Determining Your Minimum Selling Price

Follow these pointers and you won't sell yourself short. If you are operating a sole proprietorship or a partnership in Canada, do you know the lowest price you can charge for your product or service without losing money?

Essentially, the Minimum Selling Price (or Break Even Point) is calculated by adding your Variable Cost per Unit to your Overhead Burden per Unit, then adding your Profit Margin per Unit. To find the Break Even Point for your product, grab a calculator and work through the following steps:

1. **Determine your Total Productive Time per Year.**
   This is the number of hours that you, your partner and your employees will realistically devote to your business. Identify the number of weeks per year you will work at the business, and the number of hours per week that you will work. When calculating the number of weeks that you will work, remember to allow for holidays, vacations and sick time.

2. **Identify a unit.**
   If you are selling a service, the unit may be an hour of your time. If you are selling a product, a unit could be one book, one software application, one training workshop, one gift basket, etc.

3. **Divide your Fixed Costs per year by the Total Productive Time per Year to arrive at your Overhead Per Hour.**
   Your Fixed Costs are the sum total of what it will cost you to run your business for one year. Do not include the cost of capital assets such as equipment or real estate. Include office rental, office expenses, business travel, telephone, Internet, advertising, automobile, skill development, publications, business entertaining, bank charges, insurance, legal and accounting fees, licenses, salaries, etc.

   Estimate every business expense that you will incur for the following year, then decide on your Management Draw. Your Management Draw is the wage you pay yourself for running the business. If your total Fixed Costs, including Management Draw, come to $50,000 per year and your Total Productive Time Per Year is 2000 hours, your Overhead Per Hour will be $50,000 / 2000 = $25.

4. **Determine your Overhead Burden Per Unit by multiplying your Overhead Per Hour by the Number of Hours to Produce One Unit.**
   If your Overheard Per Hour is $25, and it takes two hours to produce one unit, then your Overhead Burden Per Unit will be $50.

5. **Calculate your Minimum Selling Price Per Unit by Adding your Variable Cost Per Unit to your Overhead Burden Per Unit and then adding your Profit Margin Per Unit.**
   To calculate your Variable Costs Per Unit, identify the costs that are specific to producing one unit. If your unit is a gift basket, you will need to consider cost of baskets, contents, decoration, delivery, etc. Suppose your gift basket costs you $30 to assemble. Now you must decide what profit margin you want to include.

   Your business requires profit beyond your expenses and Management Draw, since you will need funds to repay investors or loans, funds to purchase capital assets and funds for future growth. Let's say you decide you want 20 per cent profit per unit. Your combined cost per unit will be $50 + $30 = $80. Adding 20 per cent profit brings it to $80 + $16 = $96.

   This tells you that you will lose money at anything less than $96 per unit. If your market research indicates that customers won't pay this amount, you will need to find a way to reduce expenses or to add perceived value to the product without adding to the cost.

This article is part of the Marketing Plan Toolkit.

Next article in the Toolkit
Back to the Marketing Plan Toolkit page

About the Author: