Break Even Analysis

- The break-even analysis lets you determine what you need to sell, monthly or annually, to cover your costs of doing business.

- Break-even is a situation where you are neither making money nor losing money, but all your costs have been covered.

- Here the whole focus remains on Break Even Point (BEP).

- BEP is the point at which we find neither profits nor any losses, in the sense on reaching this point we find TR = TC

Assumptions of Break Even Analysis:

1. Total Cost is divided into Fixed and Variable Cost

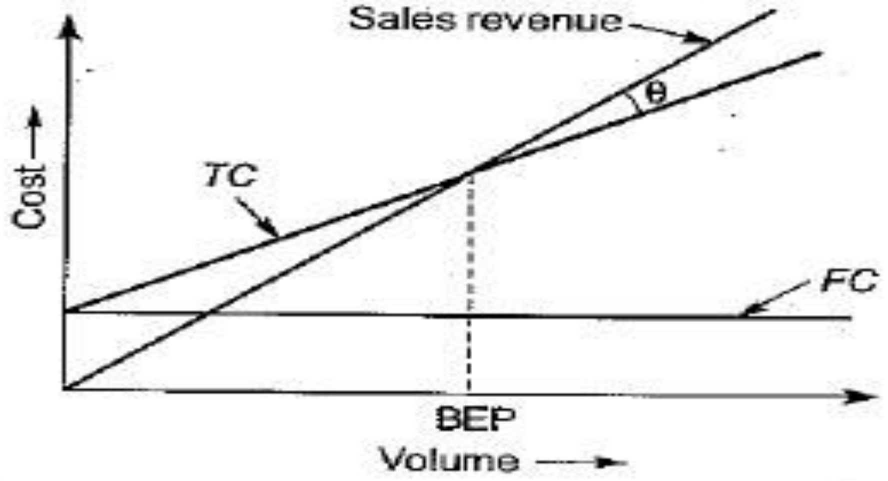
   Fixed cost will remain constant at all level of production

   Variable Cost varies in direct proportion to the volume of the production.

2. Whatever produced is sold, we mean to say they are no closing inventories.
3. The selling price does not change with the change in the quantity of sale, in the sense we assume that there are no price discounts.
4. The firm is engaged in producing only one product.

Break-Even Chart

Angle of Incidence



θ = angle of incidence

Significance of Break Even Analysis:

1. Manages the Size of Units to be Sold
2. Budgeting and Setting Targets
3. Monitors and Controls Cost
4. Helps Design Pricing Strategy
5. Used in Decision Making

Limitations of Break Even Analysis

1. We go wrong with the assumptions:

    a). It's not simply fixed and variable cost, we even find semi variable or semi fixed cost

    b) we come across closing stocks

    c) selling price might change etc.,

2. The Concept holds good only during short period.
3. BEP is based on Revenue (Selling Price) and Cost Components (Variable Cost & Fixed Cost), anytime any change in one or all these variables will lead to a change in BEP.
4. Multiproduct firms got to calculate BEP separately for each and every product. It might be little tedious to do the same.