



Finding out what sales volume you need to achieve to at least breakeven is critical to managing your business. Once you know what your variable costs and fixed costs are, finding your breakeven point is easy.

Variable costs are directly related to your sales levels in dollars or units sold. For example, materials and supplies, commissions on sales, sales incentives or bonuses for employees and shipping costs are all considered variable costs.

Fixed costs are those costs that remain the same no matter what volume of sales your business has. These include rent, insurance, licenses, wages for permanent employees, interest on loans and operational expenses.

How to determine your breakeven point:

1. Subtract your Variable Costs per Unit from your Sales Price per Unit. This equals your Contribution Margin per Unit.
2. Divide your Contribution Margin per Unit by Sales Price per Unit. This equals your Contribution Margin Ratio.
3. Now divide your Fixed Costs by your Contribution Margin Ratio. This equals your Breakeven Sales Volume.

If this seems confusing, consider this example when you receive your financial statements from your accountant you see that your
 Fixed costs = \$25,000
 Variable costs per unit of production = .50
 Sales revenue unit of production = \$1.25

From this you learn that 50 cents of every unit sold goes toward covering your variable cost per

unit. Furthermore, you know that 75 cents from each unit sold can go toward covering your fixed costs.

Now if you divide your fixed costs (\$25,000) by the contribution to those costs per unit (.75), you will know what level of sales you need to achieve in order to break even.

$$\text{Fixed Costs/Contribution to Fixed Cost per Unit} = \text{Breakeven Point}$$

$$25,000 / .75 = 33,333.33$$

Understanding your breakeven point is important. But if you take your analysis one step further you can better manage your business.

For example, you can see that a 10,000 increase in sales volume to 43,333 will yield a \$7,500 profit. Likewise you can see that a 10,000 decrease in sales volume will produce a loss of \$7,500.



The Profit Builder column is brought to you by Richard McGrath, a member of the Principa Alliance.

Understanding your breakeven point is just the beginning to making the most of your financial statements.

If you would like to discuss your breakeven point or would like help with implementing any of the ideas in this article, please contact Richard McGrath on 07 4128 2066 or richard@clm.net.au