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Entrepreneurship & Startup › Business Models & Strategy › Revenue & Pricing Strategy

Cost-plus pricing

Cost-plus pricing: Simple, straightforward, and effective for profit margins.

DEFINITION

> Cost-plus pricing is a pricing strategy where a business sets prices by adding a markup to the cost of producing a product. This ensures all costs are covered while achieving a desired profit margin.

KEY CONCEPTS

Cost Calculation

Accurately determining the total cost of production, including materials, labor, and overhead.

Markup Percentage

The percentage added to the total cost to determine the final selling price.

Profit Margin

The difference between the selling price and the cost, expressed as a percentage of the selling price.

Market Considerations

Understanding competitor pricing and market demand is crucial to set competitive prices.

Simplicity

This method is easy to calculate and implement, making it popular among small businesses.

EXAMPLES

→ A furniture maker adds 30% to the total cost of materials and labor to set prices.

→ A bakery calculates total costs of ingredients and labor, then adds a 50% markup.

→ A clothing retailer determines costs and applies a 40% markup for retail pricing.

MEMORY TIPS

★ Think 'Cost + Markup = Price' to remember the basic formula.

★ Visualize a pie: the cost is the base, and the markup is the slice added on top.

★ Remember 'C+M=P' where C is cost, M is markup, and P is price.

COMMON MISTAKES

✗ Neglecting to include all costs, leading to underpricing.

✗ Setting a markup without considering market conditions.

✗ Failing to adjust prices when costs change.

QUICK RECAP

Cost-plus pricing is a straightforward method where businesses add a markup to their costs. It ensures profitability but requires careful cost calculation and market awareness.