Financial training
For non financial staff

ATTAINMENT TRAINING

The financial training specialists

Get your prices right (profit)

The supermarket sector continues to dominate the financial news. Tesco's profit warnings; Sainsbury's 7% drop in share price; and Morrison's new loyalty card promising to match Aldi and Lidl on price.

On our TV screens the supermarket chains try and differentiate themselves, but all compete on price.

So it's a sector where prices are likely to continue to fall. But what effect does that have on profitability?

In the year to February 2014 Tesco had sales of £63.5bn (after VAT). Cost of sales (the cost of buying the goods, and running and staffing the store) were £59.5bn, leaving a gross profit of £4.0bn, or 6.3%.

That means that for every £100 you spend in Tesco, they make £6.30 profit.

This profit has to pay their head office costs of £1.7bn. After some other financial adjustments that leaves a bottom line profit of £2.25bn before tax. Still a lot, but a lot less than 2012's profit before tax of £4bn.

What if they drop their prices by 1% though? The £100 trolley becomes a £99 trolley, leaving £5.30 profit. £635m less sales, which means £635m less profit: that's a 28% fall in profit coming from a 1% drop in price!

No wonder the supermarkets are giving profit warnings!

The message is that a small change in price has a large impact on our profit – and we need to understand the relationship.

In your business what's the relationship between price and profit – and do your salespeople understand it when they're giving discounts?

