

# Set Prices Based on Customers' Buying Patterns

by Joseph Lizo

There are many schools of thought regarding how businesses should set their pricing and just as many ways of analyzing your business' pricing models. From basing prices in relation to competition, ensuring that prices cover all costs to include a component for profit to a purely market based school of thought where prices are set on what your market and customers are willing to bear.

Regardless of your school of thought, I want to add another wrinkle to the pricing dilemma. Clayton M. Christensen and others like him have poured countless hours of research and analysis into the buying decisions of customers. Regardless of where your prices fall, the bottom line is to entice customers to part with their hard earned money, thus understanding their buying behaviors.

Based on a buying hierarchy model first outlined by Windermere Associates, most customers follow a four phase buying pattern, with only the last phase being based on price.

These phases are as follows:

1. **Functionality** – Where a product or service meets a certain need or does a certain thing that cannot be accomplished in any other manner.
2. **Reliability** – When two or more competitors offer similar products that have the same functionality, consumers turn to the competitor whose product offers the better reliability.
3. **Convenience** – When competitors have products or services that offer the same functionality and the same relative reliability, consumers turn to convenience – those products that are the most convenient to use and the companies that are the most convenient to work with.
4. **Lastly, price** – When competitors all have similar products or services that offer all the attributes above in very similar manners, then, the product or service essentially becomes a commodity and at that point must compete on price (following the schools of thought outlined above).

Thus, the first question that any entrepreneur should consider when setting prices for their offerings is: "Is this product or service already a commodity?"

If it is not, then the business should be able to compete on one of the four phases listed above, without much regard to price.

A great example of this is Apple's iPhone. When this smart phone device first entered the cell phone / PDA market – it was extremely unique in its functionality and thus its price was set

astoundingly high. When it was first introduced, following the phases of the buying hierarchy, this phone was marketed based on its functionality.

As other phone manufacturers began duplicating the iPhone's functions with their own devices, the marketing focus shifted to reliability – not just based on the smart device itself, but also the reliability of the network on which it would be employed. Just think about the Verizon Wireless commercials.

As time passed again marketing efforts shifted once more, this time to both the convenience of the device (easier to use, easier to type on, easier to text or surf, running multiple apps, etc.) and the convenience of the network – customers not having to switch networks (and incur the fees of doing so) to get a compatible device with the service they already know and use.

And now we are beginning to enter the second generation of these smart phones. Many of the first generation devices are very similar in functionality and reliability and are offered on nearly every network, thus they are becoming commodity-like in nature. Therefore, Apple is now on the verge of introducing its next generation phone (hopefully with functionality that no other smart device has). But in the meantime, prices of current smart devices have fallen dramatically and are finally beginning to compete solely on price. Today, a cell phone consumer can easily purchase a first generation iPhone for well under \$100.

**Bottom line: know where your products or services fit within this buying hierarchy. Doing so may save you, the entrepreneur, countless hours of worry about prices – especially if you and your business do not yet have to compete on price alone.** The idea here is not to purely focus just on pricing but to how your business can market its offering using the four phases of the buying hierarchy and actual customer buying behavior.

Joseph Lizio holds an MBA in Finance and Entrepreneurship and has a strong commercial lending background. In his current venture, Mr. Lizio is the founder of [www.businessmoneytoday.com](http://www.businessmoneytoday.com) - a site designed to help business owners find and obtain capital to grow their businesses.