

Knocking \$1 off the price of a home may yield thousands in return

by Dina ElBoghdady

We've all seen items advertised for just a tad less than the nearest round number — \$9.99 instead of \$10. Many of us would like to think we're too savvy to let that one-cent difference influence our buying decision. But research shows, over and over, that it does. This "just below" strategy (also known as "charm pricing") dates back at least 100 years, and its use is widespread.

Surprisingly, houses — the biggest purchase any of us makes — are no exception. A study published in August in the *Journal of Real Estate Finance and Economics* found that sellers who use the "just below" pricing strategy get more money for their homes than those who don't.

In fact, they get, on average, almost 2 percent more, which is quite a bit on a house worth a few hundred thousand dollars.

"People have these psychological price barriers," said Michael Seiler, the study's co-author and a real estate professor at the College of William and Mary in Williamsburg, Virginia. "They're artificial, and they're a bit arbitrary. But they do matter."

The study examined 372,074 home sales that took place from January 1993 through September 2011 in the Hampton Roads region of southeast Virginia and identified pricing strategies.

It found that 45 percent of sellers set the asking price using the "just below" method (maybe \$199,900). An additional 31 percent asked for a round number that was close to what the sellers viewed as the fair market value (such as \$200,000). And 24 percent listed their homes for a precise price (such as \$200,347).

All three strategies have strengths and weaknesses, according to Seiler and his co-author, Eli Beracha, an assistant professor at Florida International University.

Given that many buyers search for homes on the Internet, the "round pricing"

method may be the best at attracting the most eyeballs. A \$200,000 home will show up in the searches of buyers looking for homes in the \$150,000-to-\$200,000 price range, as well as for those looking in the \$200,000-to-\$250,000 range.

But round numbers may seem like nothing more than a ballpark figure. "They signal that the seller doesn't really know what the value is," Seiler said.

A precise price might grab a buyer's attention and cause the person to pause. Buyers are more likely to assume that such prices more accurately reflect a property's value. But there's no evidence to suggest that the precision motivates buyers to pay higher prices than any other strategy.

It turns out, however, that the "just below" method was the most advantageous. The researchers built a model to determine what the true value of each home was based on its characteristics. They then compared that value to the list price. They found that sellers who used the "just below" method put a far higher price tag on their homes than the other sellers — about 5 percent above where it should have been compared with roughly 3 percent in the two other groups.

Yet the just-below sellers still attracted plenty of buyers. It seems that just-below pricing on products big and small signals a bargain in our minds, especially if the price ends with the digit 9. It's as if consumers perceive they're getting something back from the higher round number, as one study put it.

Some of this has to do with the way written information is stored. The brain starts to record numbers even before the entire price is read. The most valuable digits are the first ones. With six-figure home prices, buyers don't register much past the third digit — the thousands number, Seiler said. The numbers to the right are less psychologically meaningful, and the brain doesn't strain to remember them.

Buyers then underestimate the price.

The left-most digit is especially important, Seiler said. When a home is priced at \$199,900 instead of \$200,000, buyers tend to remember the "1" rather than the "2." That effect fades when the second or third digit is changed, even if the change lowers the price by the same amount.

Even when buyers read the whole price, the part of the brain that starts to record the numbers before that entire price is read is the same part that generates feelings and emotions, said Robert Schindler, a marketing professor at Rutgers University at Camden.

"A lower left-most digit makes a price feel lower, even if one knows it's not lower," Schindler said. "Housing decisions often involve strong feelings — say, if you really love that house, anything that would make you feel a little better about paying the price could well make a difference."

In the Virginia sales study, it's not as if buyers didn't recognize that the "just below" homes were overpriced. They did. They bargained hard and negotiated bigger discounts than they did with sellers who used round or precise pricing.

Still, the "just below" sellers came out on top. They made more money because the high initial price more than offset the discount. For instance, people who marketed their previously built homes at "just below" prices sold their properties for 1.96 percent more on average than they would have if they had used the round price, the study concluded.

It may be irrational, but the method seems to work for all sorts of products, which is why people stick with it no matter what. Australia did away with its one-cent equivalent long ago, Seiler said. Yet products there are still priced as if that currency exists. "If you buy something and there's extra change, they just round it off," Seiler said. "It's a lingering hangover effect."

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