#### **“**Price is the amount of money charged for a product or service, or the sum of the values that consumers exchange for the benefits of having or using the product or service”.

#### Kotler & Armstrong 2001

#### Pricing is one of the most important decisions facing you as a small business owner. According to Mc Kinsey (consultants) at least 80% of pricing errors result in under-pricing of goods and services and lost profits.

#### To create a unit cost you need to add your mark up to your total costs, then divide this by your product volume to give you the unit cost.

#### You need to know how much profit you want to make to cover all labour, marketing and re-invest for materials.

#### For example is you total costs plus mark up equals £51,000 and the volume is 1,000 your unit price to the customer is £51.

#### Fixed Costs + Variable Costs + Mark Up / potential sales = The price for customers

#### **Cost-Plus Pricing**

In the same way markup pricing arrives at price by adding a certain percentage to the product’s cost, cost-plus pricing also adds to the cost by using a fixed monetary amount rather than percentage.  For instance, a contractor hired to renovate a homeowner’s bathroom will estimate the cost of doing the job by adding their total labour cost to the cost of the materials used in the renovation.

The homeowner’s selection of ceramic tile to be used in the bathroom is likely to have little effect on the labour needed to install it whether it is a low-end, low priced tile or a high-end, premium priced tile.  Assuming most material in the bathroom project are standard sizes and configuration, any change in the total price for the renovation is a result of changes in material costs while labour costs are constant.

Remember the results from your research.

# Cost Plus Pricing

In simple terms this is the cost of producing the service/product with an added on **mark-up** to give the price you will charge your customers.

A Simple Example of Cost plus pricing is as follows:

Fixed costs = £10,000

Variable costs = £25,000

Total costs = **£35,000**

Quantity Produced = 2000

Unit cost of production = £17.50

Mark up = 30%

Add on = £5.25

Selling price to customers £17.50 costs plus £5.25 mark up **= £22.75**

Assuming that the business sells all 2000 of the quantity produced for a selling price of £22.75 the profit after fixed and variable costs have been taken out will be: **£10,500.00**

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| **Activity**  **TASK 1**  You have a business making T-Shirts and you want to set a selling price based on **COST-PLUS** pricing  Your fixed costs are £25,000  Your variable costs are £45,000  The quantity of T-Shirts you produce is 200,000  You want to add a mark-up of 40% to your costs  Question 1: How much will you set your selling price at?  Question 2: How much profit will be made assuming you sell all 200,000 T-Shirts produced?  **Answer**  **Answer 1: £0.49**  The unit cost of production is £0.35 add on a 40% mark-up (£0.14) = **£0.49**  **Answer 2: £28,000.00**  200,000 T-Shirts produced @ £0.49 = £98,000.00.  Subtract the production costs of £70,000.00 giving a profit of **£28,000.00** |  | 20 min |

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| **Review**  **TASK 2**  Break into small groups. Each group has time to think of factors that would have to be considered in setting a selling price. Tutor records on the board ready to produce handout for next session.  Use Ominicalculator to do the same calculations |  |  |