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How to work out variable cost in break even analysis

a break-even analysis is a financial tool that helps a company determine the stage where the company, or a new service or product, will be profitable. In other words, it is a financial calculation to determine the number of products or services a company should sell or provide to cover its costs (particularly fixed costs.) Break-even is a situation where an organization does not make money or loses money, but all costs have been covered. break-even analysis is useful in the study of the relationship between variable cost, fixed cost and income. generally, a company with low fixed costs will have a low break-even sales point. For example, says happy ltd has fixed costs of rs. 10,000 vs sad ltd has fixed costs of rs. 1,00,000 sale of similar products, happy ltd will be able to break-even with the sale of minor products compared to sad ltd. components of Break-Even analysis fixed costs fixed costs are also called cover costs. These general costs occur after the decision to start an economic activity and these costs are directly related to the level of production, but not to the quantity of production. fixed costs include (but are not limited to) interest, taxes, salaries, rent, depreciation costs, labor costs, energy costs etc. these costs are set regardless of production. in case of absence of production costs must also be borne. variable costs are the costs that will increase or decrease in direct relation to the production volume. These costs include the cost of raw material, the cost of packaging, fuel and other costs directly related to production. calculation of the breakdown analysis the basic formula for break-even analysis derives from the division of total fixed costs of production of the contribution per unit (price per unit lower than the variable costs),Rs. 400 Sale price per unit: Rs. 600 Result: Rs. 4,00,000 Total fixed costs: Rs. 10,00,000 First we mustthe breaking point per unit, so we will divide the Rs.10,00,000 of fixed costs by Rs. 200 which is the contribution per unit (Rs. 600 – Rs. 200). Break-Even = Rs. 10,00,000/Rs. 200 = 5000 units Subsequently, this number of units can be shown in rupees by multiplying the 5000 units with the sale price of Rs. 600 per unit. We receive Break-Even sales at 5000 x Rs. 600 = Rs. 30,00,000. (Break-even point in rupees) The analysis of the breaking margin of the contribution also concerns the margin of a product's contribution. The excess between the sale price and the total variable costs is known as the margin of contribution. For example, if the price of a product is Rs.100, the total variable costs are Rs. 60 per product and the fixed cost is Rs. 25 per product, the product contribution margin is Rs. 40 (Rs. 100 – Rs. 60). This Rs. 40 represents the revenues collected to cover fixed costs. In calculating the contribution margin, no fixed costs are considered. When the Break-even analysis is used Starting a new activity: To start a new business, a break-even analysis is a must. Not only does it help to decide whether the idea of starting a new business is feasible, but it will force start to be realistic on costs, as well as provide a basis for the pricing strategy. Create a new product: In the case of an existing company, the company should still do a break-even analysis before launching a new product, especially if a product of this type is about to add significant expense. Change the business model: If the company is about to change the business model, like. by switching from wholesale to retail, then a break-even analysis must be performed. Costs could change considerably and breakeven analysis will help fix the sale price. Breaking analysis is useful for the following reasons: Helps determine the remaining/unused capacityonce you reach the break. This will help to show maximum profit onparticular goods/services that can be generated. Helps determine the impact on profit on change to manual automation (a fixed cost replaces a variable cost). It helps determine the change of profits if the price of a product is altered. It helps to determine the amount of losses that could be sustained if there is a drop in sales. In addition, break-even analysis is very useful to know the overall ability of a business to generate a profit. In the case of a company whose breaking point is close to the maximum level of sale, this means that it is almost impractical for the company to earn a profit even in better circumstances. Therefore, it is the management responsibility to constantly monitor the breakeven point. This monitoring will certainly reduce the breakeven point when possible. Ways to monitor Break-even point price analysis: Minimize or eliminate the use of coupons or other price reduction offers, as such promotional strategies increase the breakeven point. Technology analysis: Implementation of any technology that can improve business efficiency, thus increasing capacity at no extra cost. Cost analysis: The review of all fixed costs constantly to check if one can be eliminated can definitely help. Also, review the total variable costs to see if they can be deleted. This analysis will increase the margin and reduce the breakeven point. Analysis of margins: Push sales of the highest items (high contribution earn) and pay attention to product margins, thus reducing the breakeven point. Outsourcing: If an activity consists of a fixed cost, try to outsource this activity (always possible), which reduces the breakeven point. Advantages of Break-even Analysis Take missing expenses: When you are thinking about a new activity, it is very possible that you can forget aboutexpenses. Therefore, a break-even analysis can help you review all financial commitments to understand your break-even point. This is it. This.certainly limits the number of surprises along the way or at least prepares a company for them. Set revenue targets: Once the break-even analysis is complete, you will get to know how much you need to sell to be profitable. This will help you and your sales team to establish more concrete sales goals. Make smarter decisions: Entrepreneurs often make decisions in relation to their activity based on emotion. Emotion is important, that is how you feel, even if it is not enough. To be a successful entrepreneur, decisions should be based on facts. Financing your business: This analysis is a key component in any business plan. It is generally a requirement if you want strangers to finance your business. To fund your business, you must demonstrate that your plan is feasible. In addition, if the analysis looks good, you will be quite comfortable to take the weight of various ways of financing. Best prices: Finding the break-even point will help you to better assess the products. This tool is highly used to provide the best price of a product that can get maximum profit without increasing the existing price. Fixed cover costs: Making a break-even analysis helps to cover all fixed costs. 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