

Small Business Management ^{19e}

LAUNCHING AND GROWING ENTREPRENEURIAL VENTURES

Longenecker · Petty · Palich · Hoy

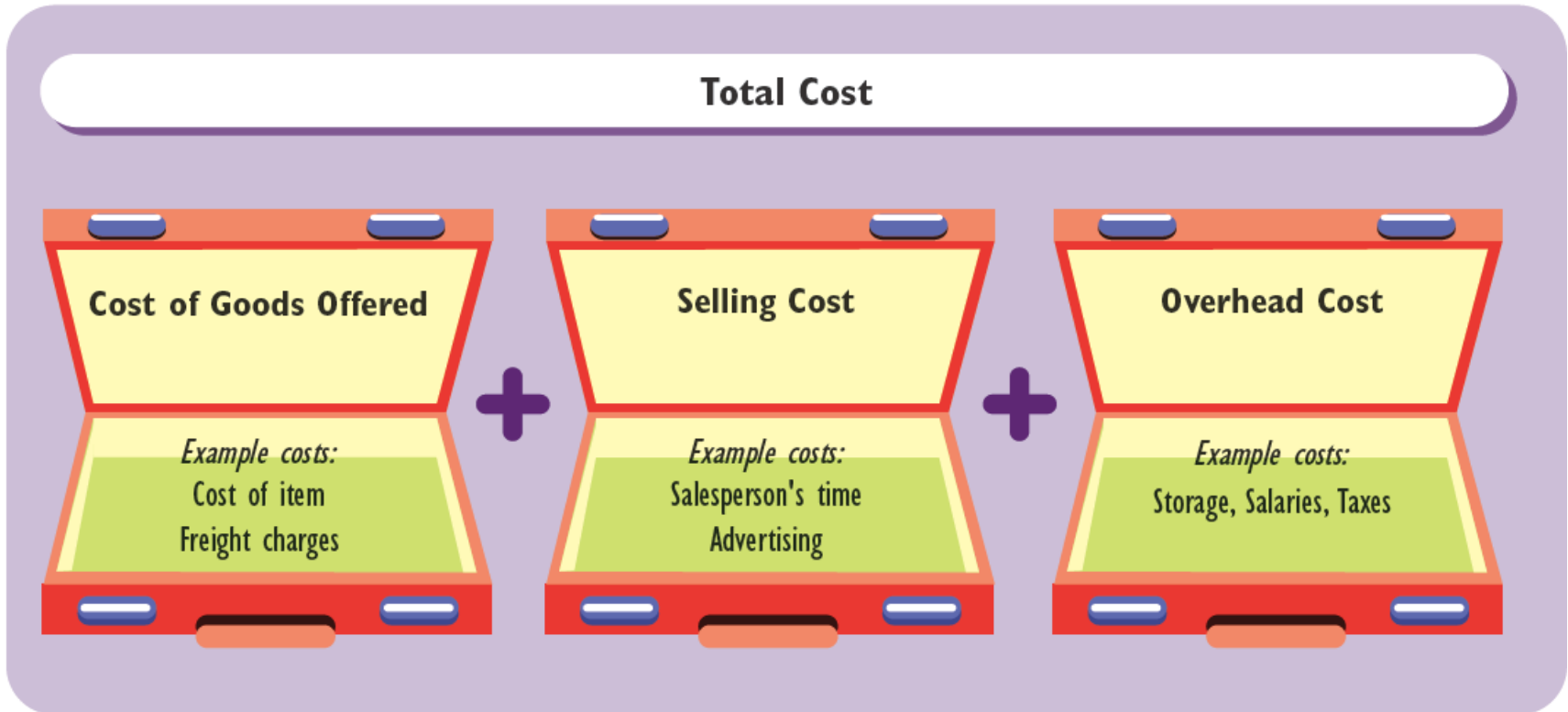


CHAPTER

16

Pricing and Credit
Decisions

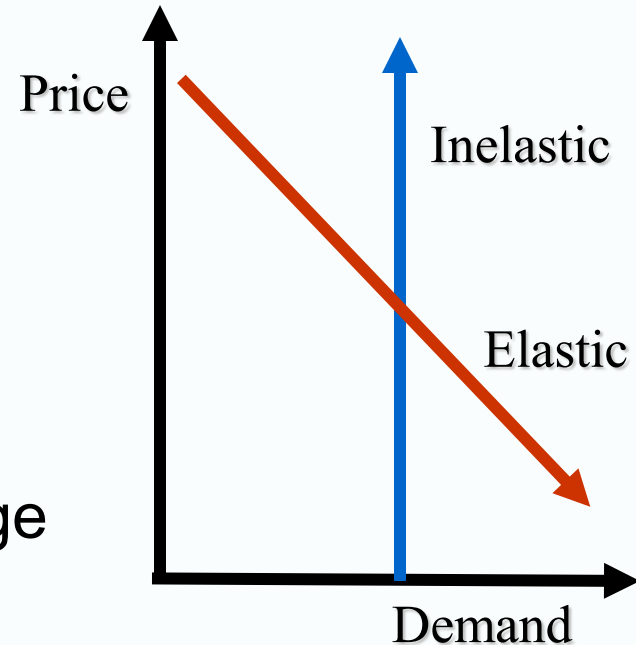
Exhibit 16.1 Total Cost in Determining Price



Total Sales Revenue = Reflection of sales volume and price
Make a little on a lot OR Make a lot on a little

How Customer Demand Affects Pricing

- Elasticity of Demand
 - The degree to which a change in price affects the quantity demanded.
 - Elastic Demand
 - Demand that changes significantly when there is a change in the price of the product. EXAMPLE?
 - Inelastic Demand
 - Demand that does not change significantly when there is a change in the price of the product. EXAMPLE?



Elasticity - Determine Price

Check out my website:

<http://instruction2.mtsac.edu/rjagodka>

Click on “Entrepreneurship Resources”

Scroll down to “Tools & Databases”

Click on “[Pricing](#)”

(FREE Excel template for you to download)

Determine which price will allow you to:

- Maximize Revenue
- Maximize Margins (profits)
- [Pricing on Amazon.com](#)

Profit Contribution vs. Mark Up

Example: **Cost = \$50.00**

Profit Requirement (PR) = 25%

What is the sales price, if I want 25% profit?

Profit Contribution	Mark Up
Cost / (1- PR) = Sales Price 50 / (1-.25) 50 / .75 = \$66.66	Cost x (1 + PR) = Sales Price 50 x (1 + .25) 50 x 1.25 = \$62.50
Sales Price – Cost = Profit 66.66 – 50 = \$16.66	Sales Price – Cost = Profit 62.50 – 50 = \$12.50
Profit / Sales Price = Profit Contribution 16.66 / 66.66 = 24.9 %	Profit / Sales Price = Profit Contribution 12.50 / 62.5 = 20 %

Determining Volume Discounts

Given: Cost = \$50.00 Profit Requirement (PR)= 25 %
Sales Price = \$66.66 Profit/unit = \$16.66

Sale of 20 units:

20 units @ 66.66 = \$1333.20 revenue

@ 25 % PR 16.66 x 20 = \$333.20 profit

5 % Discount

off the Sales Price: $66.66 - 5\% = \$ 63.33 \rightarrow$ profit per unit = \$13.33

$13.33 / 63.33 = 21\%$ PR

To earn same profit (25% PR) after the discount . . .

How many units to sell?

Profit (@ 25% PR) / Discounted profit per unit

$333.20 / 13.33 = 25$ units (need to sell 25% more units)

Profit Requirement (PR) → Discount Chart

5% Price Discount

Profit Requirement (PR)	Profit After Discount	Additional Volume needed to achieve same PR
30 %	26.30 %	20.00 %
32 %	28.40 %	18.50 %
34 %	30.50 %	17.30 %
36 %	32.60 %	16.10 %
38 %	34.70 %	15.10 %
40 %	36.80 %	14.30 %

10 % Price Discount

30 %	22.20 %	50.00 %
32 %	24.40 %	45.50 %
34 %	26.70 %	41.70 %
36 %	28.90 %	38.40 %
38 %	31.10 %	35.70 %
40 %	33.30 %	33.30 %

Pricing and Competitive Advantage

- Pricing and a Firm's Competitive Advantage
 - Customers will demand and pay more for a product or service that they perceive as important to their needs.
- Prestige Pricing
 - Setting a high price to convey an image of high quality or uniqueness (competitive advantage).
 - Customers associate price with quality.
 - Markets with low levels of product knowledge are candidates for prestige pricing. **EXAMPLE?**

Selecting a Pricing Strategy

Penetration Pricing

- Setting lower than normal prices to hasten market acceptance of a product or service or to increase market share **EXAMPLE?**

Skimming Pricing

- Setting very high prices for a limited period before reducing them to more competitive levels **EXAMPLE?**

Follow-the-Leader Pricing

- Using a particular competitor as a model in setting prices **EXAMPLE?**
- Typically set price as a percentage markdown (or up) based on leader price

Dynamic Pricing Strategy

Charging more than the standard price when the customer's profile suggests that the higher price will be accepted **EXAMPLE?**

- Coke machine in Japan changes prices based on outside temperature
 -
 - If cold – warm drink higher priced
 - If hot – cold drink higher priced
- Coke machines in Japan, Austria, etc take payment via **mobile phone** and include **video**
 -



Selecting a Pricing Strategy (cont'd.)

Price Lining

- Setting a range of several distinct merchandise levels
EXAMPLE?

Variable Pricing

- Setting more than one price for a good or service in order to offer price concessions to certain customers
EXAMPLE of Variable Pricing

Quantcast ..

Video

Spent 9 hours on websites about Portland hot spots over the past 3 weeks

Watched 3 videos on the theory of feng shui yesterday

Read 12 articles on the health benefits of kale and aojiru in the last 6 days


37x increased likelihood of buying an industrial juicer

1400% higher propensity to purchase renters insurance



Selecting a Pricing Strategy

Free Pricing

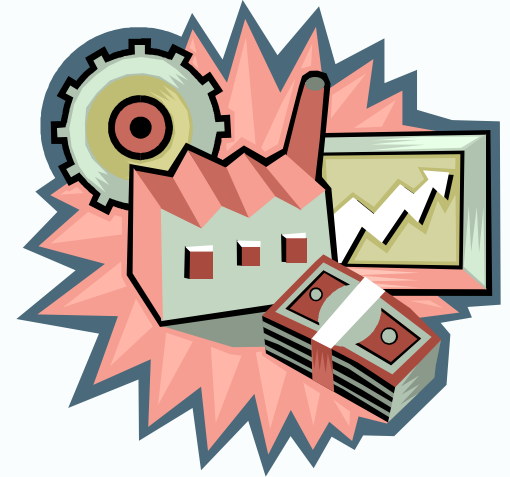
- Ever notice that you can get a printer for **FREE**
- They get you on the ink
- HP info 

	Printer price (1)	Ink cartridge price (2)	Pages printed per cartridge (3)	Cartridge price per printed page (2)/(3)	Ratio (1)/(2)
	(1)	(2)	(3)	(4)	(5)
Home office					
1018 (12ppm; 3000 pages/month duty cycle)	\$130	\$70	1,000	\$0.0700	1.857
1020 (15ppm; 5,000 pages/month duty cycle)	\$180	\$70	2,000	\$0.0350	2.571
1022 (19ppm; 8,000 pages/month duty cycle)	\$200	\$70	2,000	\$0.0350	2.857
Small and medium businesses					
P3005 series ^a (35ppm; 100,000 pages/month duty cycle)	\$549	\$129	6,500	\$0.0198	4.256
4259 series ^a (45ppm; 200,000 pages/month duty cycle)	\$899	\$150	10,000	\$0.0150	5.99
5200 series ^a (35ppm; 65,000 pages/month duty cycle)	\$1,439	\$168	12,000	\$0.014	8.57

^a HP has several printers in a series, generally rising in capability with the printer price.

Offering Credit

- Benefits of Credit to Borrowers
 - Provides working capital
 - Establishment of credit history
- Benefits of Credit to Sellers
 - Facilitates increased sales volume
 - Brings a closer association with customers



Types of Credit

- Consumer Credit
 - Financing granted by retailers to individuals who purchase for personal or family use.
- Trade Credit
 - Financing provided by a supplier of inventory to a given company which sets up an account payable for the amount.
 - Terms of sale may be 1/15, net 30— one percent discount on the invoiced amount if paid in full within 15 days of the invoice date, otherwise the full invoice amount is due in 30 days.

Marketing Strategies

What is Strategy? Harvard's Michael Porter - [film](#)

Now we will develop our Marketing Positioning Strategy

“The unique competitive position we want to achieve. What will our advantage be – cumulatively over time?”

Think of a company that you manage/own or would like to analyze:

What is the **Overall Strategy?**

- **Low Cost** – Low end price
- **Differentiated** – unique from competition

Identify the overall strategy for the firm

EXAMPLES? I chose a barbershop “Jenny’s”

Barbershop – **Differentiated** on specific neighborhood and mid to higher-end haircuts (\$65)

Lets answer a few questions:

What is your company's position?

- Industry Leader (can be just for your niche) **OR**
- Contender
- Small player

What type of industry are you in?

- New and growing industry **OR**
- Maturing industry
- "Mom and Pop" industry

Jenny's Barbershop:

- Industry Leader & Small Player
- Maturing Industry
- Individual Business

How diversified is your company?

- Individual business
- Multiple Businesses with related diversification
- Multiple Businesses with unrelated diversification

Tactics Based on Position

Industry Leader	Contender	Small Player
Attack rivals	Empire builder	Bundling
Build barriers	Niche player	Cost control
Constant innovation	Quality focus	Revenue focus
	Satisfied contender	Niche player
Describe your tactics in a “Position Statement”		

We are an “**Industry Leader**” (for our niche) & “**Small Player**”

Attack rivals - aggressively defend position and differentiation

Build barriers - “brand” key services, add value

Constant innovation - constantly poll customers - innovate

Bundle - add head massage and style consultation to cuts

Cost Control - focus on inventory control

Revenue - add product lines & services to increase revenue per customer

Niche Player - concentrate on our neighborhood / relationships
concentrate on high quality (with value)

Tactics Based on Industry

New & Growing	Mom & Pop	Maturing
Build barriers	Geographic focus	Cost control
Revenue focus	Specialist focus	Current customers
Niche player	Fewer bells/whistles	Empire builder
		Go global
		Quality focus
		Specialist focus
Describe your tactics in an “Industry Statement”		

We are in a “**Maturing**” industry - barbershop:

Cost Control - focus on inventory control

Current Customers - build on relationships

Empire Builder - identify prime locations for expansion

Go Global - develop new products, brand them and sell worldwide on web

Bundle - add head massage and style consultation to cuts

Quality Focus - provide high quality at reasonable prices

Specialist Focus - concentrate on our neighborhood / relationships

concentrate on high quality (with value)

Tactics Based on Diversification

Single business	Multiple related	Multiple unrelated
Do one thing well	Brand builder	Offset opportunities
Quality focus	Empire builder	Profitability focus
Describe your tactics in a “Diversification Statement”		

We are a “**Single business**” - barbershop:

Do One Thing Well - focus on haircuts, hair products and services

Quality Focus - provide high quality at reasonable prices

Create Positioning Statement

Leader & Small Player	Maturing	Single business
Attack Rivals	Cost control	Do one thing well
Bundling	Current customers	Quality focus
Cost control	Empire builder	
Revenue focus	Go global	
Niche player	Quality focus	
	Specialist focus	

Create a Positioning Statement

Select & Combine key tactics – (*Position, Industry and Diversification*)

Check for compatibility and consistency

Example: Key tactics chosen were: attack rivals, bundling, niche player, current customers, specialist focus, and do one thing well, with quality focus

Example: We will continue to differentiate ourselves through aggressive promotion of new bundled service combinations, build customer loyalty through referral programs and sponsorships (sports teams), while using customer information to personalize service, focus on our geographic niche (neighborhood), while we focus only on high-quality haircuts and products
Everyone in the company should align with this statement - [FILM](#)

Positioning Paper

Paper:

- 1. What is strategy?**
- 2. Why is positioning important for a small firm?**

Combination of Tactics – On-Line

Go to: My “Entrepreneur” page, scroll to “Tools & Databases”, then click on the link for “[Positioning Tactics](#)”

Input Screen

The screenshot shows the 'Positioning Tactics' interactive business tool interface. At the top, the Consultapedia logo is displayed with the tagline 'Your Information Source'. Below the logo is a navigation menu with links for 'ENTREPRENEURSHIP', 'GLOBAL BUSINESS', 'INVESTING', 'CAREER', and 'ABOUT US'. The main heading reads 'POSITIONING TACTICS INTERACTIVE BUSINESS TOOL'. A sub-heading says '+ Click [HERE](#) for help'. The interface is divided into two steps: 'Step 1: Identify/Update Position' and 'Results'. Under 'Step 1', there is a 'Name:' label and a text input field. Below the input field is a note: '(Please select all that apply to your firm)'. The 'COMPETITION' section contains three radio button options: 'We are the industry leader / We are the leader in our specific niche area. OR', 'We are not #1 in the industry, nor in our specific niche area.', and 'We are just a small player in the market (less than \$50 million in annual revenue)'. The 'INDUSTRY' section contains three radio button options: 'New & Growing industry. OR', 'Mature industry', and 'Fragmented (Mom & Pop) industry'.

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INTERACTIVE BUSINESS TOOL

+ Click [HERE](#) for help

Step 1: Identify/Update Position Results

Name:

(Please select all that apply to your firm)

COMPETITION

We are the industry leader / We are the leader in our specific niche area. **OR**

We are not #1 in the industry, nor in our specific niche area.

We are just a small player in the market (less than \$50 million in annual revenue)

INDUSTRY

New & Growing industry. **OR**

Mature industry

Fragmented (Mom & Pop) industry

Combination of Tactics – On-Line

Results:

Positioning Tactics - How We Intend to Compete

[HELP](#)

[Step 1](#) [Results](#)

Competitive Positioning Tactics

Prepared for [Name Here]

Complete this process twice annually

[Export to RTF](#) [Mobile to Table](#)

COMPETITION - You selected:

- We are not the leader - we are just one of several competitive firms in our area
- We are also just a small player in the market (even though we may be a leader for our geographic niche)

Tactics that may be appropriate for your company include:

- **Build an Empire:**

This tactic concentrates on "building an empire" through acquisitions of smaller firms. As the company grows, or the industry matures, it may be a wise tactic to continue to grow through acquisitions. Special analysis should be completed to determine the extent of structural and cultural compatibility, such as if they use a shared sales force, technology, supplier base, or distribution system. If a smaller firm has remained small due to certain inadequacies where the company excels, then this tactic might be applicable. If a smaller firm can add operating efficiencies or economies of scale to an organization, then this tactic might be applicable. The company will need to be fiscally fit to consider this tactic. Growth strategies of this sort strive to build economies of scale throughout the organization. This may also be an appropriate option for a firm that has recently "gone public" because it will produce growth.
- **Niche Player:**

This tactic concentrates on identifying and attacking a single segment that was perhaps neglected or ignored by the other major competitors (niche marketing). A firm will often begin exploring this tactic by

Interview Archives – Check it out

Archives with detailed search options for you: [LINK](#)

MT. SAC!
Mt. San Antonio College

Dr. Ralph F. Jagodka
Professor - Business Management

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