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Strategies for Increasing Your Markup

Eventually, most contractors come to the somewhat intimidating conclusion that if they want to create a sustainable and profitable business, they need to price their work high enough to cover production and overhead costs as well as to contribute to profit. This realization is frequently accompanied by feelings of panic and dread. After all, isn't there a risk that all your work will dry up if your prices are too high?

The solution, of course, is to perfect your marketing (or to start marketing, if you currently rely mostly on word of mouth) and to get some sales training. The chicken-and-egg situation then becomes one of trying to pay for sales training and marketing costs when you're barely making enough to cover production and put a few dollars in your pocket at the end of the year.

But let's say that you've already embarked on these marketing and sales ventures and are committed to raising your prices incrementally. Next, you might have the sinking feeling that you just sold a job or two at a markup you now recognize is too low. What can you do?

COME UP WITH A PLAN

First, come up with a strategy to transition from the markup figure you're using now to the new figure that you will eventually use to reach your target margin. However you design your strategy, you need to consider two key contributors to your margin: the markup you apply to your estimated costs; and the size of the job. With these figures in hand, you will be able to project the results of your strategy.

There are a few different ways to make this work. You could decide you'll mark up all jobs from now on at an additional X%. Or, if marking up larger jobs is intimidating, you may commit to increasing your markup on jobs between $X and $Y by one amount, and on jobs between $Y and $Z by another amount. Or, you could increase markups by X% on all jobs every month or increase markups by X% on each of your next jobs (see charts A and B).

In all cases, you need to identify three things:

1. Your anticipated sales volume (for a year)
2. The markups you intend to apply
3. The target margin you wish to achieve over a designated period of time (say, a year)

To create the examples in the charts, I used a simple calculator that yields the results of selling successive jobs at increasing markups. This allowed me to project what the markup on future jobs must be to achieve a particular target margin. Please note that the markup and margin figures I am using are based on actual figures from clients and do not represent my recommendations. Some benchmark figures for margins can be found in industry reports, but these figures may or may not be relevant depending on whether certain costs are classified as production costs, which affect your gross margin, or as overhead, which does not.

A. Increase Markup by 3% on Each Job

Anticipated total sales volume: $875,000
Target margin for the year: 19%

Job	Sale Price	Markup Used	% of Target Sales	Theoretical Margin	Margin Running Balance
Job 1	$175,000	12.50%	20.00%	11.11%	11.11%
Job 2	$175,000	15.50%	20.00%	13.42%	12.27%
Job 3	$175,000	18.50%	20.00%	15.61%	13.38%
Job 4	$175,000	21.50%	20.00%	17.70%	14.46%
Job 5	$175,000	24.50%	20.00%	19.68%	15.50%
Totals	$875,000		100.00%		

INCREASE MARKUP BY 3%

In the first example **(A)**, target sales for the year is $875,000; target achieved margin for the year is 19%; and current markup is 12.5%. The strategy here is to increase the markup by 3% on each job sold, irrespective of the size of the job.

For the sake of simplicity, in this first example, all the jobs have the same selling price. That means that if Job 1 has a selling price of $175,000 using a markup of 12.5% and Job 2 has a selling price of $175,000 using a markup of 15.5%, the costs to produce Job 2 are smaller.

Notice that the theoretical margin increases for each job (from 11.11% on the job with the 12.5% markup to 19.68% on the job with the 24.5% markup). Still, the running balance of the margins—15.50%—fails to meet

the target—19%—even though the projected sales volume of $875,000 is met.

VARIABLE JOB SIZE

Let's see what happens when the same conditions are in effect as in the first example, except the job sizes fluctuate significantly **(B)**. In this instance, because the higher markups were applied to larger jobs, the overall achieved margin—17.14%—is closer to the target 19%.

HIGHER VOLUME, MORE AGGRESSIVE INCREASE

Now assume we have a larger company with a higher sales volume and a more aggressive markup increase strategy **(C)**. This company's target sales for the year is $2,000,000; its target achieved margin for the year is 19%; and its current markup is 12.5%. In this case, the strategy is to increase the markup by 5% on each job sold, regardless of the size of the job.

To keep things simple, we'll assume all the jobs were sold at the same price. Notice that with greater markup increases (5% instead of 3%), this company comes closer to meeting its target margin, with an achieved margin of 18.46%.

EFFECT OF ONE LARGE JOB AT A LOW MARKUP

This is the same company as in the third example, but see what happens when it sells its largest job of the year at the old markup (12.5%), and the remaining projects that year are smaller **(D)**. This time the company doesn't come close to meeting its target margin.

BOTTOM LINE

If you have committed to increasing your prices to create a sustainable company (and maybe even get your life back), you can use a simple calculator—available as a download at jlconline.com/margin-calculator—to experiment with the results of increasing your markup. Remember that the size of the job to which the new markup figure is applied, in addition to the markup itself, will determine how quickly you can achieve the target margin you're aiming for.

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B. Variable Job Size

Anticipated total sales volume: $875,000
Target margin for the year: 19%

Job	Sale Price	Markup Used	% of Target Sales	Theoretical Margin	Margin Running Balance
Job 1	$50,000	12.50%	5.71%	11.11%	11.11%
Job 2	$85,000	15.50%	9.71%	13.42%	12.56%
Job 3	$225,000	18.50%	25.71%	15.61%	14.47%
Job 4	$175,000	21.50%	20.00%	17.70%	15.52%
Job 5	$340,000	24.50%	38.86%	19.68%	17.14%
Totals	**$875,000**		**100.00%**		

C. Increase Markup by 5% on Each Job

Anticipated total sales volume: $2,000,000
Target margin for the year: 19%

Job	Sale Price	Markup Used	% of Target Sales	Theoretical Margin	Margin Running Balance
Job 1	$400,000	12.50%	20.00%	11.11%	11.11%
Job 2	$400,000	17.50%	20.00%	14.89%	13.00%
Job 3	$400,000	23.50%	20.00%	19.03%	15.01%
Job 4	$400,000	28.50%	20.00%	22.18%	16.80%
Job 5	$400,000	33.50%	20.00%	25.09%	18.46%
Totals	**$2,000,000**		**100.00%**		

D. One Large Job at a Low Markup

Anticipated total sales volume: $2,000,000
Target margin for the year: 19%

Job	Sale Price	Markup Used	% of Target Sales	Theoretical Margin	Margin Running Balance
Job 1	$750,000	12.50%	37.50%	11.11%	11.11%
Job 2	$500,000	17.50%	25.00%	14.89%	12.62%
Job 3	$375,000	23.50%	18.75%	19.03%	14.10%
Job 4	$225,000	28.50%	11.25%	22.18%	15.08%
Job 5	$150,000	33.50%	7.50%	25.09%	15.84%
Totals	**$2,000,000**		**100.00%**		