

## Report Number 34523

### How Pricing Affects Your Business

When most businesses begin the task of pricing products or services they generally use some kind of "standard mark-up". This is fine most of the time as long as the mark-up price is OK'd by the market. It is the market that determines what something costs, not your costs.

There is a narrow "window" that determines the "premium" price you can charge for a product or service and the "floor" price. The premium price is the highest price the market will allow. The floor price is the least amount you can sell something for and still make money. The price you use has an influence on many facets of your business. Here are just a few to consider:

- **Profit:** As mentioned above the price you arrive at determines how much you make on each sale.
- **ROI (Return on Investment):** When you opened your business you may have taken a loan or invested your own money and the product price determines how quickly you recoup that investment.
- **Promotion:** The course of any small business seldom runs smoothly. There are going to be times that you will want to do some type of business promotion. Your pricing will dictate how successful you will be with each promotion.
- **Image: Lexus or Yugo?** Do these two products have a price image? How much you charge will effect the customer perception of the value of your service or product. Low price economy, savings or fewer features. High price prestige, status or quality.

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#### When to consider changing your price.

As a rule, you should constantly monitor and review your pricing. As the market changes you should change. If you raise your price you need to be prepared to back it up with benefits that justify the higher price. If you lower prices show the customer that they are not going to have to make a sacrifice of quality. Here are some circumstances where you might want to consider changes in pricing:

- **New Products:** New products are an often used way to raise prices. A newer improved product or service can command a higher price.
- **Industry Changes:** There will be times when new regulations or changes within your industry may affect your pricing. There may be upgrades required to older products that will affect price.
- **Going Into A New Market:** As new markets emerge you may want to take advantage of new profit centers. The price you charge for new products or services will determine your success or failure in these markets.
- **Competition:** If the competition raises or lowers their price should you do the same? I would ask, "How strong is your competitor?" "What is the customer perception of the competitor and their pricing?" If they are perceived as a "discount house" you may not want to change prices. Make sure you know your market, your customers, and your products.
- **Inflation / Depression:** The economy has been pretty strong the last few years so you may not think this is something to consider. Unusual things seem to affect the stock market and the buying habits of customers. Always think positive but, be prepared for the worst the economy has to offer.
- **Change of Strategy:** When you introduce a new product or service there is a period of time when sales are high because of curiosity and newness of the product. As the newness wears off, so do sales. In order to increase sales you can either, cut prices (not always the best idea) or you can increase awareness through increased advertising or promotion. Depending on the product, if sales go down, it may be the fault of the product and not the price. For example: where would you go to buy a good slide rule. They have been replaced by the hand held calculator.

### **The Robinson-Patman Act**

This legislation is designed to protect the small business owner from price discrimination by suppliers. You will find this act at <http://www.lawmall.com/rpa/rpasec13.html>

When in doubt about legalities of pricing consult an attorney.