



## THE BENCHMARK

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# Price smart to win, keep business

**P**rice competitiveness is a function of cost control and revenue generation. Cost control is a function of personal productivity (revenue per employee must increase). Revenue generation is a function of price and pressure (labor rate/price per hour must decrease, and we must be more aggressive in our sales closing efforts). Both strategies must be employed simultaneously.

Price reductions can be achieved to win and retain work; this is an essential element of the revenue-generation strategy.

Using Table 1, we start at the bottom with several givens: our current average wage rate (\$11.67, including taxes) and the net profit dollars (\$100,000) we need to earn.

Next, we budget just to maintain general and administrative (G&A) cost at current levels (\$300,000, which includes overhead for staff, who will be required to do more) while we make some

room for slight increases in indirect cost necessary for expanded sales at reduced pricing (\$170,000, which includes some increases for additional equipment to do the work).

We next incorporate market/customer feedback that is telling us that at 55% gross margin, we are “too expensive” (relative to competitor prices), and further we know that we are losing work and winning business at rates insufficient to cover the losses.

This is where industry benchmarks and trial-and-error budgeting are useful. If we are consistently 20% too high in our bids on an “apple-to-apple” basis, the gross margin must be reset to achieve this differential in labor rate/price.

Using a 48% gross margin projection achieves the 20% differential and reflects the trend in current benchmark gross margins in maintenance.

### The real price to pay

As a result of using Table 1’s pricing strategy, we would sell labor at \$25 per hour instead of \$30 per hour — 20% less. In exchange for this “pricing concession” to the market, the company would have to generate an additional \$187,500 in revenues without increasing overhead staffing.

Labor staffing will, of course, increase by the difference between Last year’s 30,000 hours and This year’s 42,750 hours.

Keep in mind this analysis provides a static example only. Real-world pricing is much more dynamic.

In the real world, you should end up pricing some jobs at the current \$30 per hour because you know you can get that price. But it’s also essential to know that you can price at lower/more competitive rates in select situations when you need to retain business or win new work — and still make your bottom line. All this requires is:

- › knowledge of the math;
- › cost control; and
- › the steely nerves of a true sales professional.

TABLE 1: PROFIT & LOSS STATEMENT

	Last year	This year
Revenues	\$1,000,000	\$1,187,500
Labor	\$350,000	\$498,750
Material	\$100,000	\$118,750
Direct cost	\$450,000	\$617,500
Gross profit	\$550,000	\$570,000
Indirect cost	\$150,000	\$170,000
G&A cost	\$300,000	\$300,000
Net profit	\$100,000	\$100,000
Labor hours	30,000	42,750
Average wage rate	\$11.67	\$11.67
Labor rate/price	\$30	\$25