that influence pricing.
- Identify these factors from given scenarios/
- statements. Quote from the scenario to support your answer.

DISTRIBUTION POLICY

- Define/Explain the meaning of distribution.
- Outline/Discuss/Explain the channels of distribution.
- Differentiate/Distinguish between direct and indirect channel of distribution.
- Explain the meaning of intermediaries
- Outline/Mention different types of intermediaries.
- Explain the role of intermediaries in the distribution process.
- Draw the channel of distribution.
- Briefly explain the reasons why manufactures may prefer to make use of direct or indirect distribution methods.

Terms and Definitions

TERM	DEFINITION
Costs	An amount that must be paid or spent to buy or obtain something.
Mark-up	The amount added to the cost price of goods to cover overheads and profit.
Bait	It is when someone deliberately acts in a way to elicit an emotional response from another person.
Wholesalers	They are large-scale traders who operate as intermediaries between manufacturers and retailers.
Retailers	They are smaller-scale traders that operate as intermediaries between wholesalers and consumers.
Intermediary	A person/business that acts as a link between people and businesses to bring about the sale.
Substitutes	A person or an object acting in place of another.
Websites	A set of related web pages located under a single domain name.
Agents	A person who organises transactions between two parties.
A broker	A person who buys and sells goods for others
Logistics	The activity of organising the movement of goods, equipment, accommodation, etc.
Profit margin	The portion of the selling price that is not allocated to input costs/overheads and contributes to the gross profit margin of the business.
Cash and carry	Wholesaler purchase where payment is made in full by the customer.
Direct distribution	Exchange of products/services between the producer and the consumer
Indirect distribution	A distribution channel with at least one intermediary between the producer and consumer

MARKETING ACTIVITIES (PRICING & DISTRIBUTION POLICIES)

1 The pricing policy

1.1 The meaning of price

- The price of a product refers to the amount of money that must be paid by the buyer to experience the benefits of the product.
- The pricing policy specifies what and how the business will work out the pricing of its product.

1.2 The importance of pricing

- The pricing process needs to consider flexibility/discount/territory/life cycle status/allowance.
- Pricing affects the number of products that an enterprise is able to sell, which in turn, affects profitability.
- The price of a product can influence the consumers' attitude towards the product or the brand.
- If the is believed to be too high, fewer consumers may buy the product.
- If the price is too low, consumers may perceive the good as being of poor quality.
- The pricing policy should explain when and to whom discounts will be granted.
- The price of a product must make provision for transport costs.
- The price of a product must make provision for VAT.
- Low sales result in stockpiles of unsold product that have to be stored and not repaying the cost of manufacturing that product.

2.3 Pricing techniques

2.3.1 Cost-based/orientated pricing

- Involves setting the price of a product based directly on its cost.
- The business calculates the cost of producing one unit of the product, called unit cost, and then adds a standard mark-up to obtain the price.
- The costs of production and supply are calculated and a suitable profit margin is added to determine the selling price.

2.3.2 Mark-up pricing

- It is calculated as a percentage.
- This percentage is calculated from the cost per unit.
- Example will include a sandwich-making a business may calculate that the cost of producing a sandwich is R10 and decide on a mark-up of 100%, setting the price at R20.

2.3.3 Customer/target based pricing

- It is when companies set certain targets to achieve.
- Based on what the business believes customers are prepared to pay.
- The perception of the product it wants to create in the customers' mind.

2.3.4 Competition based/orientation pricing

- Sets its price based on what competitors are charging customers.
- This approach is also called going rate pricing or competitive pricing.
- The more competition in the market, the lower prices are likely to be.
- If the price is set at a higher level than of competitors, consumers must be convinced that the good is better in terms of quality and usefulness.

2.3.5 Promotional pricing

- Businesses offer sales or special offers to attract customers.
- It is used when the price is lowered for a short period of time.
- At certain times of the year, end of season ranges or old stock may be sold off at discount prices.
- Example include special offers/discounts that are valid for a limited period of time/"Buy one, Get one free" type promotions.

2.3.6 Penetration pricing

- Products are sold at very low prices to attract consumers when the product is introduced to the market.
- The aim is to convince the customers to buy a product.
- As soon as the introductory offer is over, the price is increased.
- It is often used for new products and it is not a profitable long-term marketing strategy.

2.3.7 Psychological pricing

- This strategy is used when the business wants the consumer to respond on emotional basis rather than a rational one.
- It is used to give an impression that an item is cheaper than it really is.
- A CD player is priced at R699 instead of R700.
- Consumer mentally place the item in the R600 rather than the R700 price range.

2.3.8 Bait pricing

- Prices are usually set lower than the items cost price to attract customers.
- It is used to attract customers into a shop to buy the product and other items.

2.3.9 Price skimming

- Prices attached to a new innovative product that is considered unique and prestigious.
- Higher prices are charged to test the demand.
- There are consumers who are prepared to pay higher prices, because such inventions have prestige value.
- As the product gains popularity, the price of the product is gradually reduced.
- Price skimming can be successful and profitable in the short term

2.4 Factors that influence pricing

2.4.1 Input costs

- The higher the input costs, the higher the final price. An increase in labour or transportation could increase the final price.

2.4.2 Demand for the product

- The higher the demand, the higher the production volume, the lower the input costs, the lower the final price.

2.4.3 Target market

- Income level of the target market.

2.4.4 Type of product

- Luxury products can be priced higher.

2.4.5 Pricing technique used to determine the price.

- Promotional pricing could be lower than demand oriented pricing.

2.4.6 Competitive and substitute products

- If there are similar products that could replace a product, a high price may result in loss of sales to the substitute.
- If the price and demand of complement good increases, the other product may increase at the same rate.e.g. prices of computers and keyboards may increase at the same time.

2.4.7 The economic climate and availability of goods and services

- When there is a shortage of a certain product, people are prepared to pay more for it.

2.4.8 Forms of markets

- The following forms of markets will affect the price chosen

Perfect competition	• There are many buyers and sellers • Products are similar and there are many substitutes' products. • Example: Shares being traded on the JSE
Monopolistic competition	• There are many suppliers/sellers • Each supplier has his/her own brand of a particular product • Example: Car manufactures/dealers e.g. Toyota/Nissan/Ford etc.
Oligopoly	• Only a few suppliers/sellers control the prices of products. • Product are homogenous/same • Example: MTN, Vodacom /Cell C
Monopoly	• Only one supplier/seller controls prices and products • Profit margins are usually higher because consumers do not have any alternative • Example: Eskom

3 THE DISTRIBUTION POLICY

3.1 The meaning of distribution

- Every business needs to have a distribution policy so that it knows how and where products need to be distributed.
- Distribution is about how the business gets its products to its customers.
- Once products have been developed and priced, they need to be made available to consumers at the right place and at the right time.
- Products need to be distributed from the place where they were manufactured to the market place.

3.2 The meaning of channel of distribution

3 Distribution channel is the path which the product is moved from the producer to the consumer.

- It is important that the channel is the most effective and cost efficient for the product and reaches the target market.
- A distribution channel is made up of many businesses that help move the product from the producer to the final user/consumer.
- It starts with the producer and ends with the final consumer.
- The main aim of the distribution function is to ensure that the right product is available at the right time.

4 There are three kinds of participants in a distribution channel :
  - The service provider
  - Intermediaries
  - Customers

3.3 Meaning of intermediaries

- All the people that fall into the distribution process between the producer and the consumer.
- They are middlemen and act as negotiators and mediators between the producer and the consumer.
- Intermediaries can be wholesalers, retailers, agents and brokers.
- They are responsible for the transportation, storage and delivery of the goods and services.
- The organisations involved in the distribution channel are known as intermediaries.

3.3.1 Different types of intermediaries

- Wholesalers primarily sell goods to retailers.
- Retailers market directly to the final consumer.
- Agents sell products on behalf of manufactures for a commission.
- Brokers is a person who buys and sells goods for others.

3.3.2 The role of intermediaries in the distribution process.

- Finding and locating buyers on behalf of the producer.
- Help in promoting the product.
- Intermediaries are specialists in selling, so the producer may be able to reach a wider audience.
- They can achieve greater sales by using intermediaries.
- The producer may not have the expertise or resources necessary to sell directly to the public.
- The intermediary may be able to provide more efficient distribution logistics, for e.g. transporting the product to various points of sale.
- Overall distribution costs may be lower using an intermediary than if the business undertook distribution itself, even when the intermediary’s commission is taken into account.

3.4 The different types of distribution channels

Manufacturer/Producer-consumer

- This is the shortest channel as the producer sells directly to the consumer.
- It is usually found in the public sector

Manufacturer/Producer→retailer→consumer

- The producer sells goods to the consumer using the retailer.
- This is a single distribution channel and it is aimed at selling to large scale retailers

Manufacturer/Producer→wholesaler→retailer→consumer

- This is called a traditional distribution channel, the consumer buys from the shop, which buys from a wholesaler, which in turn gets its stock in bulk from the manufacturer.
- Consumer products such as maize meal are sold by the producers to the wholesalers, who again sell to retailers then to the consumers.
- This distribution channel is usually used in rural areas.

Manufacturer/Producer→wholesaler→retailer

- This is where the wholesaler buys from the producer and sells directly to retailers.
- The cash and carry wholesaler sells directly to retailers for consumption.

Manufacturer/Producer→agent→wholesaler→ retailer→ consumer

- Agents often connect the manufacturer to the wholesaler or retailer.
- The more intermediaries there are in a distribution channel the more consumers can be reached.
- Especially consumers in the rural areas who will also have access to goods.

3.5 Differences between direct and indirect channel of distribution

Direct channel of distribution	Indirect channel of distribution
• Carry all the risks.	• Risks are shifted to intermediaries during the distribution of the product to end user
• Involves the producer and the consumer	• There are middlemen between the producer and the consumer
• The wholesaler and the retailer are cut from the process	• The wholesalers and retailers act as negotiators between the producer and consumer.
• Marketing and selling of products to the customers without involving the middleman.	• Specialised agents deal with customers
• Full control over the product and marketing.	• Very little feedback from customers.
• Better end user price as no intermediaries costs	• Transportation and storage is taken care of by intermediaries.
• Provides immediate feedback	• Manufactures make use of middlemen such as wholesalers/agents/brokers/retailers.
• Needs more specialised employees' who are trained.	• The manufacture is not knowledgeable about the distribution of the product
• Better end user price as no intermediary costs.	• Products may be expensive as costs are intermediary costs are added.

3.6 Reasons why manufacturers may prefer to make use of direct or indirect distribution methods.

3.6.1 Reasons why manufacturers may prefer to make use of the direct distribution method

- Manufacturers have control over the product and marketing.
- They achieve better end-user price as there are no intermediary costs.
- The business does not need to share its profit margin with intermediaries.
- Products become very expensive once all the intermediaries have added their own mark-ups.
- There is direct contact with target market for feedback and improvements.
- Sales staff provide customer information for future market research.
- Selling through the internet allows smaller businesses to market their products all over the world.
- Businesses websites can serve as both a distribution method and a promotion method.
- Well trained sales staff are able to promote products effectively and establish good relationships with customers.
- Suitable intermediaries may not be available/Intermediaries may not be willing to sell the particular product on behalf of the manufacturer.

3.6.2 Reasons why manufacturers may prefer to make use of the indirect distribution method

- Specialised agents deal with customers.
- Transportation and storage is taken care of by intermediaries.
- There is no need to hire specialised staff to do sales complains.
- They do not have to deal with customer complaints.
- They enjoy the benefits of bulk orders from wholesalers.
- Better market coverage is achieved.
- Intermediaries understand how the market operates.
- Consumers are often spread across the country, distribution needs to be widespread as well.
- Direct distribution requires a large investment in advertising
- Intermediaries sometimes provide credit to consumers, which will help attract more consumers.