



BUSINESS 05

# Business model and strategy

How does your business work?

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Warsaw University  
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# Target



**BUSINESS**

**MODULE 5**

## Business model and strategy

This module aims to help you work on the economic model and the strategy of your future business.

# What will you learn in this module

- 1 What a business model is and how to build yours.
- 2 How to work on your business strategy.
- 3 How to fix prices.



# Chapters in this module

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**1**

Business model

**2**

Business strategy

**3**

How to fix prices



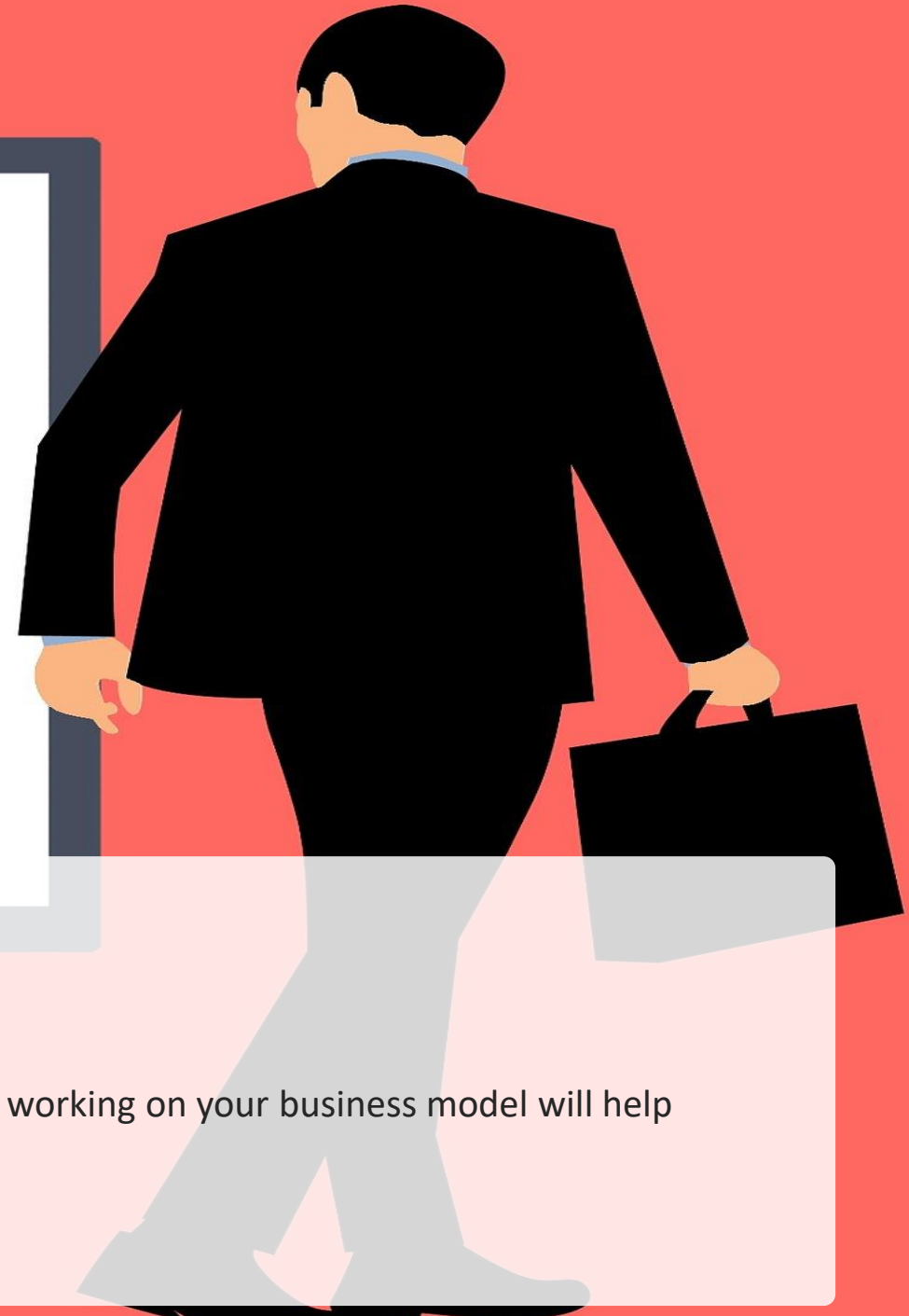
**BUSINESS**

**MODULE 5**

**CHAPTER 1**

# Business model

In this chapter you will learn about business models and how working on your business model will help you to strengthen your business project.





# What will you learn in this chapter

- 1 What a business model is.
- 2 What a business model canvas is and how to work with it.
- 3 Different types of business models.
- 4 Understanding an example of a business model.
- 5 If you have to be innovative when working on your business model.



## What a business model is?

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Before getting to the heart of the matter, let's define what a business model is and what its purpose is. Then, we will see how to strengthen your business project using a tool called a “business canvas”.



# What a business model is?

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A business model is a plan that details how a company expects to make money. In other words, a business plan is a sort of outline of the company's strategy to enter and grow in a market. It's actually a picture of the economic and commercial structure of your company.

The business model has two purposes:

- A way to make your business clearer and more precise. It's a tool that could help you to go further in the clarification of your idea, concept mentioned in Training Unit BUSINESS 02.

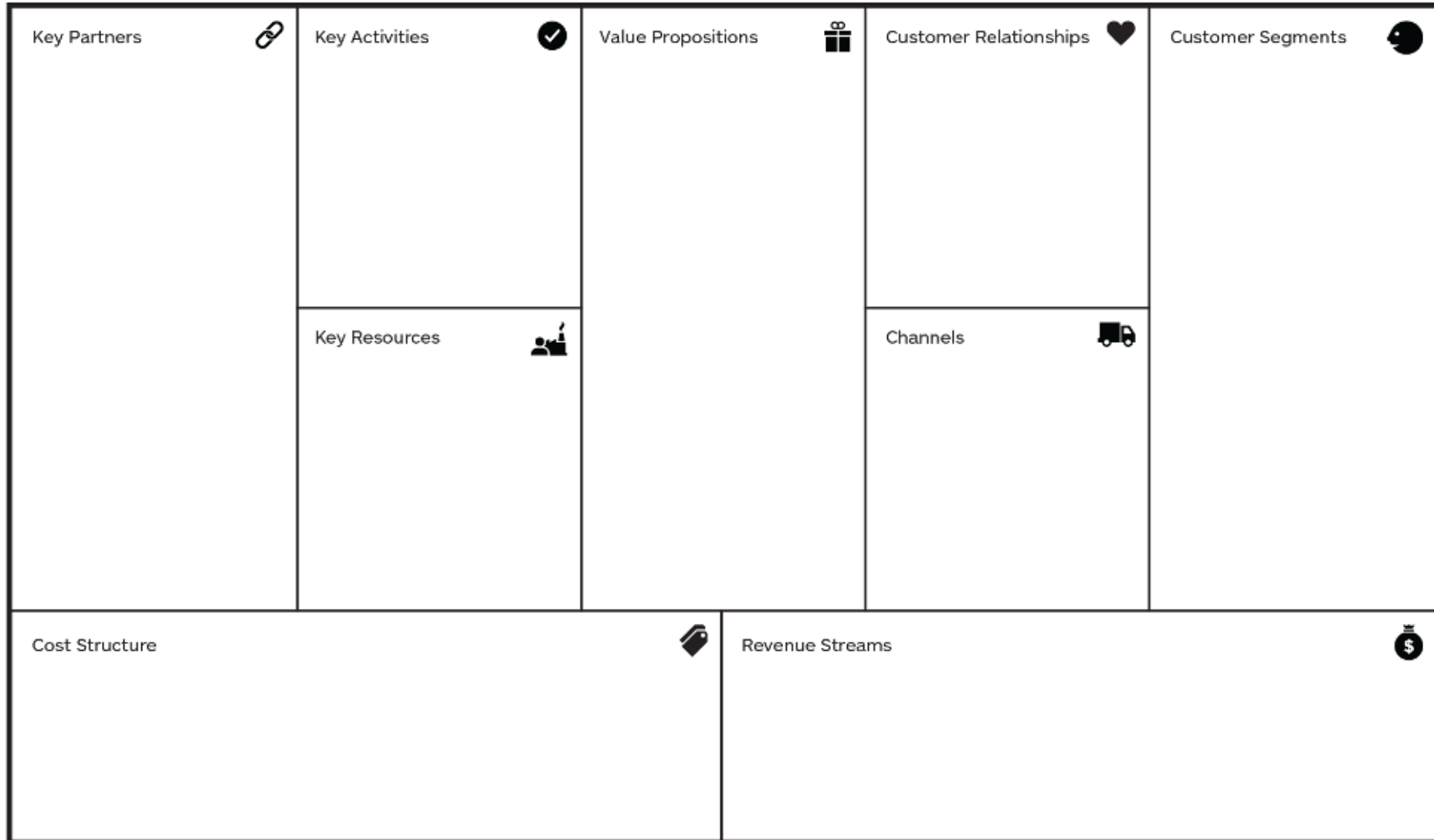
- It is a concise and understandable document presenting your company's strategy. Your future business partners, like your bank for instance, will probably be interested in taking a look at your business model. It will help them to identify the economic workings of your business.

You now understand that your business can't make it without this concept, either for yourself or your business partners. So, how will you build it?

You will learn how to use a tool called a "business model canvas" that will help you to build your business model.



# Business model canvas



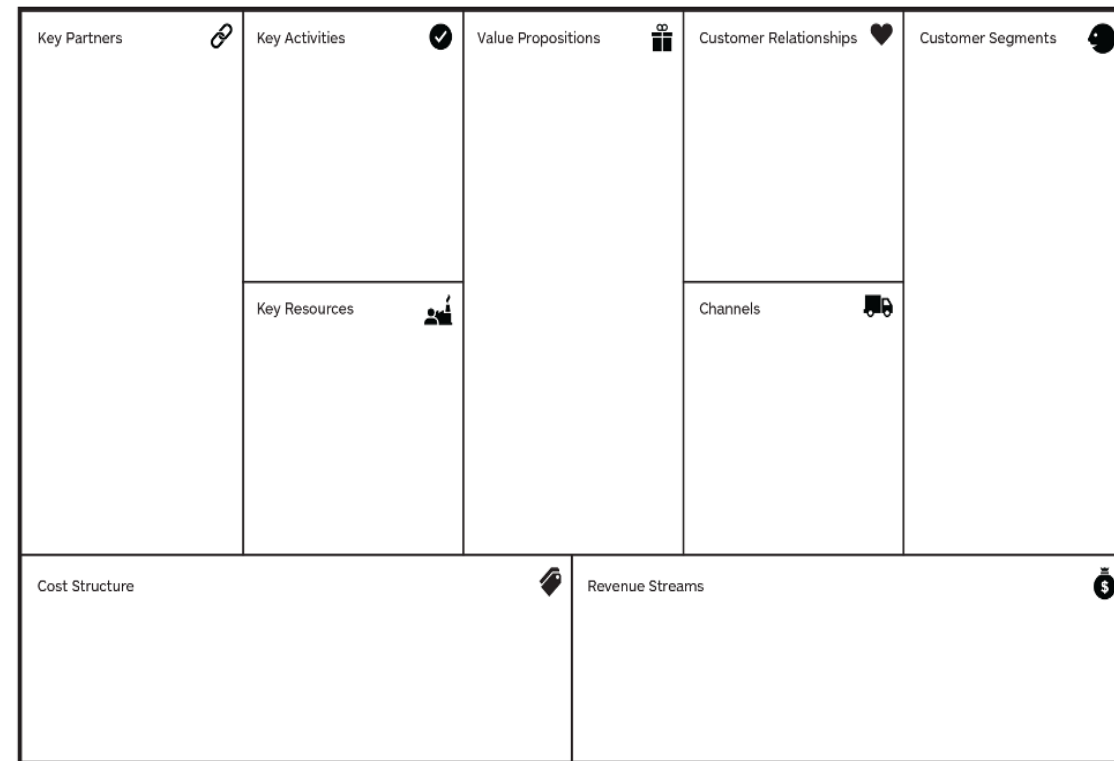
# Business model canvas

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First of all, you're invited to download your business model canvas [here](#).

As you can see, the business model canvas is divided into 9 boxes and each of them provides valuable information about how your company will create and deliver value. In other words, how it will fulfil the needs of customers and make money.

In the following slides, we will explain how to manage each of these boxes.



# Value proposition

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By value proposition, we simply mean: What do you bring to your customers?

Managing this box involves answering the following questions: “Why would my customers choose me over my competitors? Which problems, needs and expectations am I meant to solve and reach?”

The reasons why people will buy **your** goods and services (and not those of competitors) outline your value proposition and, therefore, your uniqueness.



## Key activities

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What activities/ tasks need to be completed to fulfil your business purpose?

In this box, you will detail what you sell (goods) and/or provide (services), but above all how you sell and provide them. In other words, on a regular basis, what needs to be done to make the business work?



## Key partners

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In this box, try to list external stakeholders, like other companies, suppliers or sub-contractors, that you may need to work with to create and develop your business.

In other words, these stakeholders are the allies of your company in its quest to achieve its value proposition.





## Key resources

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What resources are needed in order to create value  
(= sell/deliver/provide your goods and services)?

There are several types of resources:

- Human (employees for instance)
- Financial (cash, bank loan...)
- Material (equipment, buildings...)
- Intellectual (patents, brand...)

In this box, try to detail the most important  
resources to use and work with for your business.





## Customer segments

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Customer segmentation consists of dividing a global customer base into different groups of customers that share similar characteristics: e.g. age, consumption habits, budget, needs, expectations, etc.

For instance, for one kind of product, you can try to identify different customer groups related to your different types of offerings and classify them by similar features.

For each product line, your customers' profile will be different. Try to identify different customer groups related to your different types of offerings and classify them by similar features.



# Customer relationships

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What type of relationship do you want to set up with each of your customer groups?

There are several types of customer relationships including ones to:

- strengthen the loyalty of your customers;
- continuously acquire new “one-shot” customers;
- encourage customers to spend more or more often;
- encourage customers to talk about your business (e.g. referral/sponsorship program).

The type of relationship you want to establish with your customer groups will influence their experience.



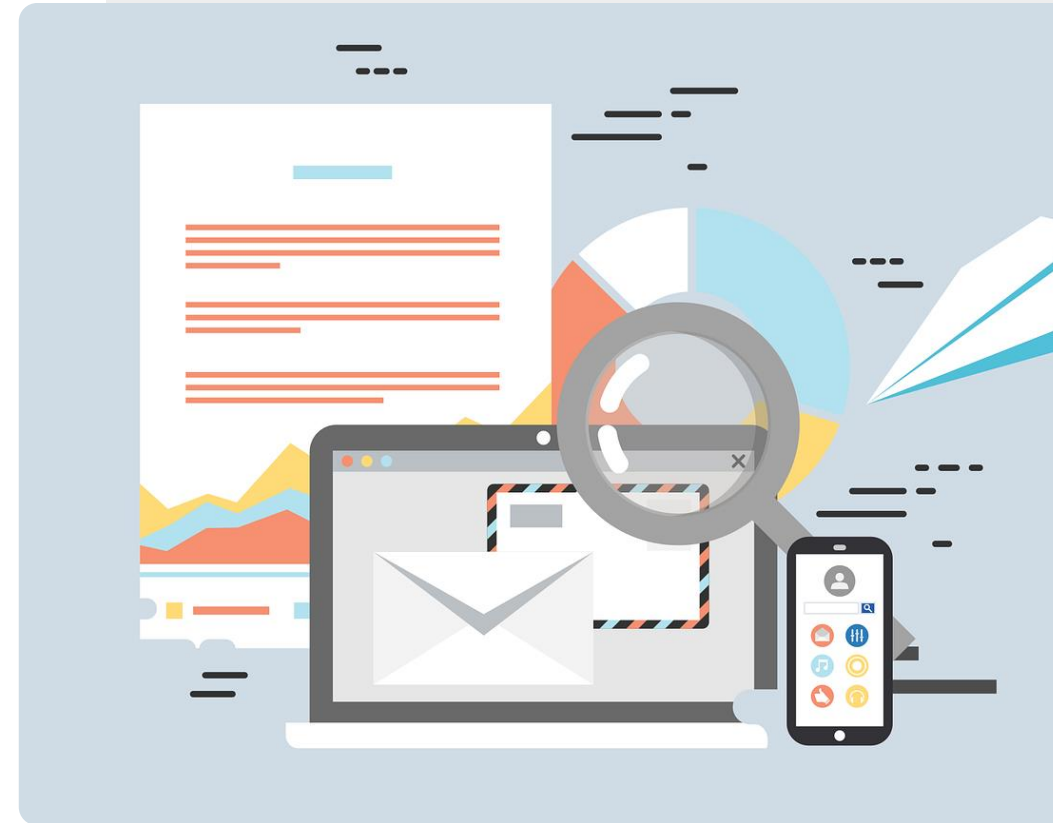
## Communication channels

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How will your company communicate with and reach out to each of your customer groups?

There are several ways (channels) to interact with customers, for instance:

- Face-to-Face (for instance in a store, at events)
- ICT (email, phone, social media)
- Self-Service (a machine provides the good/service)
- Third party (a sub-contractor will provide the service on your behalf).



## Delivery channels

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By delivery channels, we also understand how your products and services will be delivered to each customer group.

Some of the common channels to deliver goods/services are:

- Delivery at home
- Digital delivery (eBook, streaming, online rental)
- Purchases made directly from the store.





# Cost structure

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What are the costs incurred by your business?

In other words, what do you have to spend to sell your products/services?

In this block, your mission is to evaluate the costs of creating and delivering your value propositions to your customers.

What are the costs for:

- Your key activities?
- Your communication and supply channels?
- Your key resources?



# Revenue streams

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Revenues streams are ways to generate money by selling your products or services to your customers.

How exactly will you earn money from selling goods and providing services (but also by renting premises or by advertising for instance)?

There are different sources from which you can make money:

- Transaction-based revenues (customers make one-time payments)
- Subscription fees (customers pay one or several times per year for continuing use of the product/service)
- Brokerage fees (revenue generated by acting as an intermediary between two or more parties).







## Different types of business models

Now that you know a little more about what a business model is, the following slides introduce a non-exhaustive presentation of different types of business models.

## Low-cost

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More and more common in various industries, this type of model consists of drastically lowering the costs of production to propose very attractive prices for customers.

Some usual ways to lower production costs are:

- A lower quality of the raw material used and/or the goods sold;
- Economy of scale that consists of buying a large number of goods to reduce the unit cost of each item;
- Outsourcing a part of the production to a cheaper place of production (often to make savings on wages).



# Pros and cons of low-cost

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## Advantages

- Being competitive.
- Products and services affordable for low budgets.



## Disadvantages

- Perception of poor quality.
- Large volume of sales required.
- High initial fixed costs due to the large volume of products bought.

## Commissioning

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A company sells other companies' products and is paid a commission on each product sold.

This is the business model of car dealerships, insurance or real estate salesmen/saleswomen, for instance.



# Pros and cons of commissioning

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## Advantages

- You can focus all your energy only on one thing: selling.



## Disadvantages

- No control over the products (origin, quality etc.), only over the sales process.
- Dependence on the company for which you sell products: if it closes, you lose sales opportunities, for instance.

## Subscription

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This model allows the customer to get a continuous and or regular service by paying a fixed amount every week, month or year.

Streaming companies, newspapers and even some e-commerce websites are based on this business model.

A variation is freemium. It consists of offering free products/services but charging customers for improved or additional versions of these products/services. The payment for an improved/additional version can be made as a once-off payment or as a subscription fee.





# Pros and cons of subscription

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## Advantages

- Recurring sales (a steady stream of income).
- Builds brand loyalty and attachment.



## Disadvantages

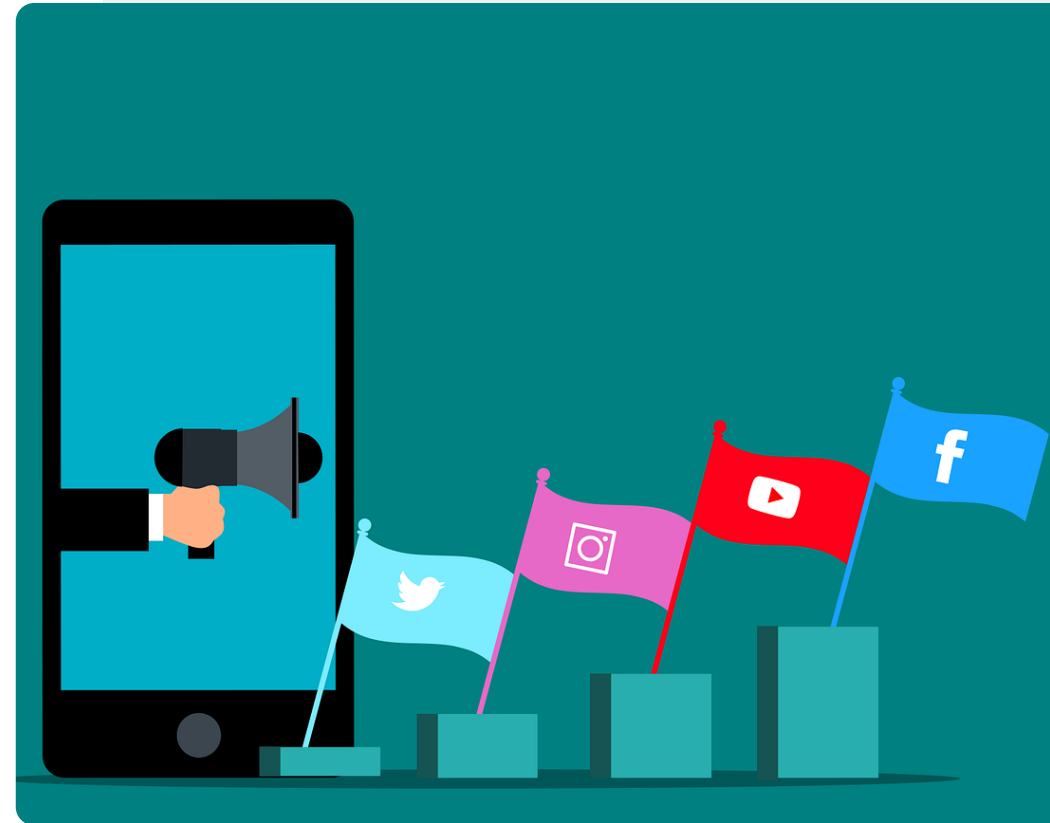
- Difficult to attract and keep customers.
- Need to innovate regularly to constantly add value.

# Advertising

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Like free newspapers and many websites, this business model consists of offering content that is completely free to users.

The company is then fully remunerated by its advertising contracts. This economic model is therefore dependent on advertisers.



# Pros and cons of advertising

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## Advantages

- Advertising companies pay you, not the people who consume your product/service.
- Offers a product/service for all budgets (as consumers do not pay directly).



## Disadvantages

- Not suitable for small companies and usually reserved for already established companies.
- Total dependence on audience volume. The survival of the company depends on its ability to attract and retain its audience.

## Consumption-based billing

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This business model allows a customer to only pay for what they have consumed. This system is growing in areas such as the car insurance business or even internet subscriptions.

Examples: Instead of paying a fixed monthly bill, the consumer pays their car insurance according to the number of kilometres driven, or their internet subscription according to the data volume they have consumed.



# Pros and cons of consumption-based billing

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## Advantages

- Generally higher unit margin than other models.
- Eco-friendly model, therefore positive impact on the brand image.



## Disadvantages

- Difficulty in setting up a system for counting and tracking the units consumed.
- Detailed financial analysis, as well as use estimations of the products, to be carried out and evaluate break-even points.

## The printer model

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Also known as the “razor and blade business model”, the principle of this model consists of selling a basic product at a very low price or even giving the product for free (printer, coffee machine...) and then charging only for the consumables (ink, coffee pods...).

This economic model allows a company, with an initial investment, to ensure long-term customer loyalty and dependence.





# Pros and cons of the printer model

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## Advantages

- Steady and stable source of income (people are dependent on your products).
- Builds customer loyalty for your brand.



## Disadvantages

- Need to innovate regularly to constantly add value.
- Higher initial fixed costs for providing the products at a low starting price.

# Franchise

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A franchise is a type of business that is operated by a company known as a franchisee using the trademark, branding and also other resources (material but also immaterial, like expertise) of a franchisor.

In other words, the franchisee is licensed to use the franchisor's trade name and business processes, such as suppliers or logistics.

Fast-food or ready-to-wear brands are particularly known for using this business model.



# Pros and cons of the franchise

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## Advantages

- Technical, organizational and eventually material assistance from the franchisor.
- Brand recognition.



## Disadvantages

- Significant costs (entry and license fees, % of sales revenue to be paid to the franchisor).
- Lack of independency (suppliers, etc.).

# Example of a Business Model

In the document

“HoS\_TU\_BUSINESS\_05\_Business\_model\_and\_strategy\_annex\_01\_EN” you will find an example of a completed Business Model.

This business model is completed with the example of a company that delivers healthy meals to ageing clients who have experienced the loss of autonomy at home.

Get inspired and then complete your business model.



## BUSINESS 05 Business model and strategy Example of a Business Model Canvas

EN

<p><b>Key Partners</b></p> <ul style="list-style-type: none"> <li>• “A” company is in charge of the preparation of organic and healthy meals.</li> <li>• “B” company is in charge of the preparation of smoothies and the fruit desserts.</li> <li>• “C” company is in charge of the preparation of the bread.</li> <li>• “D” company provides me with packaging.</li> </ul>	<p><b>Key Activities</b></p> <ul style="list-style-type: none"> <li>• Organize the daily delivery rounds.</li> <li>• Collect the dishes from the partners (cooker, baker, packaging company...).</li> <li>• Deliver the dishes to my clients’ homes.</li> <li>• Ensure customer service (phone, emails, subscription requests).</li> </ul>	<p><b>Value Propositions</b></p> <ul style="list-style-type: none"> <li>• Help ageing people by delivering healthy and organic prepared meals directly at home.</li> <li>• Help ageing people to discover new types of meals: typical meals from around the world for instance.</li> <li>• Each meal is prepared regarding the client’s characteristics: salt-free, gluten-free, vegan meals... We offer a complete customization of our meals.</li> <li>• Our offer allows ageing people’s families to stop spending time in meal preparation for their parents and have more free-time for themselves.</li> </ul>	<p><b>Customer Relationships</b></p> <ul style="list-style-type: none"> <li>• Friendly talks with customers (not being only a delivery person but having an authentic social role).</li> <li>• Regular and frequent relations with customers (not only one shot or occasional deliveries).</li> <li>• Be willing to constantly adapt to their evolving needs and requests.</li> </ul>	<p><b>Customer Segments</b></p> <ul style="list-style-type: none"> <li>• Ageing people in loss of autonomy (unable or unwilling to prepare meals themselves).</li> <li>• Ageing people who want more diversity, creativity and better quality in their daily meals.</li> <li>• People who are looking for a solution for their parents/grandparents or their husband/wife to prevent or minimize a loss of autonomy.</li> </ul>
<p><b>Key Resources</b></p> <ul style="list-style-type: none"> <li>• A refrigerated van to deliver prepared meals.</li> <li>• A customized software to help me to automate and organize the daily delivery rounds.</li> <li>• A part-time employee that will be in charge of the customer relationship (phone calls, emails, social media).</li> </ul>	<p><b>Channel</b></p> <ul style="list-style-type: none"> <li>• Deliveries directly to clients’ homes.</li> <li>• I pick up the dishes directly from the suppliers (see “key partners”).</li> <li>• Online and offline advertising to be known from potential new customers.</li> </ul>			
<p><b>Cost Structure</b></p> <ul style="list-style-type: none"> <li>• Main expenses: Purchases of ingredients, van expenses (fuel and maintenance), advertising, customized software license and employee’s wage.</li> <li>• Negotiated payments for purchases of ingredients: I pay my partners within 30 days while my customers pay me within 15 days (by automatic transfer every 15th and 30th of each month). Consequently: low cashflow requirement.</li> </ul>		<p><b>Revenue Streams</b></p> <ul style="list-style-type: none"> <li>• Revenues: Margins of 40% on sale of prepared meals. From 2,5 to 4 € of margin per meal delivered. Most of the clients will choose the 7/7 days formula so 14 meals (lunches and dinners) delivered per week in 4 delivery time slots (Monday morning, Wednesday morning, Friday morning and Saturday Afternoon).</li> </ul>		



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View annex 01 (PDF)

Download your Business Model Canvas (DoC)

# Does my business model have to be different and innovative?

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Here is a frequently asked question: do you have to think of a unique and innovative business model that none of your competitors seems to share?

In fact, it depends on numerous characteristics. It depends on your business industry, on your market, on your business vision and many more elements. No universal answer can be given here.

But remember that, as a general rule, opting for an innovative business model is a challenge and often a risky one. Being a pioneer in something is generally not an easy path. If you decide to, be prepared to take risks.

Furthermore, not every type of business is suitable for an innovative business model. For instance, if you want to open a bakery in a city that sorely lacks them, use an existing business model, open your bakery, put in some serious work and it should be enough to meet the customer demand.

In contrast, if you want to create something totally new or soon to be outdated, you will have to push the existing boundaries, which may push you to start a new business model. But we will see that sometimes, the most innovative companies apply old business models.



## New uses out of... old things

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Do you think that large, hyper-innovative global companies like GAFAM (Google, Amazon, Facebook, Apple, Microsoft) have developed novel and ingenious business models?

You may be surprised!

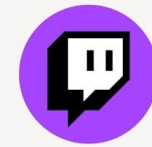


## Facebook and Instagram

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You probably know that Facebook and Instagram generate an important part of their revenues with... Advertising.

This business model is not new. Radio stations, newspapers and television channels have always been using this model.

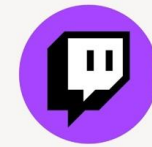


## Netflix and Amazon

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Netflix, and also to a lesser extent Amazon, generate part of their revenue via the subscription principle.

For a very long time, telephone operators or public transport companies have been working using this model.

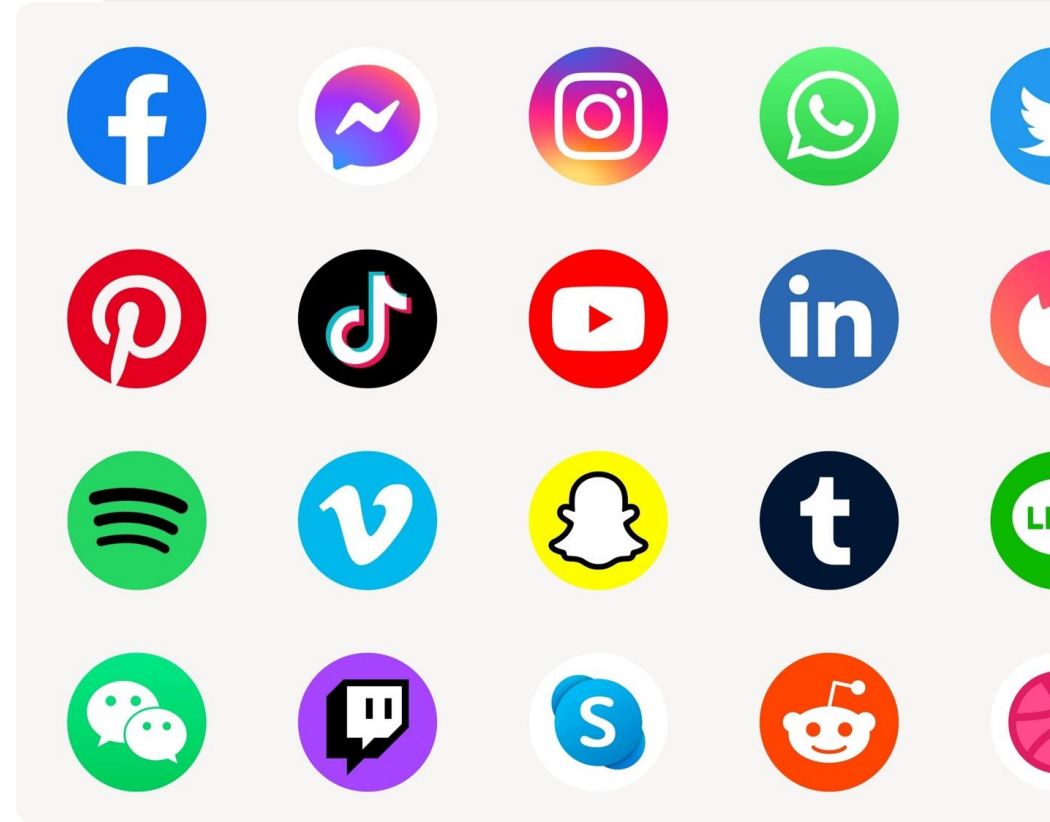


## Airbnb and Uber

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Airbnb or Uber use the commissioning model.

This is the business model of real estate and car salesmen/saleswomen.



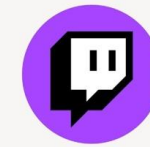
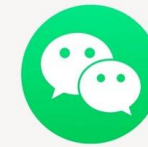
## Kickstarter

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Crowdfunding platforms such as Kickstarter seem innovative (and they are).

They use a pre-funding model which has been around a long time. When you buy a ticket for a show or a concert, sometimes more than a year in advance, you are pre-financing the show.

If you buy an apartment off-plan before it is even built, you are pre-financing its construction.



## New uses out of... old things

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What is innovative in the examples we have just analysed is not the singularity and uniqueness of their business model, but the way that they update existing and well-known business models.

Rather than reinventing the wheel, think about how you can use old concepts in new and changing environments.





# Chapter summary

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**1**

A business model is a document that shows how your business works in its different parts to make money.

**2**

There are hundreds of different business models. Every type of business model is suitable for one or several business industries and business contexts, but not all.

# Chapter completed!

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Congratulations! You have successfully completed this chapter!

## Summary of acquired skills

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1

You are now familiar with various popular business model types.

2

You are able to understand and complete your business model canvas.



## What is next?

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Now you can either repeat this chapter or follow our study recommendation by clicking on one of the buttons below:

[Restart](#)[Next](#)



## Business strategy

It looks like a magic formula. Two words that by themselves will determine the success or failure of your future business. Yet, business strategy is an abstract and complex notion that it is time to understand.

# What will you learn in this chapter

- 1 What is a business strategy.
- 2 Why you need to work actively on your business strategy.
- 3 Different types of business strategies.
- 4 An example of a business strategy.





## What is a business strategy?

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The success of a company depends a lot on its strategy to conquer a market and make a profit.

Globally, a business strategy is a plan to enter a market, make a place for yourself, grow in it and adapt over time.

In other words, a business strategy is a plan to achieve your business goals (sales goals, reputation, growth, product diversification, etc.).





# What is a business strategy?

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Be careful not to confuse strategy and tactics.

A strategy aims to define a plan in order to achieve the long-term goals of the business.

Tactics are sets of actions to reach a specific goal of your business strategy.

In other words, the strategy is the program, the tactics are the content (the set of actions) to reach this program.

So, you understand, a business strategy is a plan to make your business better fit to your market. But what is this plan based on? The answer is simple: on your market study.

The data from your market study should drive you to the most appropriate strategy to follow. Your market research will give you ideas about what works well, what doesn't work, what is outdated and what represents future opportunities you should take advantage of. These elements are carefully considered when setting a business strategy.

Now you might wonder: what is the link between the business model and the business strategy?

In fact, the business model is only a part of your business strategy. The business model is a tool to help you formalize and build a part of your business strategy.

To illustrate it with an analogy: If your strategy is a tree, your business model is the trunk.

# Why do you need to work on your business strategy?

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What are your strengths? Your weaknesses? The opportunities given by the market? Its threats? How do you plan your business development in light of this information?

Without a strategy, one can easily get lost, become confused, disorganized or even incoherent. A well-thought-out strategy is a tremendous help to avoid these traps, that are highly detrimental in too many business creations.

Here are four reasons why you should work on your business strategy.

The next slide shows 4 tips for working effectively on your business strategy.



# 4 tips to work effectively on your business model

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## Set a course

How can you go anywhere if you don't know where you are going?



## Set goals

Having specific goals allows you to put in place the appropriate tactics to achieve them.



## Make the most of the market

A strategy is all about making the most of market opportunities.



## Differentiate yourself

How can you add value if you don't bring your personal touch?

## Different types of strategies

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There is not only one business strategy.

In fact, several different strategies together form the overall strategy that defines the business.

We will see what these different types of strategies are.



# Financial strategy

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A financial strategy can be defined as the action plan intended to allow the company to reach a financial balance. Thus, the objective of a financial strategy is different depending on if it is short, medium or long term.

- In the short term: the financial strategy aims to enable the business project to see the light of day, i.e. to gather the necessary funds to launch the business in the appropriate conditions).
- In the medium to long term, the financial strategy aims to enable the business to grow and to diversify its activities and to adapt to the evolutions of the market and/or to survive.



# Financial strategy

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There are several types of financial strategies. We will not detail all of them, but, for example, we have:

- Self-financing: A method with which a company finances entirely its needs (investments for example) through its own funds (partners' contributions, cash flow generated in prior years etc.).
- The professional loan: An external source of finance by which a banking or financial institution provides a loan to the company.
- Company subsidies: During the creation or the development of a company, numerous public and private aids can be made available for the entrepreneur.





## Commercial & Marketing strategy

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The commercial strategy gathers all the methods and solutions used to adapt your offering of products/services to the demand of your potential customers, but also to pitch your business against the competition within your market.

Your commercial strategy is a strong determinant of your growth and the sustainability of your business venture.



# Commercial & Marketing strategy

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Some commercial aspects of your commercial strategy are:

- Your price and product range policy.
- Sales and services for your customers.
- Your sales distribution channels.
- Your online (digital) communication (social media, website, sales platforms, Google ads, SEO, etc.).
- Your offline communication (flyers, business cards, sponsoring, goodies, etc.).



# Human resources strategy

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The human resources strategy is defined as the way you organize your human resources to achieve your business objectives.

- Will you hire employees? Or will you work with subcontractors? Maybe both?
- How do you plan the development of your employees' skills or even your own skills as the business grows?
- How do you plan to manage resignations, sick leaves, and loss of motivation?

Working with humans requires constant adaptation to deal with unexpected situations. You need to be prepared.



# The overall business strategy

Your overall business strategy is the sum of all the sectoral strategies (marketing, finance, human, etc.) that you have worked on previously.

The key word here is consistency. All your sector strategies must be consistent with each other.

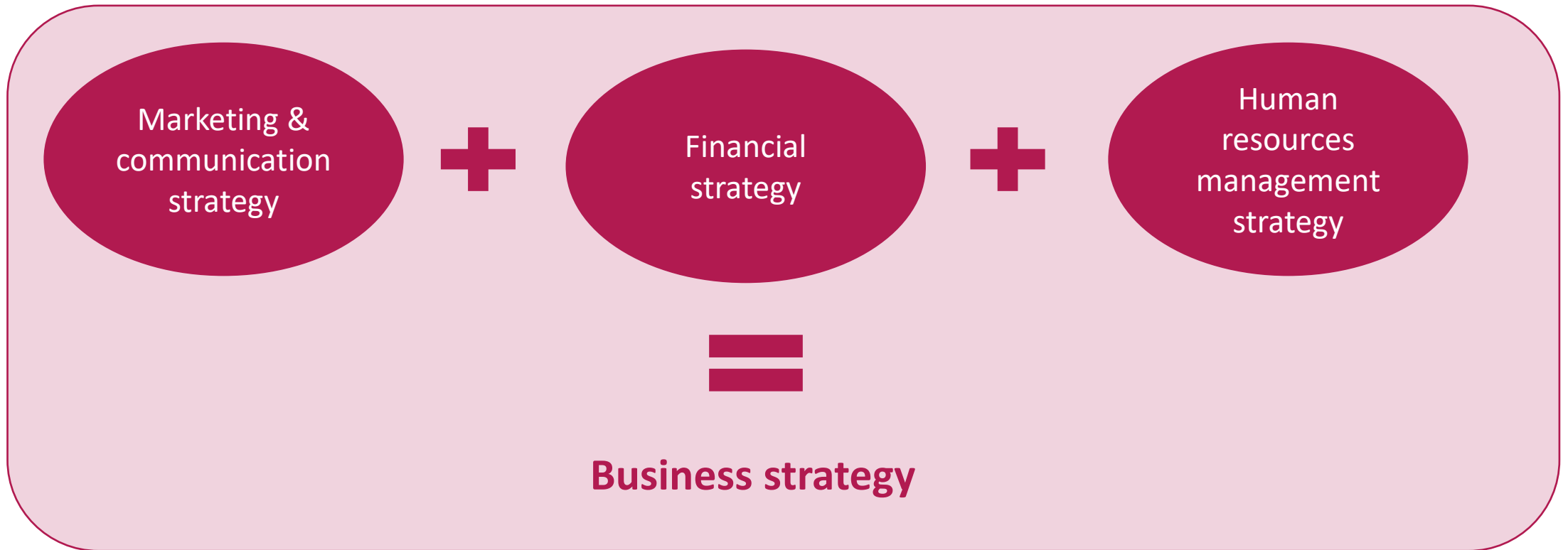
If you plan a marketing strategy, but your financial plan and your human resources organization do not follow it, your overall strategy will be fragile or unrealistic.

In the next slide, you will find an illustration of a coherent global strategy.



## The overall business strategy

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# The link between market study and business strategy

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Most of the information you collect during your market study will give you insight into your business strategy.

Indeed, your market study will allow you to observe and analyse what is done or not done in your market (by your competitors for instance), what seems to work well, what does not work at all etc.

All this information allows you to refine your strategy in order to select the best and put aside the least relevant.

Your business strategy is the result of the combination of the information of the market study.

A superficial market study including few and vague information about the best and the worst of your market gives fewer chances for creating a relevant business strategy (which is based on rich and complete information).

If you have not already worked on your market study, we recommend you the BUSINESS 04 “Market study” module.



## Example of a business strategy

Let's be concrete and take the example of a company to analyse a business strategy.

We can imagine that you manage a company that specialises in remote surveillance and home alarms (against burglary).

What might the different stages and actions of setting your business strategy look like?

This is what we will see.



## Home alarm business

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Let's imagine that you have been the manager of a home alarm company for 10 years. 70% of your clientele are ageing people who say they are worried about being burgled at home. One day, you are introduced to the Hands-on SHAFE modules and while reading the module **BUILT 06 Mobility at home** you have an idea. Given your clientele of ageing people, you decide to diversify your offering and develop technologies to facilitate the mobility of ageing people at home.



**BUILT**

## Home alarm business

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Following your readings of the Hands-on SHAFE modules, you decide to research the area further. You learn more about domestic accidents related to falls at home, about the changing demographic trends of ageing people living at home and about the existing technologies to improve safety at home.

After conducting market research, you realize that mature technologies already exist and are sold in large quantities in many cities except your own.

Installing and repairing these technologies requires similar skills to those needed to install/repair home surveillance cameras and alarms, skills that you have acquired and mastered over the past 10 years.



## Your financial strategy

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First of all, you must estimate the cost of developing this new business.

After having identified the material required for the installation of a fall detector system, you draw up the investments to be made to equip a 100 square metres house (the average size of a house in your area). Several cameras and dozens of sensors are necessary.

You estimate that to equip a house of 100 square metres would cost you 2000€ of material.

You do not have enough cash flow to build up a stock of several fall detector systems. What can you do?



## Your financial strategy

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You decide to operate without having any stock. You will order the fall detector systems from your supplier for each customer order.

Moreover, you will ask for a 30% deposit from your customer in order to cover a good part of the purchase of the fall detector system from your supplier.

In this way, you are able to develop this activity without impacting your cash flow balance.

However, this activity will require some investments: a van and various tools. These investments will be financed by the company's own funds built up after years of profits.









## Your commercial strategy

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You have planned a communication campaign on social networks.

You plan to make a promotional video clip to be broadcasted on a large scale to an audience of 50/60-year-olds who are potentially looking for home solutions for their ageing parents who they are taking care of.

Finally, you will create a business brochure that will be shared with public institutions in charge of the promotion of the ageing well in your city. Some general practitioners will be approached to promote the brochure also.



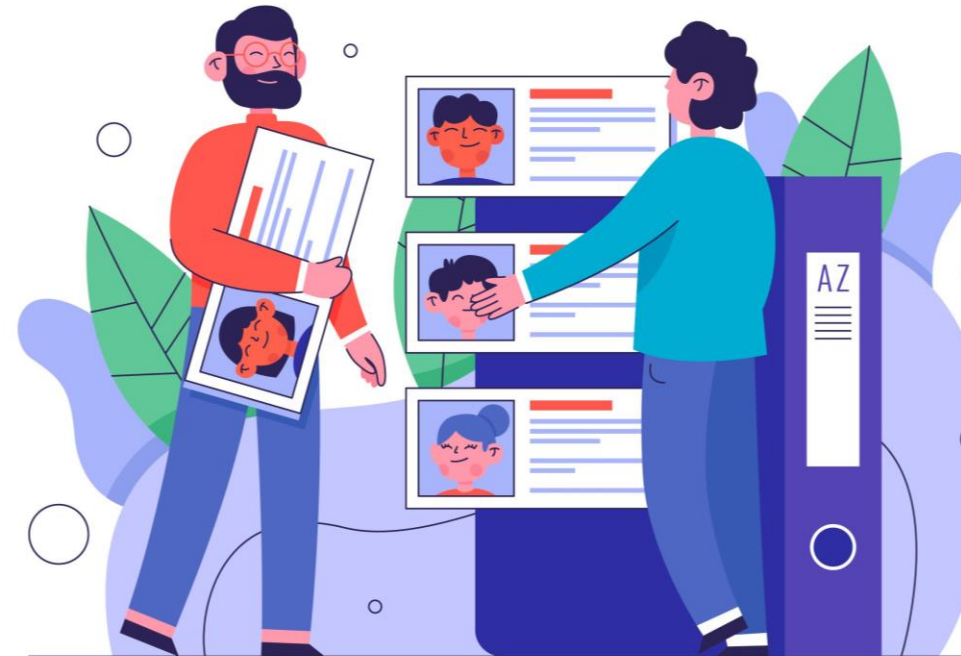
## Your human resources strategy

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This new activity will require a new employee. Installing a home fall detection system takes between one and two days depending on the size of the house.

You expect to do ten to fifteen installations per month. It will therefore be necessary to recruit a full-time person.

Moreover, this new employee will also have to be regularly trained in order to keep up with the rapid technological developments in this domain. By the way, you identified a two-week training course to learn the basics of fall detector system installation and maintenance.



## Your overall strategy

---

In summary, your global strategy consists of hiring and training a new employee that will be in charge of the installation and maintenance/repairs of the fall detectors.

This new activity will have no significant impact on the company's cash flow. The investments will be totally covered by the company's own funds, so its debt ratio will be unchanged. A debt ratio compares the debt of your business with the shareholders' equity.

Then, you will actively work on building strong partnerships with public and private companies that will have an interest (financial or not) in promoting your business.



# Chapter summary

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**1**

A business strategy is a plan to enter a market, make a place for yourself, grow in it and adapt to it over time.

---

**2**

Without a strategy, one can easily get lost, become confused, disorganised or even incoherent.

---

**3**

Most of the information you collect during your market study will give you insights into your business strategy.

# Chapter completed!

---

Congratulations! You have successfully completed this chapter!

## Summary of acquired skills

---

1

You know what a business strategy is and why working on it is important.

2

You know how your market study will directly feed your business strategy.



## What is next?

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Now you can either repeat this chapter or follow our study recommendation by clicking on one of the buttons below:

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## How to fix prices

When it comes to business strategy, one of the most common questions is: how to set your selling prices?  
This chapter aims to help you to fix your prices.

## What will you learn in this chapter

1 Difficulties about fixing the right prices.

2 How to fix relevant prices.



## Difficulties about fixing prices

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Fixing a price is a difficult undertaking.

How to be sure to be competitive without having too low or too high prices? How do you know if your prices are right?

That's what we'll see in this chapter.



## Being competitive

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Being competitive means offering a product/service that meets the needs and expectations of potential customers at a price they are willing to pay.

Being competitive implies a notion of competition with your competitors because we are only competitive in comparison with others.

So, being competitive means offering the best ratio between the perceived value of your product/service and its price.

In your range of products/services, which price/value ratio do your customers expect?

The more you respect this ratio, the higher your chances to be competitive.



**SPECIAL  
OFFER**

# Prices are too high

---

What happens when your **prices are too high**?

It means that there is a **mismatch between your price and the perceived value of your product/service**.

If your prices are too high, the more competitors there are in your market, the less likely customers are willing to pay for your products/services.

If you sell basic necessities and you are alone in your market, then people will probably pay for your products, even if prices are too high.

However, your company's image will probably be damaged.

Moreover, if a competitor enters the market with a better price/perceived value ratio, you risk losing a large part of your clientele.

If your prices are too high and you're not alone on your market and/or you sell non-essential products, you won't have a lot of customers and your business will quickly be in trouble.

If customers think that your prices are too high, you likely need to do one or several of these actions:

- You need to **improve the quality or the perceived value** of your products/services;
- You need to **improve the terms and conditions of sale** and make them better than what already exists;
- You need to **lower your prices**.

## Prices are too low

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If your prices are too low, the negative effects on your business development could be as important as when prices are too high.

What does it mean when your prices are too low?

It means that your prices are too close to your production costs. In other words, that your margin is too low to have a profitable business.

In the next slide, we will learn more about production costs.





# Production costs

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Production costs are simply what it costs you to produce a unit of product or to provide a service.

For instance, if you sell healthy meals for ageing people, some of your production costs will be:

- The cost of meal ingredients;
- Electricity/gas/water (oven, hotplate etc.);
- The rent for your food preparation premises;
- The wages of your employees;
- Bank account fees;
- Insurance charges;
- & many more.

**If you divide all of these costs by the number of products made, then you have the production cost by unit of product/service.**

Let's say all of the costs to make 100 healthy meals amounts to 800€ (meal ingredients, electricity, bank account fees etc.).

The cost of production of one unit of product, i.e. one meal, is  $800\text{€}/100 \text{ meals} = 8\text{€}$ . Each meal produced costs you 8€.

Let's conclude:

- If you sell a meal for 11€, you earn 3€ profit per meal (11€ of sale – 8€ of production costs).
- If you sell your meal for 7€, you will lose 1€.
- If you sell your meal for 8€, you won't gain or lose anything. You will just be able to cover your exact expenses.

## Fixed and variable costs

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Let's take a quick look at the concept of cost variability.

Some costs are said to be "**fixed**". This means that **they will remain the same** regardless of the quantities produced and/or sold.

Other costs are **variable**. Their **cost depends directly on the quantity** produced and/or sold.

Among the fixed costs we can think of the rent or the cost of your internet subscription. Regardless of the number of units of product sold, you will always pay the same rent or the same internet bill.

In contrast, variable costs include product packaging or the raw materials used in the manufacture of the products.

Indeed, if you sell 10 or 100 units of product, you do not pack the same quantity and, consequently, you do not buy the same volume of packaging. You also don't buy the same volume of raw materials for manufacturing 10 or 100 products.

This concept of cost variability is important when working on your production costs.

You will learn more about it in the next training module about financial forecasts.

## Prices are too low

---

As you have just seen in the previous slides, being able to deal with your production costs is extremely important to fix your prices properly.

If you cannot break down your production costs by unit, you won't be able to know your net margin on each sale. A net margin is the turnover you make, when you have already paid all the business's expenses, like employees. Consequently, your prices may not be appropriate for the cost.

If your prices are too low, not only will you jeopardize your financial balance, but you will tarnish the image of your activity as we saw.

Many marketing studies showed that people from all over the world associate low price with low quality.

In people's minds, if you are cheaper than your competitors, your products/services and your company, in general, are cheaper than others.

Maybe being cheaper is part of your business model, in that case, it could be a good thing, but as a common rule, it's not good for your reputation.

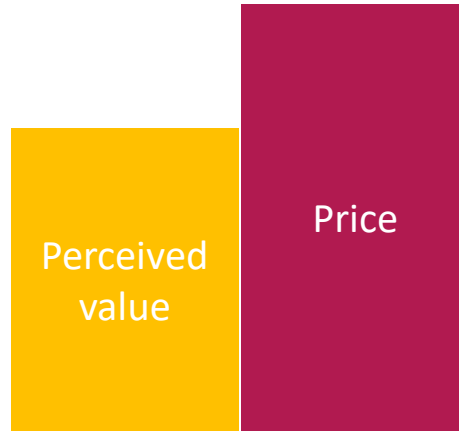
So, in order to preserve your financial balance and your reputation, be careful that your prices are not too low.

# The right price



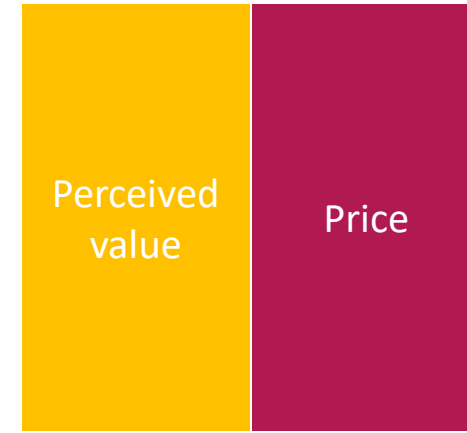
## Prices are too low:

- Risk of financial imbalance and, consequently, unprofitable business.  
*and/or*
- Risk to your image and reputation (being associated with “poor quality”).



## Prices are too high:

- Risk of not attracting enough clients and, consequently, unprofitable business.  
*and/or*
- Risk to your image and reputation.



## Prices are good:

- From a client’s point of view, your prices are in line with the value of your products/services. The ratio price/value fits their expectations.

## The psychological price

---

The psychological price is the price that a majority of consumers consider acceptable and fair for the proposed service or product. This notion is gradually evolving and depends on trends and habits of the time. For example, before the emergence of low-cost airlines, the psychological price of an airline ticket was higher than now. The psychological price of a telephone or internet subscription has dropped over a few years: now, in most countries, a telephone/internet subscription is half the price of a few years ago.

On the other hand, the psychological price of fuel has increased in recent years in most countries. Drivers are now willing to pay more than before, often because they have no choice.

In fact, the concept of choice (related to offering diversity and market size) is an important determinant of psychological price.



## Competitors' prices

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Finally, when fixing your prices, you have to refer to your competitors' prices. When entering a market, you always have to compare your products, services and value/price ratio with the ones of your competitors.

With equal perceived value [compared to your competitors']:

- If your prices are higher, you have to improve the quality or value of your products/services or lower your prices.
- If your prices are lower, it could be a very good thing. Make sure it is not at the expense of your financial balance or your image/reputation.
- If your prices are closely matched to your competitors' prices, try to differentiate your products and services from your competitors in order to build added value.





## Other factors that influence the price of your products and services

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Besides the three main factors we have seen, other factors can influence the price of your products and services.



## The degree of novelty and innovation of your offering

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If your offering is new and you need to take the time to make your products known to customers, it may be appropriate not to overprice.

On the other hand, if your products are rare and represent the cutting edge of innovation, you will probably be able to increase your prices compared to your competitors' prices, because innovation represents often important investments.

So, depending on your situation, for instance, let's imagine that you have made a place for yourself in a competitive market, you may have to charge very high prices.



## The type of market

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Whether you are in a seasonal and tourist market, for example, ice cream, your prices and the places where you sell your products may vary according to the time of the year.

Ice cream sold on a beach in a fancy resort will not be the same price as if you were selling it in a small town at the end of the summer season, even if you use the same ingredients to make it.

If you sell a product to individuals and professionals, the prices charged to these two types of customers will be different. If you sell computers, your prices will be different depending if your customer is professional or not.



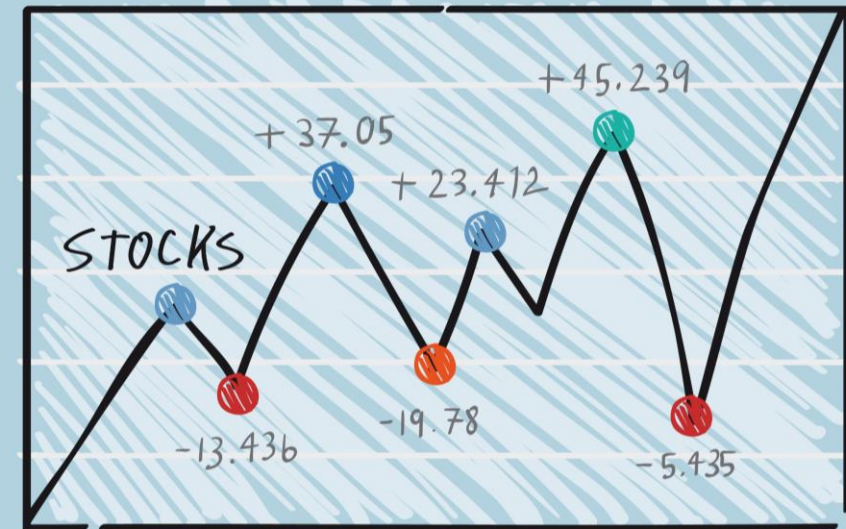
# Price elasticity

Price elasticity is a measurement of the change in consumption [of a product or service] in relation to a change in its price.

For example, gasoline has little price demand elasticity. Drivers will continue to buy gasoline in the same quantity regardless of its price because they need their car to go to work and do their essential shopping.

On the other hand, fast food is very elastic. If a fast food chain doubles its prices overnight, it will certainly lose a great part of its customers.

The more elastic your prices are, the more vigilant you should be about increasing your prices because its effect on your customer volume can be considerable.





## Examples of pricing strategies

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In the next slides, you can find some common examples of pricing strategies.



## Offensive price (Attracting people through low prices)

---

Marketing strategy	Price strategy
<ul style="list-style-type: none"><li>• Penetrate a market quickly.</li><li>• Gain market share quickly.</li><li>• Aim for a leading position in the short term.</li><li>• Build a large customer base.</li></ul>	<ul style="list-style-type: none"><li>• Define an attractive price (usually cheaper than competitors' one for the same quality) to maximise the number of customers.</li></ul>

### Industries potentially concerned by this strategy

- Every industry except:
- Luxury industry



## Competitive market

---

Marketing strategy	Price strategy
Avoid starting with an expensive price and rely on other strengths of your products and services to build differentiation.	Align your prices with those of the market but make a difference in product value.

Industries potentially concerned by this strategy
Every industry except: <ul style="list-style-type: none"><li>• Discount/low-cost industry</li></ul>

## Maximizing profitability

---

Marketing strategy	Price strategy
Adopt a high-end model. Enhance the image that customers perceive of your offer.	Charge high prices adapted to a premium segment. <i>(used in the luxury sector for instance)</i>

Industries potentially concerned by this strategy
<ul style="list-style-type: none"><li>• Clothes</li><li>• Cosmetics &amp; beauty products<ul style="list-style-type: none"><li>• Jewellery</li><li>• Cars</li></ul></li><li>• Hotels and restaurants</li></ul>

## Seasonal or fluctuating market

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Marketing strategy	Price strategy
Change your prices according to the characteristics of the demand and the constraints of your offer.	Practice yield management, a business practice that consists of varying prices according to consumer demand behaviour. This technique is used in flight and hotel reservations, for example. Depending on the occupancy rate and the season, a hotel will charge different prices for its rooms.

### Industries potentially concerned by this strategy

- Booking-based industries: airlines, hotels
- Tourist-based industries: ice cream, recreational activities (karting, laser game etc.)

# Chapter summary

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**1**

Fixing prices is a balance between production costs, competitors' prices and the expected value the customers assess your product.

---

**2**

The right price depends, to a great extent, on your market and your product and service characteristics.

# Chapter completed!

---

Congratulations! You have successfully completed this chapter!

## Summary of acquired skills

---

1

You have a better insight on how to fix your prices.



## What is next?

---

Now you can either repeat this chapter or follow our study recommendation by clicking on one of the buttons below:

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# Conclusions

---

**1**

Business models and strategies are part of a plan that describes how your business is supposed to grow and make money.

---

**2**

The clearer your business vision and the more detailed your market study is, the better the chances are that your business strategy is relevant.


---

**3**

Don't hesitate to get help to build your business strategy.

# Quiz

Click the **Quiz** button to edit this object

 **BUSINESS** **MODULE 5** Business model and strategy

A business model is a plan that details how a company expects to make money.

True

False

# Module completed!

---

Congratulations! You have successfully completed this module!

## Summary of acquired skills

---

**1**

Building a business model and a business strategy.

**2**

Fixing your prices.



## What is next?

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