



THE BENCHMARK

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The power of pricing

There is still a lot of gnashing of teeth about market pricing. I showed a chart at a recent Professional Land-care Network (PLANET) event that reported mowing prices in different regions of the country and what the average gross margin is at each price (see Table 1). The table details actual data we collect on pricing. It does not recommend a pricing strategy, nor does it suggest that this is the “right and fair” price. It simply reports what is happening and provides a benchmark for contractors.

The gnashing of teeth part is that some suggest that these numbers cannot be true — and if they are, then people must be “giving it away” and selling below cost. Certainly, some contractors are pricing some jobs very low some of the time, but *all* contractors pricing *all* jobs below cost all the time? This is simply not happening. Anyone practicing this strategy would soon be out of business.

TABLE 1: MOWING RATES VS. GROSS MARGINS

AMR	AGM
\$30	51%
\$28	49%
\$25	47%
\$23	45%
\$21	44%
\$19	42%

This table shows what a contractor's average gross margin (AGM) would be at a given average mowing rate (AMR).

TABLE 2: PROFIT PERCENTAGE

Two contractors in different regions offer a very different price for the same service and still make the same profit percentage.

Benchmarks/Calculation	Florida	Illinois
A: Crew average wage rate (data)	A: \$11	\$14.50
B: Price per hour charged (data)	B: \$19	\$28
C: Gross margin (A-B)/A	C: 42%	48%
D: Indirect/equipment cost as percent of revenue*	D: 16%	22%
E: Contribution to overhead (C-D)	E: 26%	26%

* Differences between this cost between the South and the North are due to:

- **Seasonality.** In Florida they mow all year long and get revenue all year long.
- **Equipment type.** In Florida they do not need to equip for snow and thus the heavy (and more expensive) vehicles required for snow removal.
- **Environment.** Because the weather is milder, the heavier equipment lasts longer.

Some explanation is in order, however, to explain pricing differentials. Table 2 shows how two contractors in two geographic markets can arrive at a very different price for the same service and still make the same profit percentage. In this very real example, the respective contractors each make a 26% contribution to overhead.

Is someone crazy like a fox here? Maybe. But this is what Milton Friedman meant when he said there are no free lunches. Markets find equilibrium, making certain that the grass is rarely greener on the other side — nor the profit higher (at least for very long).

It simply turns out that the firms charging \$19 per hour in Florida are charging what other firms in Florida are charging, based on their very similar cost structures. At the same time, it is also true that firms in Illinois that decided to charge \$19 per hour would not last very long, because they have a very different and higher cost structure.

Let's face it: We are in an economy where the customer has pricing power, not us. If we continue to approach pricing with old estimating methods and production standards, we are missing the boat on price. For example, let's compare two contractors in the same market.

Say one contractor bids 20% fewer hours, and the customer saves 25%. Is he giving it away? Not if he can do it in four hours on every mow, just as he estimated.

So, from whom would you purchase? Pricing pressure is a fact of life almost everywhere. Every year, manufacturers routinely go to their vendors seeking price concessions. Why? Because they can! They have the power. The smart vendor, instead of howling at the moon about low pricing, buckles down with his people in the factory and figures out how to make the widget more cheaply. This is a very good idea that will help us survive now and prosper greatly when the economy eventually improves, and power of price shifts back to us. This *will* happen, just as surely as the sun rises every day.