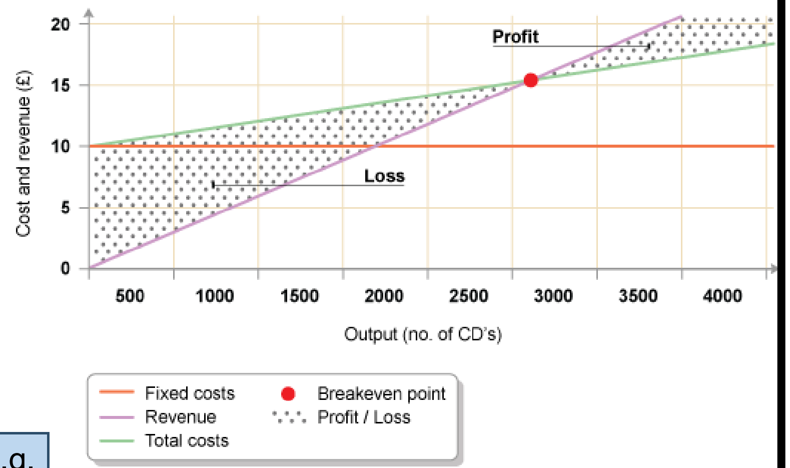
The Sir John Colfox Academy

Inspiring Learning, Achieving Excellence

Knowledge Organiser
Finance (Paper 2: Unit 6)
Breakeven

At low levels of sales, a business is not selling enough units for revenue to cover costs. A **loss** is made. As more items are sold, the total revenue increases and covers more of the costs. The **breakeven point** is reached when the total revenue exactly matches the total costs and the business is not making a profit or a loss. If the firm can sell at production levels above this point, it will be making a **profit**.

Establishing the breakeven point helps a firm to plan the levels of production it needs to be profitable.



Fixed Costs	The costs that stay largely the same, regardless of the business' output e.g. Rent, mortgagae, salaries
Variable Cost	The costs that change as the business' output changes e.g. raw materials & hourly wages.
Breakeven	The point at which the business' total sales equals the total costs. There is neither profit nor loss.
Margin of safety	The amount by which current sales exceed the break-even level of output

Using A Formula to Calculate The Break-Even Point

- Creating a graph to calculate break even is time consuming
- It is quicker to use the following formula:

$$\text{Break-Even Point} = \frac{\text{Fixed Costs}}{\text{Selling Price} - \text{Variable Cost Per Unit}}$$

- For Example:

Fixed Costs	£1,200
Variable Costs	£15
Selling Price	£20

Break Even Point = 240

Using break-even point

Advantages	Disadvantages
• shows how many items needs to be sold to make profit for the business • useful tools to set targets • identifies the fixed and variable costs • easy way to calculate the profit or loss at different level of output	• information can be reliable (less knowledge) • assumes that the costs and revenue don't change with output • target set may be too high, creating stress

<u>Contribution</u> is the difference between sales revenue and variable costs of production

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Analysing Financial Performance

Income statement

(formerly known as Profit & Loss statement)

Financial reports of LTDs ad PLCs have to be published, PLC's must make these available to anyone

Statement of financial position

(formerly knows as Balance Sheet)

Gross profit = Revenue - Cost of Goods Sold. **Gross profit** is the **profit** a company makes after deducting the costs associated with making and selling its product

The first part of the income statement is known as the Trading Account.

Sales Revenue		100,000
Less cost of goods sold		
Opening Inventory	30,000	
Purchases	60,000	
Closing Inventory	20,000	70,000
Gross Profit		30,000

The low part of the income statement includes all the other expenses that a business has, before calculating Net Profit.

Salary	30,000	
Rent	20,000	
Total Expenditure		50,000
Net Profit		10,000

Net Profit: the actual profit after working expenses not included in the calculation of gross profit have been paid

Statement of Financial Position for the Year ending 6th		
	£	£
Non-Current Assets		
Premises	200,000	
Fixtures and Fittings	50,000	
Company Vans	20,000	270,000
Current Assets		
Stock	50,000	
Cash in Bank	20,000	
Trade Recivables	40,000	110,000
Total Assets		380,000
Less Current Liabilities		
Trade Payables	70,000	
Overdraft	20,000	90,000
Working Capital		290,000
Non-Current Liabilities		
Bank Loan		80,000
Net Assets		210,000
Financed By		
Capital		70,000
Retained Profit		140,000
Capital Employed		210,000

Example

In this section all of the current assets that an organisation has will be listed.

It is also important to remember that if the business has any cash that is not in the bank, this would also be recorded here as a current asset.

Assets: Something the business owns; it has a value

Current assets: cash and other assets that are expected to be converted to cash within a year.

Liabilities: are obligations of the company; they are amounts owed to creditors for a past transactions

Noncurrent liabilities are long-term financial obligations listed on a company's balance sheet that are not due within the present accounting year