Small Business Resources

Selected for Women Entrepreneurs by Women's Enterprise Centre

PRICING YOUR PRODUCTS AND SERVICE

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BEFORE SETTING YOUR PRICES

The right price has to be low enough to attract customers and high enough to make them profitable. It's part art and part science, and there are several factors, which go into the development of an optimum price. Here are the steps to follow to make sure your price is right:

Step 1: Develop a goal for your pricing strategy

Before you start setting prices, decide what you want your prices to accomplish for you. Do you want your prices to bring in as many sales as possible in the next few months? Or to weed out unprofitable clients? Or to define your company as a prestige provider of services? Each of these goals could have implications for where, within a range, you put your prices, so make these philosophical decisions before you start crunching numbers. Remember that pricing is a strategic tool, so it should be in tune with your marketing strategy and the way you are positioning your products.

Step 2: Learn what your competitors and colleagues charge

This is easier than it used to be, if you're willing to do some online research. Many small business owners are happy to post their typical fees or share Information with colleagues who don't serve the same geographic markets. You can also find out what others are charging through your professional society or trade magazine. Many industry publications publish membership surveys with this information.

You can also get competitive information by interviewing some target customers. You might tell them you are developing your business and ask them what they would expect to pay, or typically do pay, for the types of products and services you'll be offering. Once you know what the competition is charging, that will give you a rough guide to what you can charge. You still may choose to set your prices somewhat lower or higher, depending upon your own pricing goals.

Step 3: Analyze your costs, and know what you need to make

Even if you love what you do, there's no sense losing money at it. Figure out what you need to make to keep running your business and to take home a reasonable profit. Analyze what you spend to make the product you are pricing, so you have a firm "cost" number in mind.

Pricing Services

For a service business, you can analyze your costs by adding up how much you spend on supplies, rent, your business phone bill, professional subscriptions, salaries and more. Include a target gallery figure for yourself, and don't forget to include the extras that will have to come out of your salary, such as taxes, health and life insurance, and retirement savings. When you add it all up and divide by the number of hours you and your staffs have to run your business, you'll be able to develop an approximate hourly rate. You can then use that rate to estimate how much you'll charge for individual projects. Take some time to decide whether you want to charge by the hour or the project. You might find each approach works in different situations. If the client is likely to need lots of handholding or send you back for extra work, charge by the hour. If the client is likely to be scared away by your hourly rate, charge by project. As you gain more experience, you'll develop a better feel for when each approach works best.

Pricing Products

Product pricing requires you to add a few more calculations to the task at hand. You'll set better product prices if you do a break-even analysis so you can make sure there is a sound relationship between your prices, your costs, and the quantities you expect to sell. Here are the basics for performing a break-even analysis:

Determine your unit variable costs and your fixed costs. For example, if you make doll clothes, your fixed costs will be the amount you spend on electricity and rent, and the annual cost of your sewing machine. Your variable costs will be the cost of the material that goes into each doll outfit. In this example, assume the variable costs are 75 cents per outfit and your fixed costs as $250 a month.

Set a target price, just for estimating purposes. Once you finish the calculation, you can adjust the price up or down. In this example, set a price of $5 per outfit.

Subtract the variable costs from the price ($5 -$0.75 = $4.25).
Divide that answer into your fixed costs to find your break-even point.
($250/$4.25 = 58.8)

In this example, you'd have to sell 59 outfits a month just to break even. Is that reasonable, or should the price be higher or lower? As you get more comfortable with calculations like this, you can be confident that your prices will cover your costs.

Step 4: Identify Your Added Value

Once you know the financial facts of your business life, you need to spend some time thinking of the intangibles that make your goods and services worth more than just the sum of their costs. What's special about what you do? Your customers will be willing to pay more if they know they're getting something worthwhile in return. For example, your prices could be higher if you

promise delivery of your work on a firm schedule, offer more experience than your competitors, or bake a healthier cheesecake. This concept of "value added" pricing is what's driving markets today, and more than any other component of your calculation will justify the prices you need to be profitable.

Step 5: Put It All Together in a Pricing Strategy

Your competitors' prices and your costs will help you establish a pricing range and those other considerations will help you place your prices within that range. But you must also decide how you want your product to be priced. If you are new to a service business, you might want to charge by the hour, so you won't have the risk of taking on work at prices that don't cover your time. As you get experienced, you may choose to move to project pricing so you won't have to account for every hour.

If you are selling products, you'll have to decide if you want to price them higher and sell fewer of them, or price them lower and win new customers. You may decide to package more than one product together and give price breaks for quantity.

Consider whether you want to have a one-price policy or a flexible price policy that allows you to adjust your prices for different customers, jobs and orders. This is easier to do with services than it is with goods. If you offer the same exact product under the same conditions to different customers at different

Prices, you could run afoul of the law. You could even establish different prices for different distribution channels:

You could sell your quilts directly through mail order at one price, but charge another to stores that were willing to buy and display them. And finally, decide how and when you want to adjust your prices so they can help you meet your other business objectives. Will you discount during slow periods? Offer price breaks to clients who bring in referrals? Offer to "match any offers" by your competitors? Agree to give fast paying customers a percentage off? These are all pricing actions that can bring you business and improve your cash flow, as long as you approach them cautiously and with a firm flow in mind.

Step 6: Go Back to Step One

Like every aspect of your business, your prices should be reviewed frequently. You may discover, after just a short time that you've set them too high or too low, or just priced them wrong for the industry you are in. Review your pricing goals, strategies and levels regularly, and don't be afraid to make adjustments when you need to. In the retail world, it's called a sale!

PRICING STRATEGIES

Pricing goods and services - it may be the most difficult task in the business arena.

It's generally agreed that the primary goal of business is to make a profit. But many small businesses fail to master this objective simply because they don't consider all the factors necessary to make prices competitive and yield that elusive profit.

Before setting prices, you must understand your market, distribution costs and competition. Remember, the marketplace responds rapidly to technological advances and international

competition. You must keep abreast of the factors that affect pricing and be ready to adjust quickly.

There are several pricing strategies; select the approach that will make your goods or services the most competitive and will help you reach your profit goals.

Retail Cost and Pricing

A common pricing practice among small businesses is to follow the manufacturer's suggested retail price. The suggested retail price is easy to use, but it does have one major shortcoming - it doesn't adequately account for the element of competition.

Competitive Position

An alternative is to base your price on those of your competitors. A small retailer, for example, should compare prices with a store that's comparable in size and customer volume. It's very chancy to compete with a large store's prices, because they can buy in larger volume and their cost per unit will be less. Instead, price products based on your local small-store analysis, and then highlight other competitive factors, like personalized customer service and convenient location. There are any number of factors that influence a consumer's decision to buy from a certain business, including price, convenience, and courteous and attentive service.

Pricing Below Competition

Some vendors have been very successful pricing their goods or services below the competition. Since this strategy reduces the profit margin per sale, it requires a company to reduce its costs and -

- obtain the best prices possible for merchandise,
- locate the business in an inexpensive location or facility,
- closely control inventory,
- limit the lines to fast-moving items,
- design advertising to concentrate on price specials, and
- limit other services.

One word of caution: pricing goods below the competition can be difficult to sustain. Why? Because every cost component must be constantly monitored and adjusted. It also exposes a business to pricing wars. Competitors can match the lower price, leaving both parties out in the cold.

Pricing Above Competition

This strategy is possible when price is not the customer's greatest concern. Considerations important enough for customers to justify paying higher prices include -

- service considerations, including delivery, speed of service, satisfaction in handling customer complaints, knowledge of product or service, and helpful, friendly employees;
- a convenient or exclusive location; and
- exclusive merchandise.

Price Lining

This strategy targets a precise segment of the buying public by carrying products only in a specific price range. For example, a store may wish to attract customers willing to pay over $50 for a purse. Price lining has certain advantages:

- ease of selection for customers;
- reduced inventory; and
- reduced storage costs, due to smaller inventory.

Multiple Pricing

This approach involves selling a number of units for a single price - for example, two items for $1.98. This is useful for low-cost consumable products, such as shampoo or toothpaste. Many stores find this an attractive pricing strategy for sales and year-end clearances.

Cost Factors and Pricing

Every component of a service or product has a different, specific cost. Many small firms fail to analyze each component of their commodity's total cost, and therefore fail to price profitably. Once this analysis is done, prices can be set to maximize profits and eliminate any unprofitable service.

Cost components include material, labor and overhead costs.

- Material Costs are the costs of all materials found in the final product. For example, the wood, glue and other materials used in the manufacturing of a chair are direct materials.

- Labor Costs are the costs of the work that goes into the manufacturing of a product. An example would be the wages of all production-line workers producing a certain commodity. Multiplying the cost of labor per hour derives the direct labor costs by the number of personnel-hours needed to complete the job.

  Remember to use not only the hourly wage but also the dollar value of fringe benefits. These include social security, workers' compensation, unemployment compensation, insurance, retirement benefits, etc.

- Overhead Costs are any costs not readily identifiable with a particular product. These costs include indirect materials, such as supplies, heat and light, depreciation, taxes, rent, advertising, transportation and insurance. Overhead costs also cover indirect labor costs, such as clerical, legal and janitorial services. Be sure to include shipping, handling and/or storage as well as other cost components.

Part of the overhead costs must be allocated to each service performed or product produced. The overhead rate can be expressed as a percentage or an hourly rate.

It is also important to adjust your overhead costs annually. Charges must be revised to reflect inflation and higher benefit rates.

It's best to project the costs semiannually; including increased executive salaries and other projected costs.

Figuring Costs and Profits for a Consultant Service

As a consultant, you will most likely price your services by the hour. Remember to charge for an adequate number of hours. Travel time is usually listed as an extra charge.

It's unlikely that all your time will be billed to clients. There- fore, hourly or contract fees must be set high enough to cover expenses during slow periods. That is why one-half of the total normal working hours for a given year are used in figuring overhead rates. Try to obtain long-term, monthly or contract assignments when possible.

Summary

Your pricing structure and policy are major components of your public image and are crucial to securing and keeping your clientele.

Pricing for service businesses may be more complex than retail pricing. The equation, however, is the same:

cost + operating expenses + desired profit = price.

The key to success is to have a well-planned strategy. Establish your policies and constantly monitor prices and operating costs to insure profit. Accuracy increases profits!

PRICING FOR PROFITABILITY

Pop quiz! Which of the following pricing strategies generate the highest profits?

(a) Cost-based pricing, determined by adding a fixed amount or percentage to your unit cost.
(b) Demand-oriented pricing, pegged to buyers' level of interest.
(c) Competition-oriented pricing, geared to the market.

Answer: (b) and (c). Cost (a) does play a role in pricing, giving you a break-even minimum representing your unit cost plus overhead. But to price for profitability, you need to look at demand and competition -- which tell you how high above the minimum your prices should go to stimulate the sales volumes you want and provide the profit margins you require.

However, cost-based pricing remains today's most popular strategy. And the reasons are obvious. It's simple and direct, and is viewed as equitable to buyers and sellers alike. It also has an honored history, used by regulated utility companies as well as giants like General Motors to set prices that deliver a targeted rate of return on costs.

The problem is that this method doesn't provide pricing flexibility. It doesn't allow you to react to changes in demand or competition. It doesn't permit you to establish different profit margins to maximize your returns from different items in your inventory. It doesn't enable you to price aggressively in the face of market conditions to which your competitors must respond. In sum, it doesn't let you adjust prices up and down to protect the profitability and, indeed, the survival of your business.

Granted, profitability-based pricing is more complicated than cost-based pricing, since it takes into account a host of different factors, instead of just one. Yet the rules are remarkably easy to understand and easy to use. What's more, even the most complex profit-pricing situations have only two possible outcomes: raise prices or lower them. It's that simple.

Think of Price as a Statement of Your Aims and Operations "The right price," claims Herman Holtz in "Priced to Sell: A Complete Guide to More Profitable Pricing" (Upstart Publishing,1996), "is the highest one that fits your business strategy." That business strategy may prescribe:

- Raising or lowering prices to meet the competition.
- Raising or lowering prices to prepare for technological or other changes in your industry.
- Keeping prices low to stimulate high sales volume and gain high market share.
- Keeping prices high, and your image upscale, to maintain high profit margins even if sales volume lags.

So whether the price zone your strategy calls for is high or low, the right price, i.e., the profit-based price, is the highest one in your zone.

Regardless of strategic goals, however, your pricing must also fit the type of product or service you offer. Widely available nuts-and-bolts types of products and services sell best at low prices, say the experts, while high-quality luxury goods and customized services sell best at high ones. The message here is that buyers believe they get what they pay for: if they want ordinary value, they'll pay ordinary prices; if they want high value and perceive high value, they're willing to pay a premium for it. So if you're selling thumbtacks and you decide to raise your prices, you'd better start carrying designer thumbtacks.

Second, your pricing should conform to the clientele you're seeking. Generally, low prices draw a large group of customers who base buying decisions primarily on price, while high prices attract a smaller, more select group who think that quality is a more important consideration. Note that high-end pricing (called "skimming" because you skim the cream of customers) often relaxes over time to include lower prices designed to capture a larger segment of the market.

Third, your pricing should reflect the sales-activity levels of different items in your inventory. Give low markups to your fast movers or staples to stimulate volume and meet competition. Give high markups to slow movers and specialty items to generate profit margins that will cover the higher storage and carrying costs their longer time on the shelf entails.

To conclude, whenever you're pricing or re-pricing, your first question is whether to increase prices or reduce them. This applies if you plan to introduce a new product, enter a new market, battle the competition, update your sales strategy or respond to economic upswings or downturns. And the answer depends on such key factors as your strategic aims, your clientele and the quality and sales activity of the products and services you offer. (See accompanying charts for a quick-reference summary.)

This resolved, your second question is to decide by what amount to raise or lower prices. Here you must estimate the price your customers are likely to pay, judging not only by the pressures of demand and competition, but also by psychological factors in consumer motivation such as image, novelty, prestige and impulse buying. "No sophisticated approach exists whereby you input all these variables and out pops the correct price," warn Cochrane Chase and Kenneth L.

Barasch in "Marketing Problem Solver "(Chilton Book Company, 1977), "Rather, the pricing executive must sift through all the data and say, `This price looks about right.'"

In determining that rightness, however, be sure not to undervalue the perspective of the buyer. As Ovid Riso points out in "The Dartnell Sales Manager's Handbook "(The Dartnell Corporation, 1977), pricing entails setting your price between two points: the price you, as the seller, want to get and the price your buyer is willing to pay. And the "sound approach," Riso stresses, "is from the viewpoint of the buyer."

How to Raise Your Prices

These days, many business writers and analysts advocate raising prices. "When businesses go bust," reports Joan Delaney, "it's often because their prices are too low." "Raising prices intelligently remains an important way to build your company's financial health," adds Robert J. Calvin.

Yet higher-end prices aren't for everyone. To quality, you need higher-end goods or services, along with a clientele that appreciates premium quality and is willing to pay for it. If these conditions apply, you probably should think about raising your prices.

In some cases, however, there's no "probably" about it: raising prices is not something you should do, but must. Key indications, according to Lawrence L. Steinmetz, author of "How to Sell at Prices Higher Than Your Competitors" (Horizon Publications) are that your prices are significantly lower than your competitors', your phone is ringing off the hook with requests for bids because you're known to undercharge, or your profits have declined despite a flat or increased volume of sales.

Another telling sign is that customers scanning your price list or job quote ask if it's current because "they think your prices are a steal." Further indicators, add Chase and Barasch, are that you easily sell your entire output, your customers can pay more than you are charging, and your prices remain unchanged despite cost inflation or over-demand.

Even if you don't have to raise prices, you still may want to do so in order to improve your profit margins. To support a higher price, however, you'll need to enhance the perceived value of your goods or services. Make no mistake: enhancing value can be a major undertaking, a project that may require changes in everything from your marketing and staffing to your graphics and decor, not to mention shifts in the products and services you provide.

"If you're a manufacturer," this can mean retooling to create a new gold-standard premium item or, at the very least, repackaging to emphasize the value of your current goods.

"If you're a retailer," it means upgrading your image and proving the value of your products by adding not only higher-end lines, but also free service enhancements such as installation, customization, personalized service, emergency services or training. These demonstrate premium quality, and their cost can be more than covered by the increases in price.

Whatever strategy you use to raise prices, expect to make fewer sales but derive greater profit from each one. Consequently you should raise your prices by increment, advises business writer Robert J. Calvin, "Until the additional profit generated totally offsets the sales decline."

Even more important, caution Chase and Barasch, is to be aware of the risks in raising prices - the risks that premium-price buyers may not exist in the numbers you anticipate and that increased prices will produce ill will. Added to these are the greatest risk and the most likely outcome of all: that your competitors will readily follow suit and raise their prices as well.

How to Lower Your Prices

On the other hand, your current prices may be too high. How can you tell? Chase and Barasch point to signs like excess capacity, falling market share, evidence that your prices considerably exceed the competitions for comparable quality, or proof that even small price reductions greatly increase your sales.

Under certain conditions, your prices will almost surely be too high. In a declining market, for example, you'll probably need to reduce prices, though Chase and Barasch advise you to evaluate the decline -- sorting fact from rumor. Explore causes for the decline other than price and see if the decline affects the whole market and not just your own sales -- before initiating price-cutting. "Don't be `trigger-happy' by reducing price before it's necessary," they warn. "At the same time, don't wait for a crisis to resolve itself."

Even if your prices aren't too high for the market, you may still want to lower them. One reason is that price-cutting performs a competitive assault, drawing business from your competitors as well as discouraging prospective competitors from entering the market because you've made the going profit margin so small.

A more common reason is that low prices traditionally generate greater sales volume - a key benefit, emphasizes Ovid Riso, because "the rate of turnover is the most important factor in business." After all, he points out, if you sell three articles at a 10 percent profit in the time it would take to sell just one article at a 15 percent profit, you'll make twice as much money.

In fact, Riso strongly recommends price-cutting not only as a general way to stimulate volume, but also as a sales builder in the form of loss leaders. "It has been found," he writes, "that loss leaders attract so much store traffic, which buys other goods at list price, that the loss is more than made up." And that's not all: loss leaders cost far less than the advertising needed to achieve the same promotional value.

Of course, notes Riso, the drawback to price-cutting is that competitors are likely to cut prices too. In this case, not only will you lose your low-price competitive edge, but also a "dangerous" price war may ensue, making it difficult to subsequently return prices to normal.

So if your competitors have started price-cutting, are you unwise to join them? Northwestern University marketing professor Philip Kotler proposes a game plan for deciding whether you should or not. Lower your prices, he advises in "Marketing Management"(Prentice-Hall, Inc., 1980), only if the following conditions apply:

- The price cut is liable to have a significant effect on your sales, AND
- The price cut is permanent, AND
- A lowering of prices won't hurt your company's image, AND
- There is no feasible alternative to cutting prices.

Otherwise, stick with your current prices but keep a watchful eye on the competition.

Alternatively, he writes, you can weaken the effect of your competitor's price-cutting by launching a "non price counterattack." Specifically, counter small price cuts (less than two percent) with a cents-off sale. Counter moderate cuts (two to four percent) with a self-liquidating premium. Counter larger cuts (four to six percent) with advertising aimed at increasing your exposure. And counter very large cuts (more than six percent) with an aggressive revamping of your advertising and your company image.

Yet another kind of counterattack Kotler recommends is to introduce services or product improvements to emphasize the greater value you offer to buyers. Similarly, you could increase your prices while adding lower-cost lines to compete directly with the price-cutter's prices.

How to Raise or Lower Prices Without Changing Your Price Tags

An altogether different pricing strategy is to maintain your current price schedule, yet either raise prices by charging for goods or services you now include free, or lower prices by offering a variety of discounts.

"You must determine the economic value of your add-on services to the customer," emphasizes Stanton G. Cort, associate professor of marketing at the Weatherhead School of Marketing, Case Western Reserve University, Cleveland. To assess their dollar value, he says, consider that your customers could either provide the services in-house, buy them from another company or go without. "The cost of the least expensive alternative," he concludes, "is likely to be the highest price you could hope to get for an add-on service."

Yet if a valuable service you offer, like express delivery, lets your customers turn around and offer the same key benefit to their customers, a charge for that service "is an easy sell," Cort adds. Similarly easy sells are attractive add-ons once included free in your basic package and now available for an additional charge. In short, you need to identify the services your customers deem important and therefore are likely to pay extra to receive.

On the other side of the coin, the discount side, a wide range of incentives exists from which to choose, including cash discounts, manufacturers' allowances, order-size bonuses, annual volume rebates and prompt-payment discounts, along with garden-variety sales. Besides increasing sales volume as a rule, discounts have proved especially successful with luxury items, such as high-end cars, because they make the price more attractive without jeopardizing the premium positioning of the product.

Discounts have created problems for manufacturers and distributors, however, because the practice of stringing discounts together, one after the next, may erode invoice prices to unprofitable levels. Consequently, say business consultants Michael V. Marn and Robert L. Rosiello, you need to plan your pricing policies with an eye to the actual sale price ("pocket price"), not the invoice price, and engineer the discount drop-off from invoice to pocket price in a way that keeps prices motivating to buyers but still protects your profitability.

Writing in the "Harvard Business Review", Marn and Rosiello advise monitoring the variation in pocket prices charged for your products. Out-of-control discounting can make prices vary by as much as 60 percent; and curbing these excesses enabled one company, whose pocket prices had varied by 25 percent, to achieve a 43 percent jump in operating profit on the same volume of sales.

Also critically evaluate the discounts you offer. One company found that its customers were eager for certain discounts, but indifferent to others that delivered the same reduction in price. By maximizing important discounts and minimizing the rest, the company was able to stimulate volume while also seeing a 3.5 percent rise in average pocket price and a 60 percent rise in operating profit.
In short, say Marn and Rosiello, use discounts selectively. Increasing your prices, they note, "can boost profit faster than increasing volume will." So by knowing which discounts customers consider particularly attractive, and by manipulating the package of incentives that affect pocket price, you can simultaneously offer discounts and increase your profits.

PRICING AT A GLANCE: WHEN TO PRICE LOW AND WHEN TO PRICE HIGH

"Pricing is a numbers game," claim Cochrane Chase and Kenneth L. Barasch in "Marketing Problem Solver." Despite all the detailed decision charts, task breakdowns and other price rationalizers included in their book, they conclude that instinct, not formulas, provides the best guide to good pricing. "After reviewing all information and relationships among factors," they write, "It is time to use a good instinctive feel for the market and its environment."

The following charts, compiled from Chase and Barasch's book and a variety of other texts, should help get your instincts flowing.

Pricing low is a good strategy if items are...

- Widely available
- Usable for a long time
- Not very durable
- Used for one thing only
- Low-tech; unlikely to receive rapid changes or upgrades
- Fast moving; high turnover
- A source of long-term profits
- Sold in a highly competitive environment
- Part of a line of related products
- Compatible with no or few sellable services like installation and training

Pricing high is a good strategy if items are...

- Rare or customized
- Outmoded rapidly
- Durable over many years
- Versatile; multiple uses
- High-tech; likely to receive rapid changes or upgrades
- Slow moving; lows turnover
- A source of short-term profits
- Sold in a market with little competition
- Single, unrelated, stand-alone products
- Compatible with sellable services like installation and training
- Impulse or emergency items

Pricing low is a good strategy if you, as a manufacturer or distributor, want ...

- Introduction of a new capital-intensive product, whose unit cost will decrease rapidly with volume production
- A simple distribution system involving one distributor
- A large or mass-market share

- Little or no use of promotional support through advertising and sales activities
- Entry into a well-developed market penetrating many industries
- Entry into a mature, highly competitive market
- Easy market penetration
  (Note: Downside of low-balling is that low price does not always generate volume sales.)

Pricing high is a good strategy if you, as a manufacturer or distributor, want...

- Introduction of a new labor-intensive product, whose unit cost will increase rapidly with volume production
- A complex distribution system involving multiple levels of distribution
- A small, select market share of upscale buyers
- Considerable use of promotional support through advertising and sales activities
- Entry into a poorly developed market penetrating few industries
- Entry into a new or developing market
- High profits for the short-term only

(Note: Downside of highballing is that it discourages some buyers, attracts competition and may wrongly assume availability of buyers willing to pay a higher price for higher quality.

Be aware that price shifts can raise or lower demand and sales for certain kinds of products, but have little or no effect on other products. For example, lowering the price of paper clips would not induce customers to buy and consume more than they would otherwise. Lowering the price of laptop computers, however, would indeed stimulate greater demand and a higher volume of sales.

Demand for these products DO change when prices are raised or lowered:

- Products for which many substitutes are available
- High-ticket items
- Luxury goods
- Highly durable items
- Products that satisfy a hard-to-fulfill need
- Products that buyers can postpone purchasing

Demand for these products DOES NOT change when prices are raised or lowered:

- Products for which no substitutes are available
- Low-ticket times
- Necessity goods; staples
- Not very durable items
- Products that satisfy an easy-to-fulfill need
- Products that buyers need now and cannot postpone purchasing

SELECTIVE PRICING IS THE KEY TODAY

"The pricing question with small businesses," says Leo Helzel, founder of the Enterprise Programs at the Haas Business School at the University of California, Berkeley, "is whether you want to make a living out of your operation, or want to make handsome profits beyond that to expand it." And if you want to make a very good living from your business or want to make profits, Helzel adds, "the key today is selective pricing."

With selective pricing, you segment the items you carry into three categories, each of which provides a different amount of gross profit:

1. "Specials and loss leaders" bring you little or no gross profit. Their benefit is that the low price stimulates traffic and sales.
2. "Standard or branded items" provide low gross profit. Because these items are well known and widely available, you have to charge the recognized, low-margin price to stay competitive.
3. "Unbranded, off-brand, specialty, proprietary or unusual items "deliver high gross profit. Since they're neither available from your competitors nor identified with a certain price, you can sell them successfully at a high markup.

In most operations, Helzel points out, you need to stock all three categories. This way, margins of your lower-profit items can be balanced by those of your higher-profit goods to produce the kind of gross profits you need. For example, a customer who buys an attractive loss leader may also walk away with a specialty item marked up by a hefty 500 percent.

"The salvation for small firms is having items not available elsewhere," Helzel comments, "items that are different, items that offer quality. These, and service, are the only way small businesses can successfully compete with the chains."

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