



## **The Two Piece Suit and Costs**

### **How to Calculate your Break-even Point**

# more money for shoes

## How to Calculate your Break-even Point

Calculating your break-even point can be tricky but the concept itself is simple. It is the point at which your sales exactly cover your expenses. In other words, it's when you sell enough units of your product or enough number of services (or hours of services) to cover your expenses without making a profit or taking a loss. If you sell more, then you make a profit. If you sell less, you take a loss. Still with me? Good

Before you can start working out your breakeven point in sales volume or hours volume, you need to know three things. You need to know your fixed costs, your variable costs, and the price of your product or service. If you don't know what your costs are then download the shopping list items on fixed and variable costs in this section.

Now, in order to calculate your breakeven point, you need to use the following formula:

$$\text{Fixed Costs divided by (Price - Variable Costs) = Breakeven Point in Units}$$

In this formula, fixed costs are your total for the year (or the period). Price and variable costs, however, are stated as per unit (or hour) costs - the price for each product or service sold and the variable cost for that unit of the product. Let's use an example so that you can see what I mean:

Tanya has calculated that her fixed costs add up to \$60,000 per year. She sells shoe boxes and the variable costs associated with producing these shoeboxes are \$0.80 per box. The boxes are sold at an average price of \$2.00 each. We can now work out the breakeven point for Tanya's shoeboxes by popping the information into this table.

Fixed Costs divided by	Price less Variable Costs	= Number of Units or Number of Hours
\$60,000	$\$2 - \$0.8 = \$1.2$	50,000

So we know that Tanya has to produce and sell 50,000 shoeboxes simply to cover her total expenses. At this level of sales, she won't make any profit, she will simply breakeven. Now, the problem is that Tanya thinks that she can only sell 47,000 units so what can she do? If you look at the breakeven formula, you can see that there are two solutions. She can either raise the price of her product or she can find ways to cut her costs. Tanya thinks she can reduce her fixed costs by \$1,000 and raise her prices by 5c. So her breakeven point is now:

Fixed Costs divided by	Price less Variable Costs	= Number of Units
\$59,000	$\$2.05 - \$0.8 = \$1.25$	47,200

To find out the break-even point in your business simply enter your figures into the table below and calculate the formula. If, like Tanya, you think that the number is unrealistic then look at where you can make changes so that you will not only be breaking even, but profitable.

Fixed Costs divided by	Price less Variable Costs	= Number of Units or Number of Hours