# SAFA Entrepreneurial Lesson

## Setting up profit margins

# What are profit margins?

---

You need two things in order to determine your profit margins.

1. The price to make the product your selling and packaging it.
2. The price that you sell the product to your customers.

After getting these two things, you can calculate your profit margins with a simple equation.

(price you sell) - (price you pay) = profit margins

The price you pay means how much money it costs you (the entrepreneur) to manufacture and package each product.

# Activity Time!

In your entrepreneur Journal, it will give you a few situations. It will ask you to calculate the profit margins when given the price you pay and the price you sell the product for.

Write down the answers to each of the questions in the Entrepreneur Journal

# Details about profit margins

As an entrepreneur, your goal is to increase profit margins. There are two ways to do this.

1. Decrease the price you pay
2. Increase the price you sell

The more favorable option is to decrease the price you pay, but this is often tricky and will be explained further. The other option is to increase the selling price, but you need to be careful when you set the prices. You need to be aware that you shouldn't increase the price too much or else the customers will not be satisfied, and the demand for your product will decrease.

# Types of pricing strategies

1. **Price Skimming:** A product pricing strategy by which a firm charges the highest initial price that customers will pay.
   a. As the demand of the first customers is satisfied, the firm lowers the price to attract another, more price-sensitive segment
   b. Example: Tesla, XBox
2. **Penetration Pricing** - It sets a low initial price for a product in order to gain quick acceptance a segment of the market.
   a. Calls for a sacrifice of short-term profits to establish market share
   b. Examples: Starbucks initially (1970's), RedBox
3. **Loss Leader** - A product sold at a loss to attract customers.
   a. Stimulates sales of more profitable goods or services
   b. Examples: Razors, Print Cartridges

# Calculations with profit margins

In some cases, you need to have a set profit margin in order to be a profitable company. This means that you are already given the profit margins, so now you need to change the price you sell for or the price you buy for in order to meet that margin. This can be mathematically calculated. Your equations will be in either of the two forms:

1. X - (price you buy for) = set profit margins
2. (price you sell for) - X = set profit margins

You are trying to solve for X in these scenarios.

# Activity Time!

In your entrepreneur journal, answer the practice problems about calculating the price you buy or sell for, when you are given a set profit margin.

# How to meet profit margins

Now that you solved for X, you need to actually bring the price to that. If solving for X was the price you pay to manufacturers, you will learn more about how to do that in the next lesson. But, if X is the price you sell, then you need to sell the product for that price if you determined that it is no longer possible to bring down the price you pay any further.

You need to be careful here though, as bringing the price up shouldn't sacrifice too many potential customer sales. If you bring the price up too much, you won't get sales and you won't make money.