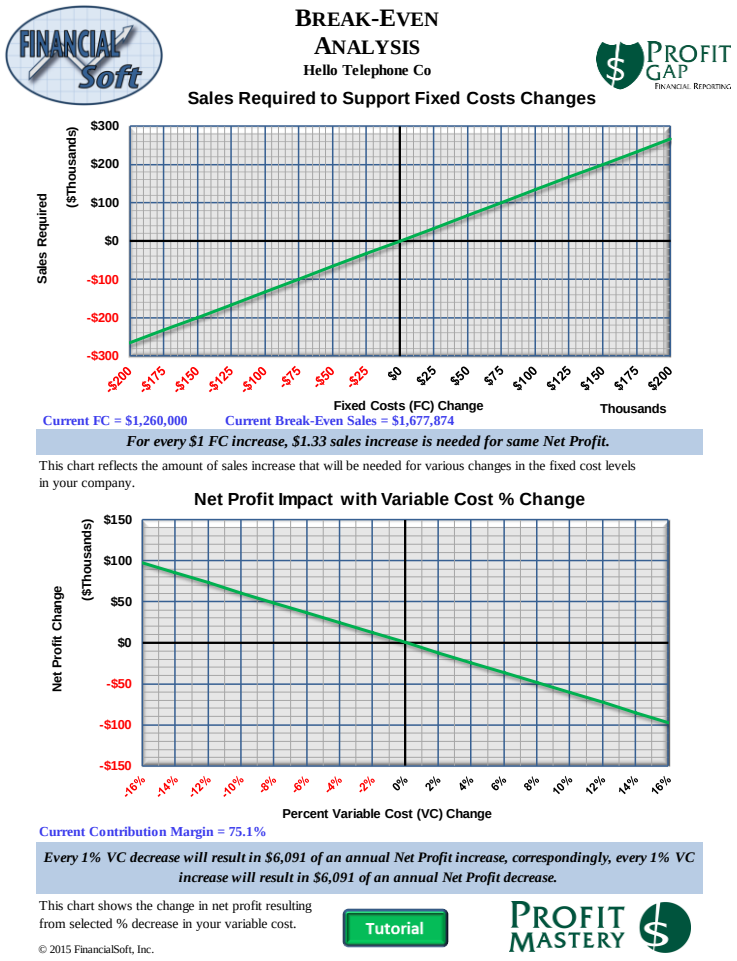
Profit Gap Tutorial

Break-Even Analysis



The Break-Even analysis taught in the Profit Mastery class can help you with your company planning to understand the effects of fixed or variable cost changes.

1) Top Chart:
Sales Required to Support Fixed Cost Changes

This chart tells you the impact on Sales that will result from an addition (or reduction) of Fixed Cost to generate the same Net Profit. In this sample company case, every $1 of Fixed Cost increase requires an increase of $1.33 in sales to result in the same Net Profit. The inverse is true as well: for every $1 decrease in Fixed Costs, $1.33 less in Sales is needed to yield the same Net Profit. The chart graphs this equation:

$1 Fixed Cost (FC) = $1.33 Sales.

Other practical examples of the power of this information about your company would include hiring a new employee at a cost $100,000 in Salary and Fringes - the company would have to increase its sales by $133,000 to support that new employee.

The same would be true for the purchase of office equipment such as computers: a $5,000 cash purchase of a computer would require $6,650 of additional sales. Likewise, on the negative side, you could determine fixed cost reduction requirements if your sales forecast were to be reduced. For example, if your forecast sales reduction were to be $200,000 you would need to reduce your operational expenses by $266,000 in order to maintain your same Net Profit.

2) Bottom Chart: Net Profit impact with Variable Cost % Change
This chart illustrates the impact on Net Profit as a result of Variable Cost increases and decreases. As you recall from the Profit Mastery University class, variable costs are directly related to sales. They are primarily affected by the Costs of Goods Sold (COGS or COS) or the total cost to deliver your product or service to a customer. In this sample company, every 1% VC decrease will result in $6,091 annual Net Profit increase. Correspondingly, every 1% VC increase will result in $6,091 annual Net Profit decrease.

This is very useful in planning future profit improvements for your company. As demonstrated with this sample company, if you wanted an additional $100,000 in profits you would need to reduce your variable cost by 16.4%. Conversely, if you knew you were going to have a variable cost increase due to a supplier raising prices, this chart would help you understand the impact on your profits. So, if a supplier cost increase has an overall 5% increase in your variable cost, this sample company would realize a $30,455 decrease in their profits.