Gross and Net Profit

Gross profit

Gross profit is the profit that a business makes on its trading activity before any indirect costs are deducted.

Gross Profit = Sales revenue – Cost of sales

Net profit

Net profit is profit that a business is able to return to shareholders or reinvest into the business

Net Profit = Gross Profit – Expenses

Improving profit

A business can improve profit by …

Lowering costs

- Lowering costs could reduce quality
- Could affect the business's reputation

Increasing revenue

- Increasing prices could reduce sales
- Advertising could increase costs

Profit Margins

A profit margin is the ratio of profit compared to sales revenue.

Profit margins show a product's profitability

Gross Profit Margin

The Gross Profit Margin indicates the proportion of sales revenue that is turned into gross profit.

$$\text{GPM (\%)} = \frac{\text{Gross Profit}}{\text{Sales Revenue}} \times 100$$

The higher the percentage the better

Net Profit Margin

The Net Profit Margin indicates the proportion of sales revenue that is turned into net profit.

$$\text{NPM (\%)} = \frac{\text{Net Profit}}{\text{Sales Revenue}} \times 100$$

The higher the percentage the better

Average Rate of Return (ARR)

The average rate of return is a method that is used by a business to assess the profitability of an investment opportunity.

The ARR calculates the average return that the business receives on an investment over the investments life span as a percentage of the initial cost of the investment

$$\text{ARR} = \frac{\text{Average Annual Profit}}{\text{Cost of investment}} \times 100$$

The higher the ARR the better

The result can be compared to different investment opportunities to find the most profitable

Interpreting quantitative business data

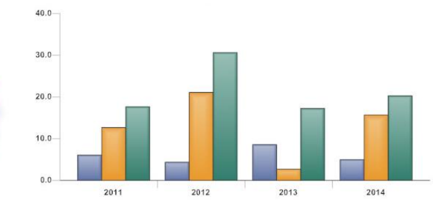
Businesses use a lot of quantitative data from a wide range of sources.

The accuracy of this data is extremely important if the business is to make the right decisions

Businesses use data to …

- Monitor the performance of the business
- Compare performance with competitors
- Identify trends in the market
- Make business decisions
- Set business aims and objectives

Data can be presented using …



Limitations of financial data

- It is historical – based on past performance
- Statistics can be manipulated
- Business performance is not judged only on financial performance
- The data does not show the reasons for the results