

Pricing Policy: Profitability

Last lesson we studied God's Word and discovered precepts (rules) and principles (guidelines) for selecting the market for your business' products or services. We learned that business, the buying and selling of goods and services, is a God-ordained activity. We were cautioned, however, that not all business is legitimate in God's eyes – only business that somehow contributes to what God wants done in the world, and does not actively contribute to what He does not want done.

We discovered three characteristics of a properly selected market: (1) Your market has legitimate needs that your business can meet; (2) Your business can meet these needs better than your competition – you can bring glory to God by your skill and excellence; and (3) Your team has a passion for serving this market, a sense of purpose and mission beyond the delivery of products or services.

The next step in developing your marketing strategy is to consider the other marketing decisions regarding product policy, pricing policy, distribution policy and communication policy – your marketing mix “tool kit.” We are going to focus on pricing policy in this study.

In general, the major factors impacting the price decision are:

- Internal
 - Business objectives
 - Are you seeking profitability, growth, or market share?
 - Marketing strategy
 - Are you the premium provider or low cost producer? Will you offer promotions? What is your discounting policy?
 - Production costs
 - What does it really cost to make your product or deliver your service?
- External
 - Consumer demand
 - Pricing is affected by supply and demand.
 - Competition
 - What is your competition's price?
 - Legal Aspects
 - Are there any legal concerns with your pricing?

We are going to search the Word for precepts and principles regarding pricing and analyze these factors in light of what we find.

James 4:13-16

13 Come now, you who say, "Today or tomorrow, we shall go to such and such a city, and spend a year there and engage in business and make a profit."

14 Yet you do not know what your life will be like tomorrow. You are [just] a vapor that appears for a little while and then vanishes away.

15 Instead, [you ought] to say, "If the Lord wills, we shall live and also do this or that."

First, let's consider the issue of profitability. This seems obvious, but is there biblical support for a market economy, for capitalism?

This seems implicit in God's design – there were free markets in Israel's theocracy, there is lots of instruction regarding private property and buying and selling, and there is no explicit teaching espousing any other form of economic system.

We are going to look at a passage in the New Testament book of James. The context of James is the emphatic teaching that a faith that saves is a faith that also produces a change in our lives. This is what being "born again" means – we are now alive spiritually and new babies naturally grow. If there is no change, no works, no fruit, no growth, then there has been no spiritual birth and we are still dead in our sins. The changed life, the works if you will, are evidence of the new life in Christ.

Our passage is James' application of this teaching to Christian business people.

*Leader: Make sure there are no questions about the context and theme of the book of James before moving on. Then, read James 4:13-16 and have the group say aloud and mark **profit**.*

OBSERVE

James is saying to Christian business people that their faith should produce a change in how they do their business planning. What is the instruction given, and why?

DISCUSS

What is the principle being taught regarding business planning?

1 Timothy 5:8

8 But if anyone does not provide for his own, and especially for those of his household, he has denied the faith, and is worse than an unbeliever.

1 Chronicles 4:10

10 Now Jabez called on the God of Israel, saying, "Oh that Thou wouldst bless me indeed, and enlarge my border, and that Thy hand might be with me, and that Thou wouldst keep [me] from harm, that [it] may not pain me!" And God granted him what he requested.

What do we learn about making a profit in business?

Let's continue to explore what God's Word has to say about making a profit. The context of 1 Timothy 5:8 is instruction given to the church regarding benevolence ministry. No one should be supported by the church if there is family capable of doing so instead. This verse is a reproof given to those believers who shirk this responsibility.

*Leader: Read 1 Timothy 5:8 and say aloud and mark **provide**.*

What is the reproof given?

What is the principle being taught in this verse?

How does this principle apply to our study of making a profit? What must a business do in order for the employees to be able to meet their God-given responsibilities to provide for their families?

Thus, one biblically based purpose of making a profit is _____.

Leader: Read aloud 1 Chronicles 4:10.

What does Jabez pray and ask God to do for him?

What are Jabez' conditions for his request? Why do you think he added these conditions?

Leader: Explain the context (Paul's defense of his apostleship and authority to instruct the church he founded) and then ask someone to read from their Bible 2 Corinthians 10:13-16.

What is this "measure," this "sphere" that Paul is referring to?

Why does he want it to grow?

What is a business' sphere in this context?

Is it a good thing for a Christian business to want to grow, to "enlarge its borders?" Why?

Does it take money to grow ministries and businesses?

Thus, tying the teaching of these two passages together, another biblically based purpose of making a profit is

Proverbs 22:7

7 The rich rules over the poor, And the borrower [becomes] the lender's slave.

Leader: Read aloud Proverbs 22:7

Compare and contrast the lender with the borrower. Which has the greatest freedom to serve Christ?

Leader: Ask someone to read from their Bible 1 Corinthians 7:20-24.

Relate the teaching in Proverbs 22:7 with this command in 1 Corinthians 7:23. Is business debt a good thing for the Christian?

Proverbs 3:9-10

9 Honor the Lord from your wealth,
And from the first of all your produce;
10 So your barns will be filled with
plenty, And your vats will overflow
with new wine

2 Corinthians 8:12-15

12 For if the readiness is present, it is
acceptable according to what [a man]
has, not according to what he does
not have.
13 For [this] is not for the ease of
others [and] for your affliction, but by
way of equality--
14 at this present time your
abundance [being a supply] for their
want, that their abundance also may
become [a supply] for your want, that
there may be equality;
15 as it is written, "He who
[gathered] much did not have too
much, and he who [gathered] little
had no lack."

1 Corinthians 9:14

14 So also the Lord directed those
who proclaim the gospel to get their
living from the gospel.

In order to avoid, or at least minimize debt while growing your
business to expand your sphere of influence for Christ, another
biblically based purpose of making a profit is

*Leader: Read aloud Proverbs 3:9-10, 2 Corinthians 8:12-15, 1
Corinthians 9:14, Acts 2:44-45, Ephesians 4:28 and Deuteronomy
8:16-18*

Take a few minutes to re-read these verses, to reflect upon them,
and then relate them to our study of making a profit.
Another biblically based purpose for making a profit is

DISCUSS

Is God for or against businesses making a profit? Let's recap and
list the biblically based purposes for making a profit that we have
discovered in this study.

Can you think of any others?

Do you see that making a profit doing business in a manner that
honors the Lord is an honorable, worthy objective for the Christian
businessperson? Is not making a profit dishonorable to God?

So what is an application of these truths regarding profitability to a
business' pricing policy?

Acts 2:44-45

44 And all those who had believed were together, and had all things in common;

45 and they [began] selling their property and possessions, and were sharing them with all, as anyone might have need.

Ephesians 4:28

28 Let him who steals steal no longer; but rather let him labor, performing with his own hands what is good, in order that he may have [something] to share with him who has need

Deuteronomy 8:16-18

16 "In the wilderness He fed you manna which your fathers did not know, that He might humble you and that He might test you, to do good for you in the end.

17 "Otherwise, you may say in your heart, 'My power and the strength of my hand made me this wealth.'

18 "But you shall remember the Lord your God, for it is He who is giving you power to make wealth, that He may confirm His covenant which He swore to your fathers, as [it is] this day.

Leader, walk the group through this little exercise. The approved solution is located on the last page of this study.

EXERCISE

You are in the widget business. It costs you \$10 in materials and another \$5 in hourly labor to make 100 widgets. Your annual overhead (salaries, equipment, lease, office supplies, marketing, etc) is \$350,000 and you expect to produce 5,000,000 widgets annually.

Your eager new sales manager asks you to approve a price of \$.18 per widget to win a big order for 50,000 widgets.

Does your business make a profit at this price?

So we've discovered that setting the price of your product or service high enough to make a profit is a biblically based principle, and that you must consider all your costs in determining what your price needs to be.

How much profit should you make? How high should your profit margin be? We would all agree that charging the United States government \$300 for a toilet seat is too high! But should we expect it to be the same price we would pay at the hardware store? The government contractor probably has higher costs of doing business due to government bureaucracy, and inane government specifications that might require their toilet seats to be just a tad different than the normal commercial ones, and that tad difference might require a whole new production run, thus increasing costs.

Or how about the high cost of prescription drugs? How much did it cost to do the research, to meet the FDA requirements? As we've learned, all of this has to be factored into the pricing calculation.

Or how about the relatively low cost of a music CD? It costs only pennies to produce the disks themselves, who is making all the money?

Here is one that hits home to me since I earned my living for years as a business consultant charging an hourly rate. Some people assumed that I made that amount 40 hours per week every week, and that it all ended up in my pocket. I wish! Most hourly rate professionals are doing great if 65% of their time is billable, and then of course there is the office, administrative staff, telephone ... and of course taxes.

My point from these three examples is that it is not easy to judge a product or service's profitability from the outside in terms of its reasonableness.

In most cases, market forces tend to keep profit margins in check since there is always a competitor willing and able to sell at a lower price. Thus, the profit margin decision is often just a business strategy decision for the Christian businessperson. Do you wish to position your company as the premium provider at the premium price, or do you wish to position your company as the low cost provider? Do you wish to trade profitability for market share? Are there economies of scale at higher volumes that drive lower costs and higher profitability even at lower margins per unit?

There are a couple of biblical parameters to consider however.

Leviticus 25:35-37

35 'Now in case a countryman of yours becomes poor and his means with regard to you falter, then you are to sustain him, like a stranger or a sojourner, that he may live with you.

36 'Do not take usurious interest from him, but revere your God, that your countryman may live with you.

37 'You shall not give him your silver at interest, nor your food for gain.

OBSERVE

Leader: Read Leviticus 25:35-37 aloud.

The context of Leviticus is God's desire for His people to be sanctified, set apart from the world, with a deep reverence and respect for God and an awareness of their own sinfulness and need for forgiveness. In this context these instructions are given to creditors.

What is the creditor to do, and not do, with people who are so poor they must even borrow money to buy food and basic needs?

DISCUSS

Do you think this applies to New Testament believers? The general rule in applying old testament commands and principles today is to determine if new testament teaching affirms, changes or nullifies the OT teaching.

Leader: Ask someone to turn in their Bible to the book of James and read James 2:14-16, taking note of what is said about the poor. Ask someone else to read Luke 10:30-37, taking note of Jesus' definition of neighbor.

Philippians 2:3-4

3 Do nothing from selfishness or empty conceit, but with humility of mind let each of you regard one another as more important than himself;

4 do not [merely] look out for your own personal interests, but also for the interests of others.

Do you think Leviticus 25:35-37 applies to us today?

What in the world does this have to do with determining your profit margin? Could there be a principle here about profiting from the misfortune of others?

There is a pricing strategy known as “predatory pricing” that deliberately sets the price below cost in order to gain market share and/or drive your competition out of business with the intention of raising prices later. Let’s evaluate this strategy biblically.

First of all, the very name “predatory” sort of suggests something doesn’t it? Satan is described in such terms, as an *...adversary prowling about like a roaring lion seeking someone to devour.* 1 Peter 5:8

Should we be seeking in any sense to prey on people or businesses?

Leader: Read Philippians 2:3-4.

OBSERVE / DISCUSS

The context of this passage is Paul’s exhortation to the believers in Philippi to follow his example and have the same attitude as Christ toward others.

What are we to do, and also not do, according to this passage?

How might this apply to “predatory” pricing, and our attitude toward our business practices in general, keeping in mind God’s purpose for your business?

Matthew 5:43-45

43 "You have heard that it was said,
'You shall love your neighbor, and
hate your enemy.'

44 "But I say to you, love your
enemies, and pray for those who
persecute you

45 in order that you may be sons of
your Father who is in heaven; for He
causes His sun to rise on [the] evil
and [the] good, and sends rain on
[the] righteous and [the] unrighteous.

How are we to think about our competitors? Are they enemies to be destroyed like the heathen nations that occupied the land promised to Israel?

Leader: Read Matthew 5:43-45.

This passage is from Jesus' Sermon on the Mount and He is teaching about true righteousness.

Compare and contrast what the Jewish religious leaders taught about our enemies with what Jesus taught.

What reasons does Jesus give in this passage for this command?

Who are the enemies referred to in this passage? Ask someone to read from their Bible Ephesians 6:11-12.

Are our competitors our enemies?

So what is your biblical evaluation of business strategies that seek to destroy the competition for financial gain?

Here are some thoughts to ponder about this question of competition in the marketplace.

- Focus on serving your selected market versus fighting the competition.
- If you cannot provide an excellent product or service at a fair price better than your competition – in other words better value - why are you in this business in this market? What benefit does your customer derive if you are successful in driving out the competition?

- Can you define your market in such a manner that there really is no competition for what you do and how you do it?
- Has it ever crossed your mind that your most dangerous competitor might be the very place the Lord wants you to share the good news of Jesus Christ?

By the way, we're not done with pricing; we actually haven't looked at the primary teaching on pricing in the Bible yet. Next lesson we will study pricing fairness and consistency.

BIBLICAL PRINCIPLES DISCOVERED

- **For-profit business is a God-ordained activity.**
 - Profits allow businesses to **pay sufficient wages** so that workers can meet their biblical obligations to provide for their families.
 - Profits allow businesses to grow and **increase their influence for Christ** in the marketplace.
 - Profits allow businesses to **minimize the use of debt** financing and increase their freedom to serve Christ.
 - Profits allow businesses to **give more money** to support God-ordained ministries.
- You must **consider the total cost** of your product and service in order to set a price that will produce a profit.
- God does **not want us to profit from the misfortune of others** when it comes to basic needs.
- God does **not want us to use pricing as a weapon** to destroy our competition, for our business competitors are not our enemies, they are part of our mission field.

BUSINESS APPLICATION

1. Is your business profitable? Have you ever done a total cost analysis of your products and services to determine if they are priced properly to produce a profit?
2. What are you doing with your profits?
 - a. Are you paying sufficient wages (or paying market wages)?
 - b. Are you re-investing to grow for Christ (or hoarding for yourself)?
 - c. Are you trying to minimize debt and self-finance your business (or leveraging your business to the hilt and becoming servant to the lender)?
 - d. Are you tithing off your profits (or just off your personal income, or maybe not at all, or some sort of sliding scale as your business has prospered)?
3. What is your attitude toward your competition? How does it measure up to God's Word? Are you engaging in "predatory" pricing? How can a Christian business compete hard in the marketplace and still reach the marketplace for Christ?

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Approved Solution

You are in the widget business. It costs you \$10 in materials and another \$5 in hourly labor to make 100 widgets. Your annual overhead (salaries, equipment, lease, office supplies, etc) is \$350,000 and you expect to produce 5,000,000 widgets annually.

Your eager new sales manager asks you to approve a price of \$.18 per widget to win a big order for 50,000 widgets.

Does your business make a profit at this price?

It costs \$15.00 "out of pocket" to produce 100 widgets. That is \$.15 per widget. Thus, you would make \$.03 ($$.18 - $.15 = $.03$) on each widget. This is known as the gross margin, and is often expressed as a percentage - $$.03 / $.18 = 17\%$ gross margin. But you still don't know if you've made a profit yet. Why?

The \$.03 is also referred to as the "contribution." Contribution to what? The contribution of that sold widget to cover overhead and then contribute to profits. Since it costs \$350,000 annually to operate this business above the direct, also known as variable, costs of production, and you plan to produce 5,000,000, the overhead per widget is $\$350,000 / 5,000,000 = $.07$ per widget.

So, the total, fully allocated cost for you to produce a widget is \$.15 (direct cost) + \$.07 (indirect cost) = \$.22 per widget.

Thus, you would actually lose \$2,000 on this "big order" ($$.18 - $.22) * 50,000 = -\$2,000$.