Raising prices, keeping customers

Many business owners believe a price increase will drive customers away. But those offering something unique may be surprised by their pricing power.

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(FSB Magazine) -- As Tracy Trotter paid his company's expenses each month, they just kept rising: bills for materials, salaries for his 22 employees, insurance premiums, etc. Yet for the past three years Potter froze his prices. Otherwise, he said, "I worried that we'd lose customers."

Trotter is CEO of Calico Coatings (calicocoatings.com), a Denver, N.C., company that makes eight types of dry film lubricants and protective coatings. His clients include NASCAR drivers, professional drag racers, and monster--truckers, who use his products to keep their engines running smoothly. Trotter, 41, was winning new customers, but with his prices fixed and costs climbing, he was seeing his profit margin shrink at a rate of five percentage points a year.

PHOTO: DAVID JOHNSON

CEO Trotter (foreground), a pair of Ford Focus Midgets, and (from left) Calico employees - and racing hobbyists - Tanner Swanson, Annie Davis and Bradley Reithmeyer at the Hickory Motor Speedway in North Carolina

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Gaylord (left, with daughter Jenny) found that her belts such as Fairy, Nouveau Purse, and Monkeys (below), rated a price hike.

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Faced with the prospect of red ink on his books, Trotter took a deep breath a few months ago and announced price hikes that averaged 18%. Calico's customers stayed put, and Trotter saw an instant boost to his bottom line. He expects the firm to reap $3 million in revenues in 2007, up from $2.6 million in 2006, and to pocket healthy profits as well. "I was surprised by how much leeway we have on what we charge," says Trotter.

Pricing issues often vex small businesses, especially in today's climate, with competition - domestic, foreign, and Internet - rising along with costs. But veteran business owners and pricing experts say that if more small companies freshly examined their competitive positions and service offerings, they would find that they could raise prices, keep key customers, and boost their bottom line. "Raising prices is risky," says Ralph Zuponcic, a Hudson, Ohio, consultant (pricepointpartners.com), "but so is not raising prices."

First, experts say, remember the rich payoff you can reap from even a small price hike. If your firm enjoys, say, a 10% profit margin, a mere one percentage point bump in the price of your product will deliver a 10% hike in profits.

Many business owners assume that any price increase will drive customers away. But consultants who work with small companies say they often under-estimate their pricing power. Those owners know their costs are rising but sometimes forget that fuel prices are soaring worldwide and that workers are demanding higher wages even in China, India, and other developing countries. Many small U.S. manufacturers, in particular, become so focused on price competition with larger rivals or foreign ones that they don't appreciate the value of the added quality they offer, their fast and reliable delivery, or other superior services they provide - or could provide - to justify higher bills.

Most small firms can afford to lose a few of their stingiest clients, says Reed Holden, the founder of Holden Advisors, a price consultancy based in Concord, Mass. (holdenadvisors.com). "They aren't the most loyal customers anyway," he says.

Business owners who offer something unique are often surprised by their pricing power. Lyn Gaylord owns Lyn Gaylord Accessories, a business that creates belts with buckles that feature images drawn from antiques (lyngaylord.com). During a rough year she cut her prices to less than $100 to compete with rival beltmakers. Sales slipped more. "I priced too cheaply, and people weren't sure my belts were special," she says.

Gaylord then raised prices 75% on average, in part to offset skyrocketing sterling-silver costs. A typical belt now costs $350. This year Gaylord expects her company, based in Rowayton, Conn., to be profitable on $250,000 in revenue, up from $210,000 in 2006. "Price doesn't matter if customers want what they can't get elsewhere," she says.

Boosting sales with pricing software.

Other savvy business owners with diverse products and customers are learning from the airlines - most of which struggle with customer service but shine at variable pricing. They know that their customers' needs and price sensitivities vary - a rushed business flier will pay more for the same seat than a leisure traveler - and set fares accordingly. "When a customer wants something faster, different, or extra, it's a chance to hike the price," says Jerry Bernstein, president of the Price Improvement Team, a St. Louis consulting firm (priceimprove.com).

Chris Carmon learned custom-pricing the hard way. When he founded the Carmon Group, a Cleveland recruiting firm (carmongroup.com), he offered faster and more targeted searches than those of his rivals. But Carmon's initial fees were nothing special. If he placed a candidate, he charged a flat 25% of the first year's salary, just as the average recruiter did. Within a couple of years, says Carmon, he had attracted noted clients such as Berkshire Hathaway and Johnson Controls. He met their exacting needs by rushing to fill jobs or locating candidates with esoteric professional backgrounds.

Yet during his firm's first three years, Carmon estimates, he left $1 million on the table by pricing too low. Now he sets prices based on a job's demands. He recently found a veteran bridge designer for a client after a needle-in-thehaystack search, says Carmon. The fee: 35%. This year he expects his 24-person firm to turn a profit on more than $4 million in revenue, up from $2.7 million in 2006.

Experienced business owners say they constantly gather intelligence on rivals' prices - and on the quality and service that those rivals deliver - through chatting with industry contacts. Some also test the waters by raising prices for just a few customers or only on certain products, and adjusting as they see the response.

A bolder strategy involves talking directly to customers to learn how you can better meet their needs and add value that will justify a higher price. The idea is to move toward work that is higher in value and more lucrative, while accepting that some price-focused clients might walk. For more complex small companies, this strategy often requires the services of a pricing consultant, at a fee of at least $20,000.

One believer is Mantaline (mantaline.com), a 135-employee firm based in Mantua, Ohio, that makes rubber parts for customers such as Freightliner, a manufacturer of long-haul trucks. A Mantaline gasket might be used to keep a truck's sleeping compartment quiet.

Mantaline CEO Mark Trushel hired a pricing expert, who anonymously queried the company's roughly 300 customers about prices. For the top 30 clients the expert conducted in-person interviews. He asked Mantaline's other clients to complete a lengthy survey.

The process showed Trushel what his customers valued - and what would prompt them to spend more. Some wanted increased collaboration, such as plant visits from Mantaline's engineers. Others cared only about cost. If Mantaline even nudged up prices, they would be gone.

Mantaline used that knowledge to focus on the customers who wanted more care - with striking results. During the past five years the company's customer count has dropped to 140, as commodity clients jumped ship. But Mantaline has made up for it by offering more services at higher prices. Its revenues will rise to about $25 million in 2007, from $13 million in 2001, and net profits have grown 8% annually over the past five years. "I can't say whether customers are happy with our prices," says Trushel. "I can say they're happy with us." ■

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