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Pricing Horticulture Products

Setting a price for your products is one of the hardest parts of running a horticulture business. The price has to be low enough that your customers see value, but high enough that you earn a profit.

If you set the price *lower* than what consumers are willing to pay, you could be leaving valuable revenue on the table. If the price is too *high*, you may struggle to sell your product.

This factsheet explores **four issues to consider** when pricing your fresh fruits and vegetables, culinary herbs, bedding plants and fresh-cut flowers.

- How to calculate costs and profitability for your product
- The market channel(s) that best match your business goal
- How knowing your competitors can help you set a price
- How consumer demand affects the price of your product

How to calculate the cost and profitability of your product

The cost incurred to produce the product is just the beginning. When determining your product's price, include *all* your costs, even your business overhead costs. Most of your costs will fall into two categories: variable (direct and indirect) and fixed.

Variable costs

For variable costs, include those expenses that change with the number of units made or grown. For some of the costs, you will see a direct relationship to the number of units made or grown while for others, the relationship may not be quite as clear.

These costs include (but are not limited to) the following:

- seed, fertilizer, water, plant cuttings
- packaging costs such as boxes, bags, labels
- shipping and/or transportation
- labour costs you pay people to grow, package or sell the product, for example:
  - yourself or family members
  - contract/seasonal employees
- marketing costs (advertising, price lists, recipe cards)
- display costs (tables, tent, booths, and signage)

Most of your costs will fall into two categories: variable and fixed

Fixed costs (overhead)

Fixed costs include expenses that do not change from month to month. The costs occur no matter how many units are made or grown.

These costs include (but are not limited to) the following:

- land and equipment expenses
- building or facility costs
- insurance (building or liability)
- utilities
- management salaries

Note: it does not matter which category you put a cost in as long as you account for all your costs.

Cost of Production = Variable Costs (direct and indirect) + Fixed Costs

Understanding your break-even point

A break-even point is a standard calculation in business used to discover the point where costs are covered by a certain price and volume. The break-even point is the price at which there is neither a loss nor a profit from the sale of your product.

For this break-even example, you will need to know the cost to produce one unit of product (variable costs), plus what your monthly business costs are (fixed costs).

$$\text{Break-even point} = \frac{\text{fixed costs/month}}{\text{unit contribution margin}}$$

Remember, this example is intended to show the process, and your numbers will vary depending on the type of product you offer and your own costs.

Break-even Scenario

Mary's Better Berry Farm produces berries for sale at a local farmers' market. Mary has added up all her costs related to one basket of berries (variable costs) and found it to be $2.50 per unit, not including her monthly business (fixed) costs.

She wants to set her price for one basket of berries at $4.00.

How many units will she need to sell to cover her monthly fixed costs and break even?

She will subtract her variable costs per unit from her selling price to see how much one unit will contribute towards covering her fixed costs.

Unit contribution = $4.00 - $2.50
= $1.50 per basket

Unit contribution margin = sale price - variable costs

So, each basket of berries contributes $1.50 towards covering the monthly fixed costs of Mary's business.

Mary's Better Berry Farm has $1,425 per month in fixed costs for the berry operation.

Break-even in units = $1,425 / $1.50 = 950 baskets of berries

To break even (have no profit), but cover all her costs (variable + fixed) by selling the baskets at $4.00 each, Mary's Better Berry Farm must sell 950 baskets of berries each month.

Break-even analysis can also help you analyze how a price change affects your business. Using the same example, Mary sells her baskets for $5.00 each. Here is what happens to the number of baskets she needs to sell to cover the same costs and break-even:

Unit contribution = $5.00 - $2.50 = $2.50 per basket goes towards covering Mary's monthly fixed costs

Mary's Better Berry Farm has $1,425 per month in fixed costs for the berry operation.

Break-even in units = $1,425 / $2.50 = 570 baskets of berries

A higher price of $5.00 per basket will mean she can sell 380 fewer baskets (950 - 570) per month and still break even, compared to selling at a lower price of $4.00 per basket.

You can use break-even analysis before you plant a new crop or try a new bedding plant variety to be sure the new product will generate enough income to cover the costs of your business.

How do I calculate my profit goals?

Covering your costs is an important starting point. Making sure you earn sufficient profit to ensure your business thrives is the next critical step.

You can set your profit goals as a percentage above the cost of the product, or you can set a total profit figure for the entire business. Make sure you are familiar with the product price range in your industry, so your profit goal is suitable for your horticulture products. You will need to balance your profit with a price that consumers see value in.

This next example shows profit as a percentage above cost, using an example of a wholesaler of cut flowers. Typical retail industry margins in Alberta for this type of product are between 30 percent and 40 percent.

Profit as percentage

Sue grows greenhouse cut flowers. She found two gift stores that want her cut flowers. The first store wants a 30 per cent margin and will price the flowers at $5.00 per bunch; the second store will set the price at $6.25 per bunch and wants a 40% margin.

How can Sue figure out the best wholesale price she will receive?

Since Sue knows the selling price and the margin, she can calculate the price she will receive by using the following formula:

selling price / mark-up factor* = cost to producer

$5.00 / 1.429 = $3.50   OR $6.25 / 1.667 = $3.75

* Sample margins converted to mark-up factor are listed in the table below. For this example, find the margin percentage (30% or 40%) in the first column, then look across to the second column to the mark-up factor of 1.429 or 1.667.

Mark-up Factor Table	
Margin %	**Factor**
30.0	**1.429**
31.0	1.450
32.0	1.471
33.0	1.493
34.0	1.515
35.0	1.539
40.0	1.667
45.0	1.818
50.0	2.000
60.0	2.500

This calculation has helped Sue determine that she will earn more profit by going with the second store, even though their profit margin is higher than the first store. The only thing left for Sue to decide is whether she can cover her costs and make a profit at the $3.75 per bunch amount.

The market channel(s) that best match your business goal

There are many possible market channels for your product, each with its advantages and disadvantages. Examine which type of market channel is the best fit for you, your product and your business.

Each channel will have different logistics such as storage requirements for your product, fees to place your product or discounts for brokers. These costs will affect the price you set.

Price can also vary by channel due to market demand. For example, the price of a basket of strawberries bought at a farm u-pick will be different than the price for a similar basket at a large retail grocery chain.

Here are some common ways to market your horticulture product.

Direct Marketing	
• farmers' markets • farmgate sales (store or u-pick)	• community shared agriculture • mail order/online sales
Advantages	**Disadvantages**
• direct contact with customers • lower marketing costs • potential to earn more profit on products you sell • a market to test new products • networking with similar sellers and/or finding collaboration opportunities	• additional time required to sell products • some of the channels are seasonal • extra costs if transporting products to customers • customer base is smaller than other market channels

Indirect Marketing	
• brokers • retailers (small shops or larger grocery stores)	• restaurants • institutional food service buyers (schools, hospitals)
Advantages	**Disadvantages**
• larger customer base • good distribution system has been established • some take responsibility for marketing your product • opportunity for higher sales volume	• adds an extra cost to your product due to fees or commissions paid • selling product at wholesale prices • lose contact with the customer if you sell only through indirect channels • may be difficult to source indirect sellers interested in distributing your product

For more detailed information on opportunities and challenges for the direct marketing channel, see the Agriculture and Forestry publication *Farm Direct Marketing for Rural Producers*, Agdex 845-6.

How knowing your competitors can help you set a price

Cost-based pricing is just one way to determine your price and works best in a market with limited competition. In a market with more competition, it is best to look at what your competitors are charging.

Knowing your competitors' price can help you price your product. When competition is low for your product, you can choose to price at the top of the price range. If competition is high, you can choose to price at the low end of the price range. If your product has a unique quality or selling feature not being marketed by your competitors, you could demand a higher price.

Here are six ways to learn about your competition's pricing strategies:

Prepare a competitor list

Select who your key competitors are and review how their price compares to yours. Focus on those with a similar product and similar-sized business to keep price comparisons relevant to your business.

Analyze your main competitors

Ask customers and suppliers about your competition. If possible, visit a competitor's business to learn how products are priced and distributed. See how your competitor's product strengths, weaknesses and price compare to yours.

Watch new competitors as they enter your market

Regularly check with customers, suppliers and your competition to gather information about new businesses in your field. A growth in competition could require an adjustment in your pricing.

Use your networks to stay informed

Stores that carry your products (or do not yet) are a great resource as they can tell you about other companies they purchase from, and why. You might ask if the competition offers discounts to retailers or price cuts to consumers.

Attend trade shows

Industry trade shows are a great way to find new customers and learn about how your competition prices and promotes its products.

Welcome customer input

Have a process that makes it easy for customers to communicate with you about your product. If you are conducting market research, be sure to include your current customers in the process because they have experience with your product.

How consumer demand affects the pricing of your product

Another way to look at pricing is to review purchasing patterns and demand for your product or for products similar to yours.

For example, in Alberta over the last decade, consumer demand has increased for products that are locally grown, but there is also a high expectation for an abundant (and inexpensive) supply of fresh fruits and vegetables year-round, so pricing can be tricky.

To factor consumer demand into your pricing, you will want to know if consumers think your product offers good value for their money. To learn what consumers think, you will need comprehensive information about the size and nature of your customer base and their feelings about price.

Ask the following questions:

- How many customers do I have and where do they live?
- What is the age, income and education of my customers?
- Where do my customers spend their money?
- Do my customers believe price indicates the quality of a product?
- Why might a customer favour my competitor's product?
- What type of service does my customer value?

Getting accurate consumer information can be time-consuming and costly, but it is an important factor for setting price. Companies often hire market research firms to determine answers to these questions. A market research professional will design the research questionnaire and provide unbiased analysis of the results.

Market research information is also available through public libraries, on the Internet or through publicly-funded business development centres such as the Business Development Bank of Canada. This type of information tends to be general, but it is less expensive than creating new research.

Bringing it all together: the Pricing Horticulture Products Worksheet

Making informed pricing decisions for your horticulture product is an essential step in developing your business. Monitoring your cost of production, your competition and what your customers want – and being flexible enough to incorporate price changes over time – are key to a successful product and a profitable business.

Below is a working example for a business and product that brings together all the topics in this factsheet. Use this process as a way of setting your own price, using numbers specific to the type of product you offer and your profitability goals.

This factsheet presents an overview to the subject of pricing of horticulture products. For a more detailed analysis on different aspects of pricing, see the factsheets on *The Essentials of Pricing*, Agdex 845-1, or *Methods to Price Your Product*, Agdex 845-2.

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Pricing Horticulture Products Worksheet – Know Your Costs and Market Assessment

Example: Plump Berry Farm – Saskatoons 2 pint baskets

Product Cost	**example**
Total variable costs per unit Total fixed costs per month Current selling price	\$2.40 per basket \$3,000 \$4.00 per basket
Break-even Price	**example**
Unit contribution margin = selling price – unit variable cost	\$4.00 - \$2.40 = \$1.60 per basket
Break-even point $= \dfrac{\text{fixed costs/month}}{\text{unit contribution margin}}$	$\dfrac{\$3{,}000}{\$1.60} = 1{,}875$ baskets
Profit Goals	**example**
Develop a profit goal for the business	To generate \$2,000 profit monthly from the saskatoon berry business
Target Profit:	
N = # of units required to make a profit	
$N = \dfrac{\text{fixed costs + target profit}}{\text{unit contribution margin}}$	$N = \dfrac{\$3{,}000 + \$2{,}000}{\$1.60}$ $= 3{,}125$ baskets
Marketing Channels	**example**
Direct Marketing Options: • Farmers' markets • Farm gate sales • Community shared agriculture • Mail-order/on line	I will sell saskatoons in 2 pint baskets to the Farmers' market
Indirect Marketing Options: • Broker • Retailer • Restaurant • Institutional buyer	
Target Price Range	\$3.50 - \$4.50 per basket
Competitor Pricing	**example**
Main Competitor A	Southern U-pick
Strengths	lower price, broad selection of basket sizes and berry varieties
Weaknesses	need to travel to farm and pick product
Price Range	\$3.00 per basket

Competitor Pricing (*cont'd*)	**example**
Main Competitor B	Berry Merry Market
Strengths	fancy baskets, clean, bright specialty shop demonstrates products and recipes
Weaknesses	higher prices, limited range of basket sizes
Price Range	\$4.00 per basket
Customer Demand	**example**
Demographics of customer base	loyal customer who prefers fresh product 25 - 45 years of age likely to have post-secondary education
Wants, needs and feelings of customer base	associates price with quality expects freshness and quality when buying from Farmers' Markets likes to support local producers
Secondary data-search findings	research has found that people are eating 40% more fresh produce today than in 1970. It is estimated that the consumption of fresh and chilled foods will continue to increase which will provide new market opportunities particularly for fruits, vegetables and related industries direct marketing bypasses traditional "middlemen"– doing this the vendor can realize additionalincome from 40% to 80% on their products

Note: your costs may be considerably different than those in the example.

Cost of Production – Horticuture

Variable Expenses	example
Production Expenses: • Seed • Chemical • Fertilizer • Packaging • Irrigation • Custom work • Other	
Operating Expenses: • Trucking • Repair and maintenance (buildings) • Repair and maintenance (machinery) • Fuel, oil and lube • Advertising and marketing • Travel • Farmers market booth fees • Other	
Labor expenses: • Paid labour • Unpaid labour	
Total Variable Costs	
Fixed Expenses	**example**
Operating interest: • Depreciation (building) • Depreciation (machinery) • Small tools • Land taxes • Vehicle registration • Insurance (building, vehicle, liability) • Utilities (heat, electricity, telephone) • Office supplies • Professional fees (i.e. accounting) • Other	
Total Fixed Costs	

Cost of Production = Variable costs + Fixed costs