



Jeans and Pricing

The Effect of a Discount

more money for shoes

The Effect of a Discount

Discounting or having a sale is often seen by a business owner as a great way to drum up sales and new customers for a business. However it's important to understand the effect this discount has on your profits, or the money that you get to keep after paying your costs.

The table below may look confusing but it demonstrates how much additional sales you need to make if you offer a discount, simply to make the same amount of profit as if you hadn't discounted the price.

For example, let's say Mary owned a clothing shop. She has a 60% gross profit margin on her clothing. So, if an item of clothing was selling in the store for \$100 then the cost of that item would be \$40 and Mary's gross profit is \$60. (The gross profit margin is \$60 or the profit divided by \$100 or the price).

Mary usually makes \$1,000 worth of sales per day with a gross profit of \$600. She decided to have a sale and discount her clothing by 20% but she wanted to make the same amount of profit so that she could pay her bills for the week. So, using the table below, we can see that Mary needs to make an additional 50% in order to make the same amount of profit. That means her daily sales during the sales needs to be \$1,500 ($\$1000 + \$1000 \times 50\%$). (Look across the top for the margin of 60% and then head down the rows until you reach the 20% price cut column, gives you the additional profit needed of 50%).

Margin→ Price ↓ Cut	10%	20%	30%	40%	50%	60%	70%	80%	100%
5%	100%	33.3%	20%	14%	11%	9%	8%	7%	5%
10%	-	-	50%	33.3%	25%	20%	17%	14%	11%
15%	-	-	100%	60%	43%	33.3%	27%	23%	18%
20%	-	-	200%	50%	66.6%	50%	40%	33.3%	25%
30%	-	-	-	200%	150%	100%	75%	60%	43%
40%	-	-	-	-	400%	200%	133.3%	100%	66.6%
50%	-	-	-	-	-	500%	250%	166.6%	100%

Once you know your margin, you can work out the additional sales that you need in order to maintain the same profit level if you were to discount your price.

Discounting or having a sale can be a way to let new customers test your product, to let customers test a product that is new and they haven't tried before or to move old stock. However it is important to understand the effect that this strategy has on your profits.