

How Pricing Affects Your Brain

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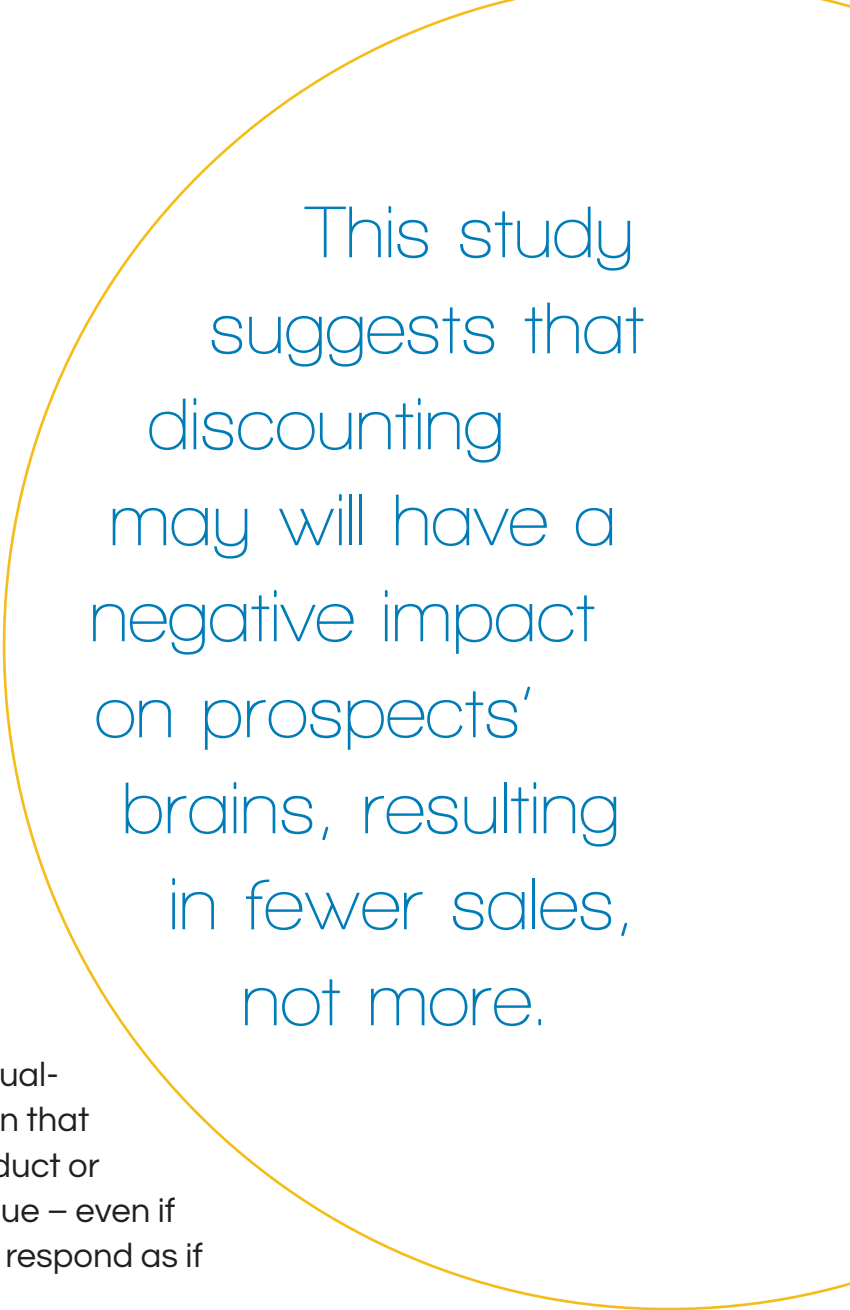
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How Pricing Affects Your Brain

It's not just marketing and perceptions. Pricing affects the brain.

"We have known for a long time that people's perceptions are affected by marketing, but now we know that the brain itself is modulated by price," said Baba Shiv, a professor at the Stanford Graduate School of Business, in reference to a recent study. Although many studies have looked at how marketing affects behavior, this is the first to show that it has a direct effect on your brain.

In the study, while the subjects' brain activity was being monitored, they were given wine to taste. Some were told the wine was very expensive and



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some were told it was inexpensive – but it was exactly the same wine tasted by all. The monitored brain activity of the subjects who were told the wine was expensive showed significant increases in the part of the brain that registers pleasure: the medial orbitofrontal cortex. The subjects who were told the wine was inexpensive did not exhibit the same response.

This study shows that perceptions of quality trigger activity in the part of the brain that registers pleasure. Conversely, if a product or service is perceived as being of low value – even if it really is of high value – your brain will respond as if it was of low value.

Many business owners are tempted to discount their prices in order to increase sales. This study suggests that if discounting causes the product or service to be perceived as less valuable, it will have a negative impact on the prospects' brains, which will result in fewer sales, not more.

In addition, keep in mind that discounting damages your profit margin to a greater degree than the

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amount of the discount. For example, say your profit margin is 20 percent and you discount your price by 10 percent. You have actually reduced your profit margin by a huge 50 percent! (Discounts are usually applied to the gross price, not to the net profit, so a 10 percent discount shaves half off a 20 percent profit margin.)

What if, instead of discounting, you increased your prices by 10 percent? Would prospects consider your product or service to be more valuable? If so, their brains will respond positively, according to this study.

Sure, you might lose a few customers if you increase your prices, but remember, you can often greatly increase your profit margin by just a 10 percent increase in price. A 10 percent price increase would boost a 20 percent profit margin to 30 percent, which actually results in 50 percent increase in profit! So even if you did lose a few customers by increasing your prices, you could well end up with more net profit overall, due to the increased profit margin. Additionally, your customers will experience more pleasure because they perceive an increase in value – and

happy customers are usually repeat customers.

According to Professor Shiv, "Marketers are now going to think twice about reducing the price. If an experience is pleasurable, the brain will use it to help guide future choices."

I strongly encourage you to think twice before giving in to the temptation to discount your prices in an attempt to increase sales. Because of the way our brains respond to pricing, increasing your prices may well be a better way to increase your sales.

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