

11.23: Discounting Strategies

Learning Objectives

- Explain the methods businesses use for discounts and allowances



In addition to deciding about the base price of products and services, marketing managers must also set policies regarding the use of discounts and allowances. There are many different types of price reductions—each designed to accomplish a specific purpose. The major types are described below.

Quantity discounts are reductions in base price given as the result of a buyer purchasing some predetermined quantity of merchandise. In a B2B environment, a noncumulative quantity discount applies to each purchase and is intended to encourage buyers to make larger purchases. This means that the buyer holds the excess merchandise until it is used, possibly cutting the inventory cost of the seller and preventing the buyer from switching to a competitor at least until the stock is used.

A cumulative quantity discount applies to the total bought over a period of time. The buyer adds to the potential discount with each additional purchase. Such a policy helps to build repeat purchases. Both Home Depot and Lowe's offer a contractor discount to customers who buy more than \$5,000 worth of goods. Home Depot has a tiered discount for painters, who can save as much as 20 percent off of retail once they spend \$7,500.^[1]

B2C examples of quantity discounts are everywhere: “two-fors” (buy one for \$2.00 or buy two for \$3.00), “BOGO” (Buy One Get One free), etc. There are as many quantity discount deals as there are products to price.

Seasonal discounts are price reductions given for out-of-season merchandise—snowmobiles discounted during the summer, for example. The intention of such discounts is to spread demand over the year, which can allow fuller use of production facilities and improved cash flow during the year.

Seasonal discounts are not always straightforward. It seems logical that gas grills are discounted in September when the summer grilling season is over, and hot tubs are discounted in January when the weather is bad and consumers spend less freely. However, the biggest discounts on large-screen televisions are offered during the weeks before the Super Bowl when demand is greatest. This strategy aims to drive impulse purchases of the large-ticket item, rather than spurring sales during the off-season.

Cash discounts are reductions on base price given to customers for paying cash or within some short time period. For example, a 2 percent discount on bills paid within 10 days is a cash discount. The purpose is generally to accelerate the cash flow of the organization and to reduce transaction costs.

Generally cash discounts are offered in a B2B transaction where the buyer is negotiating a range of pricing terms, including payment terms. You can imagine that if you offered to pay cash immediately instead of using a credit card at a department store, you wouldn't receive a discount.

Trade discounts are price reductions given to middlemen (e.g., wholesalers, industrial distributors, retailers) to encourage them to stock and give preferred treatment to an organization's products. For example, a consumer goods company might give a retailer a 20 percent discount to place a larger order for soap. Such a discount might also be used to gain shelf space or a preferred position in the store.

Calico Corners offers a 15 percent discount on fabrics to interior designers who are creating designs or products for their customers. They have paired this with a quantity-discounts program that offers gift certificates for buyers who purchase more than \$10,000 in a year.

Personal allowances are similar strategies aimed at middlemen. Their purpose is to encourage middlemen to aggressively promote the organization's products. For example, a furniture manufacturer may offer to pay some specified amount toward a retailer's advertising expenses if the retailer agrees to include the manufacturer's brand name in the ads.

Some manufacturers or wholesalers also give retailers prize money called "spiffs," which can be passed on to the retailer's sales clerks as a reward for aggressively selling certain items. This is especially common in the electronics and clothing industries, where spiffs are used primarily with new products, slow movers, or high-margin items.

When employees in electronics stores recommend a specific brand or product to a buyer they may receive compensation from the manufacturer on top of their wages and commissions from the store.

Trade-in allowances also reduce the base price of a product or service. These are often used to help the seller negotiate the best price with a buyer. The trade-in may, of course, be of value if it can be resold. Accepting trade-ins is necessary in marketing many types of products. A construction company with a used grader worth \$70,000 probably wouldn't buy a new model from an equipment company that did not accept trade-ins, particularly when other companies do accept them.

Price bundling is a very popular pricing strategy. The marketer groups similar or complementary products and charges a total price that is lower than if they were sold separately. Comcast and Direct TV both follow this strategy by combining different products and services for a set price. Similarly, Microsoft bundles Microsoft Word, Excel, Powerpoint, OneNote, and Outlook in the Microsoft Office Suite. The underlying assumption of this pricing strategy is that the increased sales generated will more than compensate for a lower profit margin. It may also be a way of selling a less popular product—like Microsoft OneNote—by combining it with popular ones. Industries such as financial services, telecommunications, and software companies make very effective use of this strategy.

? Practice Question

<https://assessments.lumenlearning.co...essments/14509>

1. Home Depot. "Pro Loyalty Program." Pro Xtra. Accessed June 25, 2019. http://www.homedepot.com/c/Pro_Xtra. ←

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