

## Calculating the Discount Impact

Today, discounting is the norm rather than the exception. But when you discount you need to generate additional sales to make up for the cash you forgo in the discount.

Your business needs to generate sufficient cash to:

- Cover the cost of buying the next lot of stock
- Pay the costs of operation – wages, rent etc
- Return you, the owner, a profit.

Before you discount, think – how much more will I need to sell for the same returns?

Set out below is a table which may be of assistance in calculating how much you need to sell to generate the same level of gross profit dollars at varying discount levels. You all have different gross margins and differing promotional strategies so we have constructed a matrix, which highlights the number of units you will need to sell to give you the same cash that you would generate from a single sale at full price.

### Definitions:

**Gross margin** = (Selling price – cost price) / selling price x 100.

For example, you buy for \$50 and you sell for \$100. Your mark-up is 100% and your gross margin is 50%.

**Discount** = the amount, in percentage terms, taken off the selling price.

For example, a selling price of \$100 reduced to \$70 is a 30% discount.

**Volume calculation** = the number of units you need to sell to return the same gross profit you would have made from the sale of one unit at full price, as shown in the matrix. For example, if your normal gross margin is 50% (i.e. 100% mark-up) and you discount by 30%, you need to sell 2.5 units to generate the same profit it would yield at full price. That is an increase in sales of 1.5 units or 150%.

*Note: The GST impact has been excluded from all calculations.*

### The Discount Matrix

		% Gross margin							
		15	20	25	30	35	40	45	50
% Discount	10	3.00	2.00	1.67	1.50	1.40	1.33	1.29	1.25
	20	-	-	5.00	3.00	2.33	2.00	1.80	1.67
	30	-	-	-	-	7.00	4.00	3.00	2.5
	40	-	-	-	-	-	-	9.00	5
	50	-	-	-	-	-	-	-	-

### Worked Example

Cost price	\$50.00	Discount	30%
Gross Margin	50% (100% mark up)	New Selling Price	\$70.00
Selling Price	\$100.00	New Gross Profit	\$20.00
Gross Profit	\$50.00		

Volume calculation      \$50/\$20 = 2.5

That is, to generate the same gross profit (\$50) you need to sell 2.5 units @ 30% discount (\$20 x 2.5 = \$50).