



UNIVERSITY OF MINNESOTA EXTENSION

PRICING FOR PROFIT

PRICING BASICS AND STRATEGIES
FOR FARMERS MARKET VENDORS

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table of contents

1. Pricing Basics
2. Identify your Niche
3. Define your Strategy





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University of Minnesota Extension has assisted farm operators for over 100 years to better raise and market crops and livestock. As an Extension Educator, I've had the privilege to work with hundreds of farmers to sell their goods directly to consumers.

I'm happy to share the combination of this knowledge together with my own direct experience over 20 years as a commercial vegetable operator myself.

This workbook will focus on the basics of pricing your products at a farmers market and provide the space for you to start thinking through your own pricing strategy.

LET'S DO IT!



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01

PRICING BASICS

Whether you are selling shoes or artisan bread, the first step is to learn the fundamentals including the common strategies businesses employ.

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Pricing Basics

Pricing can be more art than science. Even small changes in price can convey a different value to your customers and make the difference between a product slowly wilting away on the farmers market table or languishing in the freezer on the farm and one that customers eagerly snatch up.

“The farmer is the only man in our economy who buys everything at retail, sells everything at wholesale, and pays the freight both ways.”

President John F. Kennedy

Common Pricing Strategies

A pricing strategy is simply an intentional approach to guide how to price your products. Your purpose ought to drive the strategy and is often associated with where you stand in your business lifecycle or the lifecycle of the product. New operators are often looking for ways to find and grow a customer base, whereas established businesses often search for ways to incrementally maintain or improve profit margins while keeping their customer base.

Relative Pricing

Probably the most common pricing strategy, especially for new and beginning operators. You base your price on the prevailing price in the marketplace for a comparable product, that is, you set your price in relation to others to be competitive. You may choose to set your price 5% or 10% above or below the average but remain competitive. This is a straightforward approach but you must take on a quick assessment of your competitors first (see competitive analysis activity below).

Cost-plus Pricing

To truly know whether your price will provide you with a profit, you should base the price off the total cost of production and apply a margin. Retail stores which buy in products (called cost of goods) all have standard margins for departments based on their industry. For example, food service in a grocery store commonly stands at a 50% margin whereas refrigerated grocery products sit at a 25-27% margin. This margin must be high enough to cover all costs for retailers over the cost of goods from labor to marketing and other overhead costs like rent.

Unlike retailers, however, you are not simply purchasing a good, but producing it yourself. Whereas a retailer has a cost of goods, you first need to calculate a cost of production before you can employ cost-plus pricing. To calculate a price based on a margin, use this formula:

$$\text{Price per unit} = \text{cost of production per unit} / (1 - \text{margin})$$

For example, you know it costs you \$2.50 per pound of finished pork to raise hogs. You apply a 40% margin to cover your labor, overhead costs, and provide yourself a profit. Therefore, you would calculate $\$2.50 / (1 - 0.40)$ for an average price of \$4.16 per pound across all cuts. You would more than likely round this up for high value cuts and down for basic or highly competitive cuts. These price points would be informed by your relative price research.

Penetration Pricing

The idea behind penetration pricing is to set a price lower than competitors to gain customers. This can be used by new operators who need to build a customer base or to bring sales to a new product with a lot of competition in the marketplace. The challenge, however, is that this type of pricing can create enemies of competitors and possibly spark a price war. Customers may also perceive your products as low value or quality simply due to the low price.

Skim Pricing

This strategy is to set a high price for a product for a high profit. This makes sense to use with niche products that are uncommon in the marketplace or trendy and in demand. When some Midwestern growers first got into growing ginger, for example, they had an opportunity to skim price the product. Likewise, with Wagyu beef or other specialized high-value meat products. The challenge, however, is that this kind of pricing attracts competitors, which, in turn, will bring down the prices. Furthermore, setting a high skim price may affect your overall sales as customers perceive your business as expensive on all the things you sell.

Variable Pricing

With variable pricing, the prices you set will fluctuates based on the time of day or time of season. For example, pricing tomatoes higher at the beginning of the season and lower at the end. This strategy can frustrate customers or train them simply to wait for your fluctuating prices to fall before purchase. Finding a way to sell off a large supply of products is absolutely necessary. A smarter approach is to find another set of customers to sell discounted products to

rather than cannibalizing an existing market. For example, you would do well to hold your price constant at a farmers market and sell excess volume at a discount directly from the farm to a list of local customers.

Tiered Pricing

The model of tiered pricing involves setting prices based on the features, benefits, or level of service offered. The most common tiered prices for farm operators are having different retail and wholesale prices. A tiered pricing can also be done with retail customers where you offer a lower price per unit for a greater quantity. For example, a CSA delivery per week can be lower for customers who join for the full 20-week season instead of an every-other-week shareholder.

Pros and Cons of Pricing Strategies

Pricing Strategy	Advantage	Challenge or Risk
<i>Relative</i>	Easy to implement, keeps you competitive	Prevailing price may be below your costs
<i>Cost-plus</i>	Based on your costs - clearly profitable	Can be difficult to identify if you have many products or are new to business
<i>Penetration</i>	Can attract customers and pull them from existing businesses	You attract customers only looking for deal, give perception that products are low quality, anger competitors, price does not cover costs
<i>Skim</i>	High profit, set perception of high value	Will attract competitors, could create price perception of too expensive
<i>Variable</i>	Tactical way to move produce in high supply	Can frustrate customers or cause them to wait until price drops
<i>Tiered</i>	Provide different prices for different customers	Must manage multiple price schemes and requirements



02

IDENTIFY YOUR NICHE

Now that you've got a handle on the big picture of pricing strategy, it's time to take a fresh look at what you sell. Identify your customers and where your product fits within the marketplace.

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Identify your Niche

Where you choose to set your prices and even which products you choose to sell are driven primarily by customer base and competition. You must have some idea of where you stand in the marketplace. Do you have a competitive advantage over others? What kind of customers are you selling to? What are their primary concerns, values, and wants?

A quick examination of your customers and the competition can help you find your niche.

Know your Customers

Successful marketing derives from knowing your target customer. Customer segments are groupings of customers based on defining characteristics such as interests, shopping habits, and demographics. The purpose is to have an image of customers you are trying to serve to better tailor your product offerings, marketing messages, and pricing. If the bulk of your customers are price sensitive and traditional 'meat and potatoes' women over 70, your trying to sell only trendy and high-priced microgreens would be futile. Other customers may love the microgreens, however you would do better to at least offer some staples in your product mix such as competitively-priced red potatoes and standard bi-color sweet corn.

Activity: Customer Segments

Fill out the following table to ID your top three customer groups or approximate them for your area if you are just starting out. Provide a name such as Minivan Moms or Volvo-Driving Professionals and sketch out the primary traits as customers, including basic demographics and interests. Most importantly, identify their shopping habits.

Segment Name	Demographics (age, education, income)	Price Sensitivity	Shopping Habits or Interests
Example: Minivan Moms	Late 20s into early 40s with kids	Medium, but like bulk deal	In hurry, buy staples, want kids to eat healthy, farmers market a good outing for family

Next, reflect on how best to serve each of your customer segments. Identify products of interest, price points, and marketing messages to best reach them.

Segment Name	Ideas on how best to serve them
Example: Minivan Moms	<u>Pricing</u> – give bundle price, weekly bulk pricing. <u>Message/promotion</u> : “From our family to yours, farm fresh for your family”... web saavy – use text updates? Pre-orders online? <u>Product mix</u> : provide staples in good portions for reasonable price, maybe a package/bundle deal.

Activity: Competitive Analysis

Look for comparable products in the local marketplace and record their pricing and any notes about their quality and how they sell their product. If you are planning on selling at a farmers market, you must know the going price there, but also in other stores and sources where your customers are shopping.

For example, if you are looking to sell salad mix, what is the most popular size of package? Is the quality similar? Are competitors certified organic? What are their marketing messages on the package?

Competitor	Price	Packing Size	Quality or other Notes

After a look at relative prices and others selling a similar product, where do you think you should set your own pricing? You need not feel compelled to match a competitor but find a 'sweet spot' that makes sense for you. If you feel your quality is head and shoulders above the competition, you may decide to price higher than others, but keep competitive at no more 10% over others.

Ideally this exercise will also inform how your pack and merchandise your product, provide you ideas on messages you want to emphasize or packing size, quality, or labeling that will help you stand out of the crowd.

03

DEFINE YOUR STRATEGY

Pick a direction. You have thought about your market, your niche and costs. Now is the time to land on an approach to try.

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Your Pricing Strategy

Let’s bring this work together to set your approach to pricing.

Hopefully the customer and competition activities provided you with some insights into where to set your prices. The trick is to carve out a place where you stand out in the marketplace and serve as many of your target customers as possible.

Although price is important, please note that price is not everything. Research shows that food customers rank price highest, although they also rank other factors high including health, taste, time, and quality (Fox et al, 2021).

What's your overall goal for the next year (sales, profitability, get started)?

With your customers and competition in mind, what's your pricing strategy?

This can drastically range from a simple pricing strategy for a single product to a sophisticated mix of pricing strategies across multiple market channels.

Product or Market 1:	Product or Market 2:	Product or Market 3:
Typical Price Range:	Typical Price Range:	Typical Price Range:
Competition for my product(s):	Competition for my product(s):	Competition for my product(s):
My approach:	My approach:	My approach:

How will you communicate about your prices and products to customers?

Action Steps: List the next three items you must do to implement your strategy:

1. _____
2. _____
3. _____

Works Cited

Fox, E. L., Davis, C., Downs, S. M., McLaren, R., & Fanzo, J. (2021). A focused ethnographic study on the role of health and sustainability in food choice decisions. *Appetite*, 165: 105319. <https://doi.org/10.1016/j.appet.2021.105319>

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