HOW TO DETERMINE THE RIGHT RETAIL PRICE FOR YOUR PRODUCT

BC Ministry of Agriculture Marketing Guide Series

Pricing is a Critical Decision

Setting the "right" price is one of the major decisions you will have to make as a small business owner.

When selling to a retailer you will be expected to provide a suggested retail price for your product. It should be competitive, cover your costs and contribute to the growth of your company.

PRICING STRATEGIES

The right price for your product not only covers costs, but also generates a profit and funds to grow your business.

What is the right pricing strategy?

The right pricing strategy is typically a blend of several strategies to achieve balance between costs and value.

Covering your costs is only part of the equation. Pricing should also factor in the value and benefits the product offers, your customers' willingness and ability to pay as well as the value the product provides compared to competitive products.

What is value?

To the retail buyer value may mean a professional marketing plan, guaranteed delivery dates and in-store promotions. To the end consumer value may include local, convenient packaging, environmentally friendly or high nutritional quality.

The following table compares five common pricing strategies:

Strategy	Description	Advantages	Disadvantages	Marketing Tactic
Cost Based Pricing	Costs + profit = price	Works well for companies with higher volumes	Hard for small companies to compete against larger, more efficient companies	Target consumers who buy on price
Break-Even Pricing	Provides minimum quantity required to break-even and cover all costs	Easy to determine provided costs are known	Hard for small companies to compete against larger, more efficient companies	Use to gain market share
Competition Based Pricing	Set price based on competitors' price	Easy to determine	May not cover costs	Use to gain market share
Customer Based Pricing	Price based on customers' willingness to pay	Capture new target markets	Requires investment into market research	Use to access specialty markets; i.e. athletes, special diets
Premium/Value Based Pricing	Differentiate based on higher perceived quality or special features	Opportunity to capture higher prices based on perceived value	Requires investment into market research	Capitalize on trends and perceived value; i.e. people will pay more for local

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Retail is About Margins

KNOWING YOUR COSTS

Business owners must keep track of fixed and variable costs:

Fixed costs: Costs that do not change regardless of the amount of product produced.

Variable costs: Costs that vary depending upon the amount of product produced.

Fixed Costs	Variable Costs
Administrative Expenses	Processing
Payroll (not related to production)	Payroll (Production)
Facility	Ingredients
Equipment	Packaging
Sales and Marketing	Shipping

"HIDDEN" COSTS

When selling to a retailer, you may be faced with a number of additional costs that must be factored into your pricing. Examples are listed below:

Listing Fee or Slotting Fee: a fee charged by the retailer to put your product on their shelf.

- Negotiable between seller and retailer.

Cash Discount: the retailer takes a discount for early payment.

- Example: 2/10 net 30; retailer takes 2% off the invoice when they pay in 10 days, or pays the full amount in 30 days.
- Provides incentive to pay faster but costs you, the vendor, a lot more; a 2/10 discount equates to 37% of sales on an annual basis.

Product Liability Insurance:

- Required by most retailers.

Promotional Allowance: reduced pricing to the retailer to promote product sales.

- Expect to offer reduced pricing three or four times per year.

Tip **Always read the fine print before signing a contract and plan for hidden costs.**

PRICING FOR RETAIL

The retail grocery business is all about margins. Buyers refer to margin percentages which are related to profitability.

MARGIN PERCENTAGE =

PROFIT/PRICE = (PRICE-COST)/PRICE

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Easier to Lower Prices Than to Raise Them

CALCULATING YOUR SUGGESTED RETAIL PRICE

The example below uses cost-based pricing to demonstrate the different layers involved in pricing to the retail trade. While you may not have a broker or distributor right now, you may want to factor these costs into your introductory pricing rather than risk raising prices later.

Category	Example	Formula	Pricing Layers
Your cost	$2.00	n/a	n/a
Your margin	15%	n/a	n/a
Your revenue	$2.35	=2/(1-0.15)	$2.35 (cost to broker)
Broker fee (typically 3-10%)	3%	=2.35/(1-0.03)	$2.42 (cost to distributor)
Distributor margin (typically 25 – 30%)	25%	= 2.42/(1-0.25)	$3.23 (cost to retailer)
Retailer margin (typically 35-40%)	35%	= 3.23/(1-0.35)	$4.97 Suggested Retail Price

There are many margin calculators available online. Search for margin calculators or profit margin calculators.

What happens if your suggested retail price is too high?

If your suggested retail price is too high the retailer may not list your product. A product listed at a high price may not sell resulting in it being delisted.

Should your price be higher than competitive products make sure to examine your costs and identify savings opportunities or find ways to build value to differentiate your product from the competition.

Tip **Differentiate your product from others by emphasizing your unique company story, the use of high quality local ingredients etc..**

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Differentiate Your Product

THINGS TO THINK ABOUT WHEN SETTING YOUR PRICE:

Getting your product onto the retail shelf is only a start.

Getting it into consumers' carts is also your responsibility. In-store demos, social media campaigns and special promotions all need to be factored into your costs.

Selling retail <u>and</u> direct-to-consumer?

You risk putting your relationship with your retailer at risk if you sell the same product directly to the consumer (e.g. e-commerce) at a lower price.

Your direct-to-consumer price should be similar to the retail price or you should differentiate your product so the consumer sees it as a different product. For example make a 6-pack for retail and a 10-pack for online sales.

PRICING FOR OTHER DISTRIBUTION CHANNELS

The pricing strategies and principles for retail can be applied to other channels as well.

Your pricing strategy is a critical component of your company's overall marketing plan. For more information see the Ministry of Agriculture's guide on "How to Develop and Use a Marketing Plan".

MORE INFORMATION

See the Ministry of Agriculture's Marketing Guide Series for more information and additional topics by visiting http://www2.gov.bc.ca/gov/content/industry/agriculture-seafood/statistics/market-analysis-and-trade-statistics