

Making The Right Pricing Decisions

By Michael Neidle

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MAKE A PROFIT DON'T JUST SELL

Your objective as a businessman or woman is to make a profit, not to simply make a sale. Anyone can make a sale if their price is low enough, but it takes a business person to make money at it. Profit occurs only when revenue exceeds cost. That may seem to be obvious, but you would be surprised how many personnel services think that by simply getting the order, everything will be taken care of. I've heard the comment many times that "if my competitor can afford to take business at that price, I have no choice but to meet it". The problem is that not all operations have the same cost structure and product mix and what is right for one company might not be right for another. It is also difficult to determine what price to charge in order to make money. Simply put, do what is right for you or you may price yourself right out of business.

KNOW THYSELF

The temporary business has been great, but the high stakes are attracting sophisticated players. You must understand your strengths and weaknesses to be a player now. In fact, your objective should not only be to make money, but to get a decent return on your investment (ROI), one that is commensurate with your hard earned capital, the risk you have undertaken (often even using your house as collateral) and the long hours you put in. Surveys have shown that our industry ranks right up there in ROI, but that does not mean that everyone does well.

If you are large, you may have an "economy of scale" to spread your overhead (i.e. front and back office) and have the buying power to reduce

your outside costs (i.e. insurance and interest rates). This may allow you to be competitive on low mark-up, commodity type jobs. Otherwise, your strategy should be to let your competitors fill up on low end jobs and you should go after the higher mark-up jobs.

KNOW YOUR MARKET

You can't be all things to all people, so concentrate on what you do best.

Light Industrial and Low End Office Services

Light industrial jobs and low end office services often behave as commodities. That is, low prices and low margin % are critical to high volume. It is anticipated that this strategy will yield sufficient margin \$ to offset incremental staff and other fixed costs to still yield a decent profit.

If your strategy is high volume, however, beware of the "Sears Syndrome". This syndrome is where the noted department store became such a large portion of a given suppliers business, that the former was able to squeeze the latter profit margin down to a subsistence level.

Specialty and Boutique Services

Harder to fill jobs, which include specialties and boutique business, involve qualitative factors and personal relationships and typically carry higher margin %. Pricing, while important is far less critical than service, quality, timeliness, etc.

If your strategy is geared to high margin business, beware of becoming marginalized. This is where one works their way into a very attractive niche that may become obsolete, leaving the company up the proverbial creek without a paddle. Technol-

ogy areas fall into this area.

Interestingly, the greatest profit is obtained at neither the highest nor lowest margin %, but at something in between. This is the optimal margin %, the exact value will depend upon the specifics of the marketplace.

EXCEPTIONS TO THE RULE

There are exceptions to the rule in trying to maximize profit, three of which are noted below.

Loss Leaders

This is where you use one portion of your business to subsidize other parts of the company or attract new clients. This may be done by providing low prices on one service, with the anticipation of making it up elsewhere or gaining a foothold with a key client. It is important to monitor your results closely or you may turn your whole company into a loss leader.

Strategic Planning

Here you are making a conscious effort to gain market share and may have to buy your way into the market. If you adopt this strategy, you will need to know when you have achieved your goal and raise prices accordingly.

Defensive Pricing

You may be subject to someone else's strategic efforts to enter your marketplace and you need to defend your market. You may also be pressed to keep your doors open during a business downturn and discount your prices, but know your limitations, including your cash reserves.

LOOKING OUT FOR YOURSELF

Be careful not to price too low, as there are many forces encouraging you into "profitless sales".

The Franchiser

If you are a franchisee, remember that if your agreement is based on sales not margins, it is not important to the franchiser whether or not you make a profit. The greater your revenue the greater their profit, but not necessarily yours. You may even be encouraged to expand

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