

Exercise 8a: Figure out how much to charge for your product

Almost every new entrepreneur starts by selling their product at the same price as their competitors. This is a good idea since the other businesses have figured out how much people are willing to pay for the product or service.

If you have a product or service that nobody else in your community or a community nearby offers, there are a couple of ways to help you decide what to charge. The two most common ways to decide on a fair price are:

1. Survey potential customers and ask how much they'd be willing to pay for your product or service.
2. Use the "cost approach" which requires doing a good amount of math. The upside to this approach is that it will tell you exactly how much it costs to produce your product so you'll know how much you're earning for yourself when you sell it. It will also tell how much you can reduce your price in a sale and still make money.

Competition or market price?

1. Using the phone book, the internet, word of mouth and going into shops in your community, identify all of the companies that offer a product or service similar to yours.
2. Call all of the competition and ask how much they charge for a product or service that is like the one you will be offering.
3. Write this information down to see what the range of prices is.
4. See if you can figure out why some of your competition charge more than others. What do they offer that makes their product or service worth more than others offering similar items?

5. Using this information, write down a price range for your own product or service and what you'll provide that will make your offer the best and most desirable deal in town.

Cost Approach

This approach may take more work but it is the very best way to set a price that will guarantee you're making money with every sale.

1. Calculate all of the costs related to producing your product or service.
2. Figure out how much time it takes you to make one item.
3. Set a pay rate for yourself, based on how much you'd like to make an hour.
4. Multiply the time it takes you to make one item by the fee you want to earn to get the cost for labour for your product or service.
5. Add operating costs, which may be tricky at first since you might not know what these will be. Operating costs are the money you pay for business cards, phone, an office if you have one, etc. You have to guess at how many items you'll make in one month or year, and then divide your total operating cost by that number.
6. Add #1 (cost of one item) plus #4 (pay you want for making one item) plus #5 (a percentage of your operating costs). That will give you the minimum amount you should charge for your product or service.

For example, if you have a service-based business, this is how you'd figure out how much to charge:

How much does it cost to do the job?

What gets paid for	How much?	Why that amount?
Cost of materials for one job	\$ 0	the client will pay for materials (as in a repair person, for example) there just are no costs (service provider, for example)
Cost of labour for one job	\$ 100	based on estimating 4 hours of time to complete the job at \$25/hour
Direct operating costs	\$ 5	percentage of cell phone used for business
Total cost of goods sold	\$ 105	

Now try this for your own business!