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Matrix Pricing – What’s That? - How Can I Use It To Help Me Make More Profits

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There is a trick to being successful and making sure that your retail margins are high enough to cover your “nut” (the cost of opening your doors) while leaving enough on the bottom line to reward you for your investment and for your efforts to build your business.

That trick is called *MATRIX PRICING*. Matrix pricing divides up products into categories based on their level of demand, the gross margin that is possible to get based on the first factor (together with competition) and the percentage of the total business that particular product has compared with all the others in the retail store.

Who uses Matrix Pricing? Just about every grocery store chain, most retail & franchise chains, the big-box stores (WalMart, Target, Lowes, Home Depot, hardware store chains (franchise, coops and independent chains), etc. The list goes on and on. Many people who work in these stores are not aware of how pricing is done. It is a science that requires an understanding as to the buying patterns of the store’s customer base.

Lets take a grocery store. All of us go to a grocery store regularly and buy a mix of products.

A typical big box grocery store has approximately 25,000 items - they call them SKUs – for stock keeping units. *For example: a red pen and a blue pen are 2 stock keeping units whether there is 1 on the shelf or 1 million – get the idea).*

Some products are very price sensitive - they’re the ones you buy most times you go to the grocery store. Lets call this CATEGORY 1. Category 8 might be the least competitive category. Get the idea. Inbetween there are 6 categories of varying degree of price sensitivity. Each category allows the store to get a higher gross profit margin even though the % of the total store sales is far less than the higher category.

Category	Descript.	Mark Up Over Cost	Category As % Total Prod. Mix	%/Total Store \$
1	Most Price Sensitive	20%	3%	25%
2	2 nd Most Price Sensitive	25%	8%	20%

Mark Up Category As %

Category	Descript.	Over Cost	Total Prod. Mix	%/Total Store \$
3	3 rd Most Price Sensitive	30%	10%	15%
4	4 th Most Price Sensitive	38%	12%	10%
5	5 th Most Price Sensitive	45%	15%	8%
6	6 th Most Price Sensitive	50%	18%	6%
7	7 th Most Price Sensitive	60%	25%	4%
8	8 th Most Price Sensitive	75%	8%	2%

Notice anything?

% of total product mix in this virtual grocery store:

Category 1 = Of total product mix (25,000 items) or 3%	750 SKUs
Mark up over cost	20%
% of gross overall sales revenue	25% of sales \$'s

Category 7 = Of total product mix (25,000 items) or 25%	6,125 SKUs
Mark up over cost	60%
% of gross overall sales revenue	4% of sales \$'s

So how do these companies price? They know their breakeven cost of doing business requires them to generate a profit of 27%. Obviously they can't sell too much of category 1 product at 20% if they expect to make a profit. Right?

What do they do? They encourage you to buy products from price categories where their margins are much higher and the price sensitivity is much lower. For example, most people know what the price of a gallon of milk might be. But do they know what the price of truffles might be? Probably not especially if they don't buy truffles every day (smile). At least I don't buy them very often.

Can you see that *getting customers to mix what they buy from various product categories can produce an AVERAGE GROSS MARGIN* significantly above the stores break-even? Maybe that's the reason they put impulse items at the checkout counter. What about those items that are stacked right in front of the check out counter or in the area where you initially come into the store? See a pattern here? You bet.

This same technique is used by a broad spectrum of retailers. Think about your last trip to Home Depot or Lowes. Notice anything (smile)? If you're not using Matrix Pricing techniques in your retail operation, consider creating your own price matrix based on your product demand mix and product price sensitivity. If you do it well, your profit margins will grow – big time.