

## MARKUP AND MARGIN: What is the difference?

*Markup* is adding a percentage of the cost to the cost in order to reach a desired retail price.

*Margin* is the amount of profit produced in the sell of an item expressed as a percentage of the retail price.

**Example 1:** for an item that costs \$1.00.

*Markup:* If you want a 50% markup the item's retail price is \$1.50. The easiest formula for determining Markup is:  $\text{cost} \times (100\% + \text{desired markup \%}) = \text{Desired Retail Price}$

In our example of the item with a \$1.00 cost @ 50% markup this would be:  $\$1.00 \text{ times } 150\% = \$1.50$

*Margin:* What would be the margin in this example? Retail price of \$1.50 with cost of \$1.00 means that .50 or 33% of the selling price equals the *margin* also known as the *profit margin*. So what is the easiest formula for determining Margin?  $\text{Cost} \div (100\% - \text{desired margin}\%) = \text{Desired Retail Price}$ . In the example above that would look like  $\$1.00 \div (100\% - 33\%) = \text{DRP}$  or  $\$1.00 \div .667 = \$1.499$  or \$1.50 rounded.

Why is margin so important when markup is so much easier? Most accountants, tax professionals, and bankers talk in terms of "Business Profit Margin" Most financial reports and projections are based on Profit Margins. If your accountant says you need to be making a 33% margin on your retail pricing and you think this means "Markup" then you are setting your pricing substantially below the amount of profit you need to make. The higher the desired profit margin the greater the difference (loss!) in true profit.

**Example 2:** Your accountant tells you that you should be making a 50% *Margin* on your sells. You think he means *Markup* and proceed to price all your products using the *markup* formula. Your projected *margin* is 50% but the 50% **markup** results in a 33% *margin*! So for every \$1,000 in sells, you receive \$333 in gross profit but you really needed \$500 to produce your required "*Profit Margin*" of 50%. If your business had \$1,000,000 in sells, at the end of the year this miscalculation would result in an unanticipated loss of \$167,000 or 33.4% of your total expected operating profit for the year. Who can afford that!!

**Use the handout from tonight's class to complete the Comparison Chart below for clarification of the difference between Mark-up and Margin.**

Markup % of Cost	Margin % of Selling Price
	10.0
25.0	
	25.0
	30.0
	40.0
75.0	
	50.0

**Use the Profit Margin formula in Example 1 above to determine the answers to the following:**

Joe operates a local shoe store. He is operating on a 45% profit margin on children's and women's shoes and a 35% margin on men's shoes. Help Joe determine the proper selling price for each of the following items:

$\text{Cost} \div (100\% - \text{desired margin}\%) = \text{Desired Retail Price}$

Item	Cost	Retail price
Children's Sneakers	\$5.44	\$
Women's Sandals	\$9.87	\$
Men's Dress Shoe	\$22.31	\$