



WWJMRD 2018; 4(11): 8-11
www.wwjmr.com
International Journal
Peer Reviewed Journal
Refereed Journal
Indexed Journal
Impact Factor MJIF: 4.25
E-ISSN: 2454-6615

Laxman Pokharel
1PhD Scholar, Mewar
University, Rajasthan, India

Bihari Binod Pokharel
Professor, Tribhuvan
University, Kathmandu, Nepal

Cost Based Pricing Methods of Small Scale Industries of Mid-Western Region, Nepal

Laxman Pokharel, Bihari Binod Pokharel

Abstract

Every production industry has their system of pricing of their goods and services. Cost based pricing is one of the pricing methods of determining the selling price of a product by the company, wherein the price of a product is determined by adding a profit element (percentage) in addition to the cost of making the product. Most of the Nepalese industries are involved in processing and manufacturing of food items, consumer and household goods, and textiles and related products, both for exports as well as the domestic market. The main aim of this study was to identify the cost based method of small scale industries of mid-western region of Nepal. The study was conducted among the 264 industries of three districts: Jumla, Banke and Dang. The findings of this study shows that majority of small scale industries had considered the markup pricing method then second highest number also considered the target return method. Comparatively very low industries had followed the break-even analysis during the price fixing. There was no significant difference between the districts regarding the cost-based method.

Keywords: Cost, Industries, Nepal, Price, Small scale

Introduction

Small-scale Industry is playing a vital role in the growth of national economies the world over and is considered to be the engine of growth in most countries. The small Scale Industries are labor intensive and provide huge amount of employment in developing countries like Nepal. The emphasis on Small Scale Industries has always been an integral part of the Nepalese Industrial strategy. It was envisaged that Small Scale Industries would play an important role as producer of consumer goods and absorber of surplus labor thereby addressing to the problems of poverty and unemployment. Other advantages of small industries are that they ensure a more equitable distribution of national income, enhance balanced regional industrial development, act as a nursery for entrepreneurship and facilitate mobilization of local resources and skills which might otherwise remain underutilized.

Pricing has always been major decision areas of Small Scale Industries. Most of small firms set prices based on cost, competition or customer's value perception of their products and services. Most of the Nepalese industries are involved in processing and manufacturing of food items, consumer and household goods, and textiles and related products, both for exports as well as the domestic market. Rice, pulses, oil and flour mills, dairy, aerated soft drinks, fruit juices and processed products, noodles, biscuits and light snack products, chocolates and candy, mineral water, dried vegetables, and some other household utilitarian and consumption goods have dominated industrial activities in Nepal.

In any companies or industries, price is one significant factor in attaining high market share. Main pricing objectives are, profit maximization, high market share, to attain status quo by stable price and meeting competition in the market (Singh, 2013). Various previous literatures have explained about the importance of pricing decision for the economic performance or industries. Nagle and Holden (1995, p. 1) has explained that:

"...if effective product development, promotion and distribution sow the seeds of business success, effective pricing is the harvest. Although effective pricing can never compensate for poor execution of the first three elements, ineffective pricing can surely prevent those efforts from resulting in financial success."

Correspondence:
Laxman Pokharel
1PhD Scholar, Mewar
University, Rajasthan, India

Moreover, Marn and Rosiello (1992), Simon (1992), Lovelock (1996), and Shipley and Jobber (2001) have suggested that pricing is the only element of the marketing mix that produces revenues for the firm, while all the others are related to expenses. Diamantopoulos (1991) has also argued that price is the most flexible element of marketing strategy in that pricing decisions can be implemented relatively quickly in comparison with the other elements of marketing strategy.

Cost based methods are Cost-plus method, target return pricing, breakeven analysis, contribution analysis and marginal pricing. In cost-plus method, a profit margin is added on the service’s average cost. Secondly, target return pricing determines the point at which the firm targets the rate of return. Break-even analysis is focused at the point where total revenues equal total costs. Contribution analysis is slightly different from break-even analysis in this regard that it only considers the direct cost of a product or service. Lastly, marginal pricing is placed below total and variable costs (Accounting Tools, 2017). Hall and Hitch (1939) found that approximately 80% of the firms they investigated used cost-plus pricing. Shipley (1983; 1986) found that 59% of the firms in his study reported using cost-plus pricing on all their products. Nagtegaal (1974) reports ‘a definite cost-orientation in pricing in Germany’. Wied-Nebbeling (1975) reports over 70% of respondent firms using cost plus pricing at least as a guideline. As a dynamic policy, cost-plus pricing is more flexible than has commonly been realized (Hanson, 1992). Nagle and Holden (1995) to suggest that pricing is the most neglected element of the marketing mix. Within this context, the empirical research that has been conducted on

the field of pricing is very limited in the context of small scale industries of mid-western region of Nepal, while this is even more evident in the case of services. So the study is set its objective to identify the practice of customer based method of pricing adopted by the small scale industries of Nepal.

Materials & Methods

The study was conducted in the three districts of Mid-western region of Nepal among the 264 small scale industries. It was cross-sectional study; data collected from the one visit by using the structured questionnaire survey. The study was based on the descriptive design as well as it was quantitative study. The study used the simple random sampling technique to select the industries from the total list. There were total 5279 industries working in the selected three districts (Dang = 2285, Banke = 2368, and Jumla = 626), among them 5% sample was taken from each districts. The collected data was analyzed from statistical software and findings are presented in the tabular form in below section.

Results & Discussions

The study was conducted to identify the pricing method following the customer based method adopted by the small scale industries of Mid-western region of Nepal. The below data presented in the Table 1 shows that there were total 264 small scale industries selected for the study to know their pricing method. The distribution shows that 43.2% from Dang, 44.7% from Banke and 12.1% from Jumla. The sample was taken from the total number of small scale industries on the basis of weightage of size.

Table 1: Districts’ Name

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Dang	114	43.2	43.2	43.2
	Banke	118	44.7	44.7	87.9
	Jumla	32	12.1	12.1	100.0
	Total	264	100.0	100.0	

Source: Field Survey, 2018

Cost Based Pricing Methods

Diamantopoulos (1991, p. 139) suggests that pricing objectives can “fall under three main headings relating to their content (i.e. nature), the desired level of attainment and the associated time horizon”. While the pricing objectives provide general directions for action, Oxenfeldt (1983) defines pricing methods as the explicit steps or procedures by which firms arrive at pricing decisions.

The respondents were asked about the method of pricing fixing adopted by their industry. The data shows that 91.2% respondents of Dang, 89.8% of Banke and 62.5% agreed that they adopted the Markup pricing method. It shows that majority of industries of all three districts adopted that method. In total, 87.1% agreed and 6.1% strongly agreed about it.

Table 2: Cost Based Methods

		Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree	Total
Markup Pricing	Dang	0.0%		1.8%	91.2%	7.0%	100.0%
	Banke	0.0%	1.7%	6.8%	89.8%	1.7%	100.0%
	Jumla	0.0%	6.2%	12.5%	62.5%	18.8%	100.0%
	Total	0.0%	1.5%	5.3%	87.1%	6.1%	100.0%
Target Return Pricing	Dang	0.0%	1.8%	7.0%	89.5%	1.8%	100.0%
	Banke	0.0%	1.7%	27.1%	69.5%	1.7%	100.0%
	Jumla	0.0%	6.2%	6.2%	87.5%	0.0%	100.0%
	Total	0.0%	2.3%	15.9%	80.3%	1.5%	100.0%
Break-Even Analysis	Dang	0.0%	47.4%	24.6%	28.1%	0.0%	100.0%
	Banke	0.0%	28.8%	39.0%	32.2%	0.0%	100.0%
	Jumla	6.2%	50.0%	25.0%	18.8%	0.0%	100.0%
	Total	0.8%	39.4%	31.1%	28.8%	0.0%	100.0%

Source: Field Survey, 2018

It is stated in the literatures that target return pricing – the price is determined at the point that yields the firm’s target rate of return on investment (McIver & Naylor, 1986; Meidan, 1996). The study had explored this practice also among the small scale industries of study districts. The data presented in Table 2 shows that in total 80.3% agreed and 1.5% strongly agreed that the adopted the ‘Target Return Pricing’ method in their industries. The district wise response shows that 89.5% of Dang, 69.5% of Banke and 87.5% of Jumla agreed that they had adopted this method for price fixing.

Within the cost based method, the study had measured the Break-even analysis method also. The literatures said that ‘Break-even analysis – the price is determined at the point where total revenues are equal to total costs’ (Channon, 1986; Lovelock, 1996). In the context of Nepalese small scale industries, this method was not so popular and adopted by the majority of industries because the findings presented in the Table 2 shows that higher number (39.4%) of total respondents disagreed about the adoption of break-even analysis method, 31.1% had given neutral response and 28.8% agreed on it. The distribution of response shows

that district wise also, comparatively majority of respondents disagreed. The data shows 47.4% of Dang, 28.8% of Banke and 50% of Jumla had given disagree response on it. It clearly indicates that this price fixing method was not correctly applicable in Nepal.

One previous literature conducted on ‘Economic potential and marketing trend of bamboo in Nepal’ shows that there was no fixed market, no fixed price and no guarantee in selling the products were found to be the major problems for market development of the bamboo products (Jha & Yadava, 2015).

Differences of cost based method in study districts

The study had explored the relationship between the study districts on adoption of cost based pricing method. The study runs the ANOVA to see differences between the districts in their response. The statistical findings of ANOVA presented in Table 3 shows that there were no significant differences between and within groups of study district regarding the practice of cost based pricing method because the $p = .094$ which is greater than .05 significant levels.

Table 3: Differences of cost based method in study districts

ANOVA						
	Sum of Squares	df	Mean Square	F	Sig.	
Between Groups	5.281	2	2.640	2.381	.094	
Within Groups	289.386	261	1.109			
Total	294.667	263				
Multiple Comparisons						
(I) District	(J) District	Mean Difference (I-J)	Std. Error	Sig.	95% Confidence Interval	
					Lower Bound	Upper Bound
Dang	Banke	.11091	.13828	.423	-.1614	.3832
	Jumla	.45943*	.21065	.030	.0446	.8742
Banke	Dang	-.11091	.13828	.423	-.3832	.1614
	Jumla	.34852	.20987	.098	-.0647	.7618
Jumla	Dang	-.45943*	.21065	.030	-.8742	-.0446
	Banke	-.34852	.20987	.098	-.7618	.0647

*. The mean difference is significant at the 0.05 level.

Source: Field Survey, 2018

The multiple comparisons of districts show that there was significant difference between Dang and Jumla because $p = .030$ which is less than .05 significant levels whereas there was no difference between Dang and Banke ($p = .423$), and Banke and Jumla ($p = .098$).

Conclusion

Cost based pricing method is one very popular method adopted by many industries and production companies. Cost based pricing is one of the pricing methods of determining the selling price of a product by the company, wherein the price of a product is determined by adding a profit element (percentage) in addition to the cost of making the product. The study had collected the data from three districts: Dang, Banke and Jumla from the small scale industries. Regarding the objective of pricing method, under the cost based method, majority agreed (87.1%) markup pricing, and second highest number (80.3%) agreed the target return pricing and very less number (28.8%) agreed on break even analysis was considered during the price fixing. It was observed that Nepalese small scale industries did not prefer the breakeven analysis for the price determination because in this technique, industries

neither gain profit nor loss. But producer wants to gain the profit from business so industries gave value to the markup pricing and target return pricing. There was no significant difference between and within the districts regarding the cost based method of price fixing. The further research can be done to explore the practice of other pricing method adopted by the Nepalese industries.

References

- Accounting Tools. (2017, July 24). *Articles: Accounting Tools*. Retrieved October 11, 2018, from Accounting Tools: <https://www.accountingtools.com/articles/2017/5/16/cost-plus-pricing>
- Channon, D. (1986). *Bank Strategic Management and Marketing*. Chichester: John Wiley & Sons.
- Diamantopoulos, D. (1991). Pricing: theory and evidence – a literature review. In M. (. Baker, *Perspectives on Marketing Management* (pp. 61-193). Chichester: John Wiley & Sons.
- Hall, R. L., & HITCH, C. J. (1939, May 22). Price theory and business behaviour. *Oxford Economic Papers*, 12-45.

5. Hanson, W. (1992). The Dynamics of Cost-plus Pricing. *MANAGERIAL AND DECISION ECONOMICS*, 13, 149-161.
6. Jha, R. K., & Yadava, J. N. (2015). Economic potential and marketing trend of bamboo in Nepal: A case study from Rautahat District. *Banko Janakari*, 25(1), 63-75.
7. Lovelock, C. (1996). *Services Marketing, 3rd ed.* PrenticeHall, Englewood Cliffs, NJ.
8. Lovelock, C. (1996). *Services Marketing, 3rd ed.* PrenticeHall, Englewood Cliffs, NJ.
9. Marn, M., & Rosiello, R. (1992, September-October). Managing price, gaining profit. *Harvard Business Review*, 70, 84-94.
10. McIver, C., & Naylor, G. (1986). *Marketing Financial Services, 2nd ed.* Canterbury: The Institute of Bankers.
11. Meidan, A. (1996). *Marketing Financial Services.* London: Macmillan Business Press.
12. Nagle, T., & Holden, R. (1995). *The Strategy and Tactics of Pricing.* Prentice-Hall, Englewood Cliffs, NJ.
13. Nagtetaal, H. (1974). *Der Verkaufspreis in der Industrie.* Wiesbaden: Gabler.
14. Oxenfeldt, A. (1983, November). Pricing decisions: how they are made and how they are influenced. *Management Review*, 23-25.
15. Shipley, D. D. (1983). Pricing flexibility in British manufacturing. *Managerial and Decision Economics*, 4, 224-233.
16. Shipley, D. D. (1986). Dimensions of flexible price management. *Quarterly Review of Marketing*, 11, 1-7.
17. Shipley, D., & Jobber, D. (2001). Integrative pricing via the pricing wheel. *Industrial Marketing Management*, 30 (3), 301-14.
18. Simon, H. (1992). Pricing opportunities and how to exploit them. *Sloan Management Review*, 33 (2), 52-62.
19. Singh, M. (2013, April - June). Important Pricing Methods in 4P's. *International Journal of Management & Business Studies*, 3(2), 147-150.
20. Wied-Nebbeling, S. (1975). *Industrielle Preissetzung.* Tubingen: Mohr-Siebeck.