

Worksheet - Pricing Models for Successful Business

The concept of “price” is a topic many entrepreneurs ponder as they begin shaping their business ideas. The *Introduction to Pricing* course examined three pricing models—Cost-based Pricing, Customer-based Pricing, and Competition-based Pricing. The *Pricing Models for Successful Business* course explores those pricing models in more detail and offers methods to help you adapt pricing for your market.

*Of the four “Ps” in the marketing mix, **Price** is the only component that generates revenue; Product, Promotion, and Place are all costs.*

Use this worksheet to document your thoughts, ideas, and action items as they relate to developing a pricing model for your business. There are many variables that will affect your price, and these exercises are designed to structure your research for the best results.

Use the fillable PDF form fields to write your responses or print the worksheet and write in the space provided.

Cost-Based Pricing Model

To implement a cost-based pricing model, you first need to calculate the costs incurred by producing, marketing, and distributing your product or service. Use the table below to calculate the variable and fixed costs for your product or service.

Variable Costs: Write down the variable costs you have to produce your product or deliver your service. To make this easier, try to do this for an average year or month. For example, if you normally produce 5,000 units a month use that as your basis to calculate these costs.

| Item | Cost | # of units produced | Cost Per Unit |
|------------------------------|-----------------|---------------------|----------------------------|
| <i>(For example, Flour)</i> | <i>\$500.00</i> | <i>5,000</i> | <i>\$500/5000 = \$0.10</i> |
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| TOTAL VARIABLE COSTS: | | | |

Add up all the costs in the “Cost Per Unit” column to calculate total *variable costs*: _____

Fixed Costs: Now, write down all the fixed costs you have. If you were able to calculate your variable costs based on your monthly production rate, use your monthly fixed costs here.

| Item | Cost | # of units produced | Cost Per Unit |
|----------------------------|-------------------|---------------------|-------------------------------|
| <i>(For example, Rent)</i> | <i>\$2,000.00</i> | <i>5,000</i> | <i>\$2,000/5,000 = \$0.40</i> |
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| TOTAL FIXED COSTS: | | | |

Add up all of the costs in the “Cost Per Unit” column to calculate total *fixed costs*: _____

You can find your total cost per unit by adding your *variable cost* per unit and your *fixed cost* per unit:

$$\frac{\text{Variable Cost Per Unit}}{\text{Variable Cost Per Unit}} + \frac{\text{Fixed Cost Per Unit}}{\text{Fixed Cost Per Unit}} = \frac{\text{Total Cost Per Unit}}{\text{Total Cost Per Unit}}$$

Adding Markup: Separating your costs into variable and fixed costs allows you to perform different calculations and play around with various factors to see how they influence your prices. By changing these factors, you can reduce costs to increase profits or decrease prices to increase sales and market share. What percent markup would you like to add to your product?

HINT: Your markup should allow you to make a reasonable profit. If your Total Cost Per Unit is more than your current price, your business is losing money.

To find your final price, first calculate your Markup Cost by multiplying your Total Cost Per Unit with the Markup % you chose. Enter Markup % as a decimal (e.g., 25% is .25, 10% is .10, etc.)

$$\frac{\text{Total Cost Per Unit}}{\text{Total Cost Per Unit}} \times \frac{\text{Markup \%}}{\text{Markup \%}} = \frac{\text{Markup Cost}}{\text{Markup Cost}}$$

Then, add your Markup Cost to the Total Cost Per Unit for your final price:

$$\frac{\text{Markup Cost}}{\text{Markup Cost}} + \frac{\text{Total Cost Per Unit}}{\text{Total Cost Per Unit}} = \frac{\text{Final Price}}{\text{Final Price}}$$

Customer-Based Pricing Model

The Customer-based pricing model, also called value-based pricing, involves using information about your customers to set a price. To implement a customer-based pricing model, you need to study the market to understand how much your customers can and are willing to pay. Finding this out requires you to do some research.

When able, select one of the five research ideas below to research. Then, in the space provided, write down how you plan to implement your research. End your research by writing down the results from your research.

1. Perform Satisfaction Studies
2. Research Customer Decision-making Process
3. Measure Effect of Prices
4. Monitor Social Media
5. Research Customer Perception

NOTE: If you choose more than one, make sure you keep track of the Research Idea, Execution Plan, and Results separately to keep your research accurate.

Often in the Customer-based pricing model, you will offer your product at different prices to different segments in your target market. These segments are divided based on the customers' requirements, attitudes, culture, and various other characteristics.

In the space below, identify market segments you want to target and write down information about how you might do that. Although there is no wrong way to document this process, the example below uses a 4-column table to categorize the Market Segment and Description, Segment Size, Segment Price Consideration, and Segment Price

| Market Segment & Description | Segment Size | Segment Price Considerations | Segment Price |
|---|---|--|----------------------|
| <i>For Example: France This is the market I export to in France</i> | <i>~\$1,500,000 annually ~15% of my sales</i> | <i>Less sensitive to price than my other segments – I could charge 10% more and not lose sales</i> | <i>\$10/each</i> |

Competition-Based Pricing Model

When using the Competition-based pricing model, a business sets its prices based on where its competitors set theirs. Like the Customer-based pricing model, the Competitor-based model relies heavily on research.

In the space below, identify your competitors, a short description, Analysis about how their products compare to yours; and provide insight about Price. Although there is no wrong way to document this process, the example below uses a 4-column table to categorize the research:

| Competitor | Description | Analysis | Price |
|-----------------------------------|--|--|---|
| <i>For Example: Acme Products</i> | <i>Online store that offers the same widgets that I sell</i> | <i>The widgets are the same but Acme Products doesn't offer a guarantee. However, they are considered the leader in the widget industry.</i> | <i>Acme price is \$5/widget I would probably need to sell at that price to bring in customers because they are so popular, even though I offer a guarantee.</i> |

Breakeven Analysis

Regardless of the pricing method you chose, a breakeven analysis is essential to determine the volume of sales you need to achieve to recover your costs at a certain price. You will need the Variable and Fixed Costs you calculated in the cost-based pricing section as well as the price you plan to charge for your product.

To find the Breakeven Quantity (BEQ) that you must sell each month to cover your costs use the following formula.

$$\text{BEQ} = \frac{\text{Fixed Costs Per Month}}{\text{Price per unit} - \text{Variable Cost per unit}}$$

Fixed Costs Per Month:

Price per Unit:

Variable Cost per Unit:

Breakeven Quantity:

Change the quantity of units sold for each month. The breakeven quantity is <

Do you think you can sell that many units each month at that price?

How would changing your price affect the number of units you need to sell?

Price per unit of product sold. The breakeven quantity is the number of units you need to sell to cover your costs. The breakeven quantity is the number of units you need to sell to cover your costs.

Selecting Your Pricing Model

Now that you've analyzed the various pricing models for your business, which one is right for your business? Will you need to mix some aspects of each model? What do you think your final price will be?

For example, you calculate your costs to be \$5/unit (Cost-based). You know your competitor sells a similar product for \$10/unit. Consequently, you sell your product at \$9.50/unit (Competition-based). Researching your competitor's sales price helped you decide what markup to add to your product.

Similarly, if you know your competitor sells for \$10/unit (Competition-based), and your customers are willing to pay a little more as long as you offer free installation (Customer-based), you may decide to charge \$15/unit, and based on both your competitor's price and what your customer is willing to pay, offer free installation. Regardless of which model you use as the basis for your price, you should consider your costs, customers, and competition to ensure you're offering the right price.