Mark-up Pricing

The Mark-up pricing is the method of adding a certain percentage of a markup to the cost of the product to determine the selling price.

In order to apply the mark-up pricing, firstly, the companies must determine the cost of a product and decide on the amount of profit to be earned over and above it and then add that much markup in the cost.

Selling Price = Cost + Mark Up

Let's understand the mark-up pricing through an example.

Suppose, there is a laptop manufacturer who has the following cost and sales expectations:

Variable cost per unit: Rs 30
Fixed Cost: 5, 00,000
Expected Unit Sales: Rs 50,000

The manufacturer's unit cost is given by:

Unit Cost = Variable cost + Fixed cost/unit sales

Thus, Unit cost = 30 + 500000/50000 = Rs 40

Once the cost is determined, the manufacturer decided to add a 20% markup on sales. The mark-up price is given by:

Mark-up price = unit Cost/1-desired return on sales

Thus, mark-up price = 40/ 1-0.2 = 50

Hence, the manufacturer must charge Rs 50 to earn a profit of Rs 10.

The benefit of using the mark-up pricing is that it is very simple to calculate and understand. Also the same type of pricing used by all the firms in the industry, the price tends to be similar and hence, the price competition reduces in the market.

But however, it also suffers from limitations, while computing the mark-up price the actual demand for the product is ignored. Also, the perceived value of the customer and the amount of competition prevailing in the market is overlooked.