

Pricing Practice (margin pricing)

- It costs \$57 to create your product
- The monthly fixed costs are \$15,000
- The retail margin you want is 18%

Figure the retail price...

$$\text{Retail price} = \frac{\text{Cost}}{1 - \text{Desired return}}$$

$$\text{Retail price} = \frac{\$57}{1 - .18}$$

$$\text{Retail price} = \frac{\$57}{.82} = \$69.51$$

Let's check it...

$$\$69.51 - 18\% = 56.998 \text{ or } \$57$$

Pricing Practice (markup pricing)

You have purchased a product line that cost you \$219 each. Your company uses a mark-up pricing model of 30%. What is the retail price of these products?

Cost is \$219 and you wish to add a 30% markup to determine the retail price.

$$219 + 30\%$$
$$(30\% \text{ of } 219 = 65.70)$$

So...

$$\$219 + \$65.70 = \$284.70$$

The price would be \$284.70

Pricing Practice (Break-even)

- Consider the first item we calculated, it costs \$57 to create your product
- The monthly fixed costs are \$15,000
- The retail markup you want is 18%
- Now we know the retail price is \$69.51

Computer the break-even...

$$\text{Break-even} = \frac{\textit{Fixed costs}}{\textit{Price-Variable Costs}}$$

$$\text{Break-even} = \frac{\$15,000}{\$69.51 - \$57} = \frac{\$15,000}{\$12.51}$$

$$\text{Break-even} = \frac{\$15,000}{\$12.51} = 1,199 \text{ units}$$

Pricing Practice (elasticity of demand)

- At \$69.51, you sold 185,000
- When the price was raised to \$79.99, you sold 153,000

Should you raise the price more, keep it the same, or reduce it?

$$\text{Elasticity} = \frac{\text{Pct. change of Quantity}}{\text{Pct. change in Price}}$$

$$\text{Elasticity} = \frac{185,000 - 154,000}{\$79.99 - 69.51} = \frac{31,000}{\$10.48}$$

$$\text{Elasticity} = \frac{31,000/185,000}{\$10.48/69.51} = \frac{16.7\%}{15.1\%} = 1.11$$

It is over 1, so it is elastic.

Check it...

$$185,000 \times 69.51 = \$12,859,350 \text{ (old revenue)}$$

$$154,000 \times 79.99 = \$12,318,460 \text{ (new revenue)}$$

The new pricing brings in lower revenues. That's bad.
You should reduce the price.

Doesn't raising your price always mean fewer sales? Usually, but fewer sales does NOT always mean lower revenues

- At \$69.51, you sold 185,000
- When the price was raised to \$74.99, you sold 173,000 (again, demand dropped)

Is this demand elastic or inelastic?

$$\text{Elasticity} = \frac{\text{Pct. change of Quantity}}{\text{Pct. change in Price}}$$

$$\text{Elasticity} = \frac{185,000 - 173,000}{\$74.99 - 69.51} = \frac{12,000}{\$5.48}$$

$$\text{Elasticity} = \frac{12,000/185,000}{\$5.48/69.51} = \frac{6.5\%}{7.8\%} = 0.83$$

It is under 1, so it is IN-elastic.

Check it...

$$185,000 \times 69.51 = \$12,859,350 \text{ (old revenue)}$$

$$173,000 \times 74.99 = \$12,973,270 \text{ (new revenue)}$$

The new pricing bring is higher revenues. That's good.

As long as the elasticity of demand is under 1—raise your price.

Forward Pricing

Your product that costs you \$9.80 to produce. You know the wholesaler's markup is 40% and the retailer's markup is 22%. What will be the like retail price of your product if you sell it to the wholesaler for \$20?

Forward Pricing

Your price to wholesalers is \$20. They want to add 40% to it. What is the price the wholesaler will charge to the retailer?

Price to wholesaler = \$20

Wholesaler markup = 40%

40% of 20 is \$8.00

So...

$$\$20 + 8 = \$28$$

Forward Pricing

The wholesalers' price to retail was \$28. They want to add 22% to it. What is the price the retailer will charge to the consumer?

Price to wholesaler = \$28

Wholesaler markup = 22%

22% of 28 is \$6.16

So...

$$\$28 + 6.16 = \$34.16$$

Using odd-even pricing, to show that this product is a good deal, what is the likely retail price?