

# Back to Business...

## Small Business and Pricing



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One of the most difficult issues that every business owner must face is how much to charge for a product or service. This question is far more complex than it appears on its face. Let's look at the potential issues that go along with charging either too much or too little.

**It is a given that it is very difficult to make a profit in a company at any given point in time, the first reaction many business owners have is to raise the price.** However, the negative to raising prices is the possibility of declining sales. As everyone understands, declining sales means that fixed expenses, as a percentage of total revenue increased, cause bottom line profitability to be reduced. In addition, a negative associated with raising prices is increased competition, such as more competition with goods and services sold at a given price than what there were at originally.

**Although it seems like the opposite should be true, raising the price actually reduces cash flow. The reason for reduced cash flow is that if the product price and service charge is increased, it will be more difficult for the customer to pay for the product.** Therefore, the number of days that they take in order to pay for the product or service will escalate.

The advantage to a price increase is, theoretically, an improvement in bottom line profitability, but only if you maintain control over revenue as the price is increased. On the other hand, if it seems like

not enough revenue is being produced and/or not producing enough profit, many business owners believe that the right approach should be to reduce price. The negative to a price decrease is that it reduces your bottom line profitability—based now on charging less and having the same basic costs as when the price was higher. The advantage, of course, would be increased revenue.

**Thus, we come back to the on going problem of whether to be a revenue-producing company or a profit-driven company.** Every entrepreneur initially believes that producing revenue is one of the key components of success. I would challenge every one of those entrepreneurs, and rather, would set forth that the key consideration is to develop a business that is not resistant to profit, but that employs profitability as the first item of expense. In addition, make sure that the product or service offered is second to none as it relates to quality. Make sure your product or service stands out and adds value to your clients.

If a business is built upon the quality of the product or service being extremely important, coupled with maximizing profitability, then the probability of the business being successful in the long term increases dramatically. If on the other hand, the focus is on driving revenue only and not on controlling critical variables and maximizing profitability, what we end up with is a company that generates substantial revenue, but has severe cash flow problems and produces very little profit, then what good is it if any. That has never been a model proven to be successful. It is important to have the mind set that you are building something for the long term. Yes you need to manage the business day to day but you must have a mindset of long term viability. Even the big corporation was once

small and gradually over time grew to become big.

As we look at the overall economic conditions in America at the moment, businesses are still perplexed by the age old question, "Should revenue or profit come first?" I implore every one of you to look yourself in the mirror and demand of yourself not increased revenue, but increased profitability. This is especially important if the business in its infancy stage. What can you do to increase the bottom line and control costs? What can you do to build a business that will be a lasting legacy to yourself for the rest of your and your family's lives? How can you make sure that

this business will survive through your lifetime and after in order to protect each individual who comes into contact with it? That includes not only yourself and family, but also your clients, customers and vendors. If in fact the company is profit-driven rather than revenue-driven, then it ensures that every person who comes into contact with the business is better protected.

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