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Video Transcription: Understanding Mark-Ups

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Hello there, my name is Jacqui and this video is going to look at developing an understanding of mark ups.

A business is generally started to sell goods or to provide a service. For that business to be successful in the long run, it is essential that the selling price of the product or service being sold by the business is higher than the cost price of the product or service.

So, let's take a look at a retail business. Remember the business will incur costs in purchasing the item it intends to sell. These could include the purchase price of the items as well as any costs incurred to get the inventory to the condition and location from which it could be sold. All of these costs would be included in the cost of inventory or we could say in the cost price per unit.

The price at which each item is normally sold (or the selling price) will be higher than the cost price. The difference between the selling price per unit and the cost price per unit is referred to as the mark-up (or the gross margin).

Now a mark-up can be stated as a percentage of either the cost price or as a percentage of the selling price. When the mark-up is stated as a percentage of sales it can also be referred to as a gross margin. Let's think about this a little. Do you think it is correct to say that a mark-up on cost of 40% is the same as a mark-up on sales (or gross margin) of 40%?

The answer to this question is definitely NO, so this means that we need to be very careful to understand how the term mark-up is actually being used. Let's spend a little time trying to understand why. A mark-up on cost means that the mark-up is stated as a percentage of cost price. Cost is 100 percent and mark-up is 40 percent of cost, as selling price equals cost price plus mark-up. Selling price is 140%.

If an item, with a mark-up on cost of 40%, has a selling price of R280, what would the cost price and mark-up be? If the measure of mark-up is based on cost and the mark up is 40%, then the selling price is 140% of cost, so the rand amount of the cost price is calculated by multiplying the selling price by 100/140. The rand amount of the mark-up is calculated by multiplying the selling price by 40/140.

Do you see that the mark-up is NOT 40% of the selling price, as the selling price includes the mark-up? So, let's look at mark-up on sales (gross margin). A gross margin means that the mark-up is stated as a percentage of selling price. So Selling price is 100% and the mark-up (or gross margin) is 40% of selling price. As selling price less cost price gives you mark-up, the cost price would be 60% of the selling price.

So if an item, with a gross margin or mark-up on sales of 40%, has a selling price of R280, what would the cost price and mark-up amount be? Selling price is 100%, and we know that the cost price is 60% of the selling price of R280, so if the measure of the mark-up is based on selling price, the rand amount of the cost price is calculated by multiplying the selling price by 60/100.

Selling price is 100%, and we know that the mark up is 40% of the selling price, so the rand amount of the mark-up is calculated by multiplying the selling price by 40/100.

Do you see that gross margin on sales is exactly the same as a mark-up percentage calculated on sales? But a 40% mark-up on cost is not the same as a mark-up on sales or gross margin. This is because a mark-up on cost is quoted as a percentage of cost price and a mark-up on sales (gross margin) is quoted as a percentage of selling price.

Thanks for watching.