

Topic 2.4.1 Business Calculations

BUSINESS: *Creating informed, discerning employees, consumers and future leaders*

Key Vocabulary

Revenue – the money that a business receives from selling its goods and services. Also called Turnover or Income

Cost of sales – the name for the costs that are directly involved in the making of a product for a manufacturer or the provision of a service for a service provider

Gross profit – the amount left after the cost of buying or making the product has been deducted from revenue

Expenses – costs of the business that are not directly involved in the making of the product, e.g. rent, rates

Net profit – overall profit made by a business. What is left after deducting all costs.

Gross profit margin – expressed gross profit as a percentage of sales revenue

Net profit margin – expresses net profit as a percentage of sales revenue

ARR – Average Rate of Return. Expresses the average yearly profit as a percentage of the sum invested. Shows profitability and can be compared with interest rates on bank deposits

Core Knowledge

Key formulas:

Gross profit = Revenue – cost of sales

Net Profit = Gross profit – expenses

Gross profit margin = $(\text{Gross profit} \div \text{Sales revenue}) \times 100$

Net profit margin = $(\text{Net profit} \div \text{Sales revenue}) \times 100$

ARR = $(\text{lifetime profit} \div \text{years the investment will last}) \div \text{initial investment} \times 100$

In all cases the higher the number the better, BUT these must be compared to other businesses and previous performance

Misconceptions

- Remember not all investments will be profitable
- Even if an investment is not profitable, this does not mean a business should dismiss it – it may be needed to maintain a competitive position
- A business can not lose profit – it makes a profit OR a loss
- A loss in one year does not always indicate failure – this may be due to high one-off costs

Application

RyanAir – has a greater Net profit margin than other airlines as it keeps costs down by not offering meals on board



Topic Links



Revenue & costs – knowledge of these terms is built on in this topic; fixed costs are expenses; variable costs are cost of sales

