UNIT 8: BREAK EVEN ANALYSIS

CHAPTER: BREAK-EVEN ANALYSIS

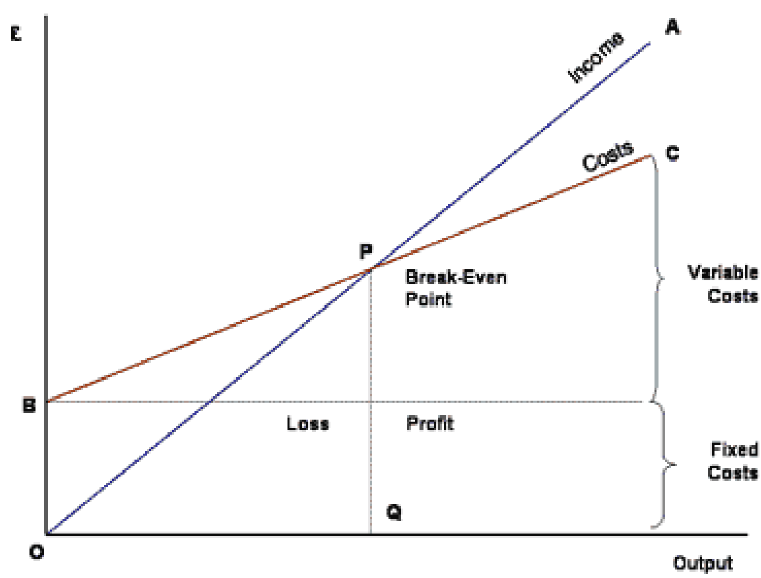
WHAT:

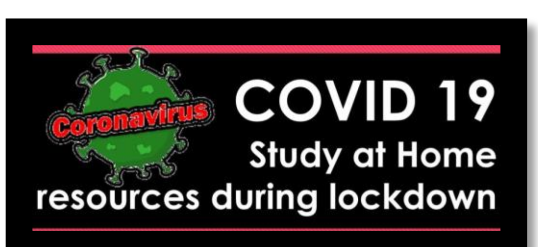
Break-even analysis is a technique widely used by production management and management accountants. It is based on categorising production costs between those which are "variable" (costs that change when the production output changes) and those that are "fixed" (costs not directly related to the volume of production).

Total variable and fixed costs are compared with sales revenue in order to determine the **level of sales volume, sales value or production at which the business makes neither a profit nor a loss (the "break-even point").**

THE BREAK-EVEN CHART

In its simplest form, the break-even chart is a graphical representation of costs at various levels of activity shown on the same chart as the variation of income (or sales, revenue) with the same variation in activity. The point at which neither profit nor loss is made is known as the "break-even point" and is represented on the chart below by the intersection of the two lines".

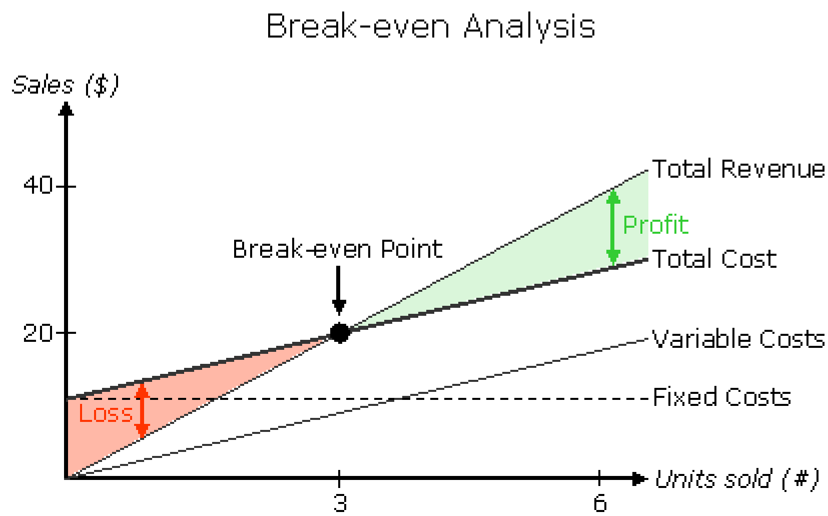




For Example,

Let's say there is a restaurant ABC, which plans to introduce a new product xyz and which to do break-even analysis to the new product to know how many units of xyz the restaurant needs to sell to break even the cost and to know at how many sales how much profit it will be making. ABC observes that it has a fixed cost of 10$ on xyz product, and for each unit of xyz an additional variable cost of 3.33$ occurs. ABC decides to sell xyz at a price of 6.66$/unit.

Now after plotting the break-even chart, it seems that it needs to sell a minimum of 3 units to prevent loss & more than that to make a profit. A lot of other conclusions also can be derived from the Break-even chart.



IMPORTANT

IMPORTANT QUESTIONS FOR THIS CHAPTER

Discuss break-even analysis with the help of a neat chart and suitable example

Explain the importance of break-even analysis for a catering establishment.