

Types of Expenses and Profit

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Expenses

- “ It costs money to make money. “
- Cost of operations that a company incurs to generate revenue

Expenses v/s Investment

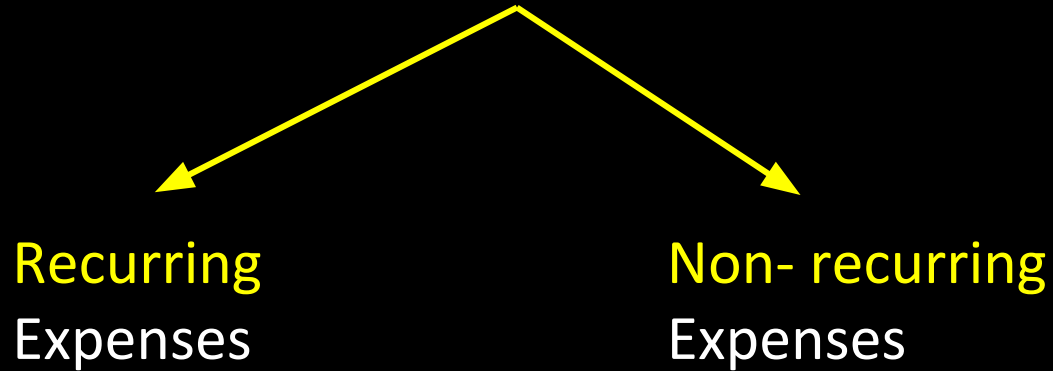
- Expenses are costs which are incurred in the current period and are not expected to generate future cash flows.
- Investments are expected to generate future cash flows and are the result of a different set of activities than expenses.

Some Expenses are:

- Payments to suppliers
- Employee wages
- Factory leases
- Equipment depreciation.

Etc..

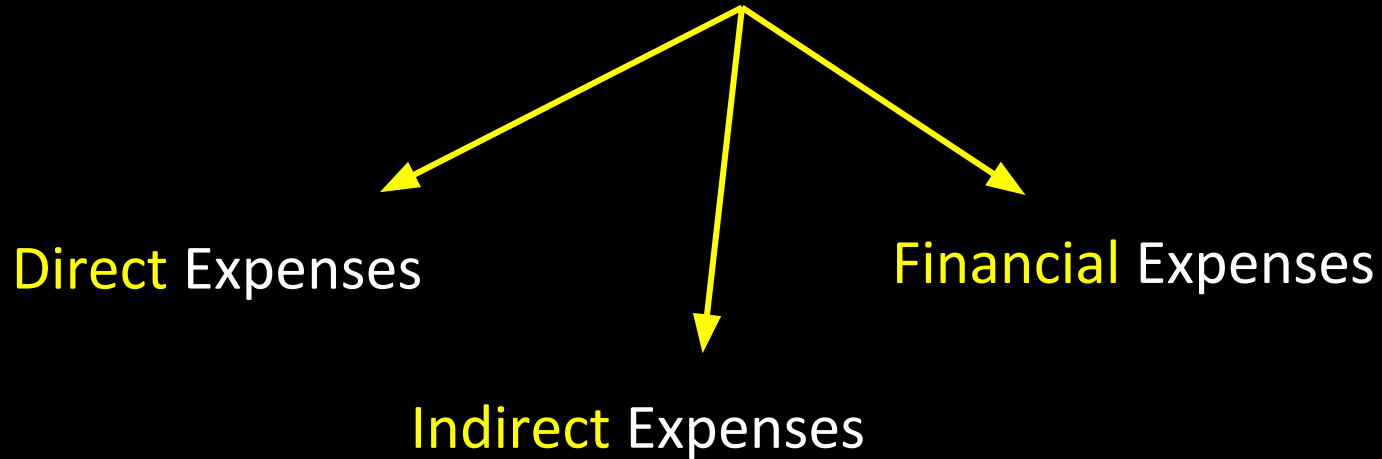
Types of Expenses



Recurring expenses

- Expenses incurred by a business on a regular basis.
- Essential for running a business.
- Examples:
 - Electricity
 - Salaries
 - Transportation, etc.

Types of Recurring Expenses



Direct expenses

- Varies directly with the change in qty. produced.
- Purchase of goods
- Commissions
- Wages of Labour
- Many more examples.....

Indirect expenses

- Cannot be directly associated with Production
- Keeping up and running entire company
- Production supervisor salaries
- Quality control cost

Financial expenses

- Income taxes
- Company's interest expenses in long term debt
- Foreign exchange losses on debt

Non-Recurring expenses

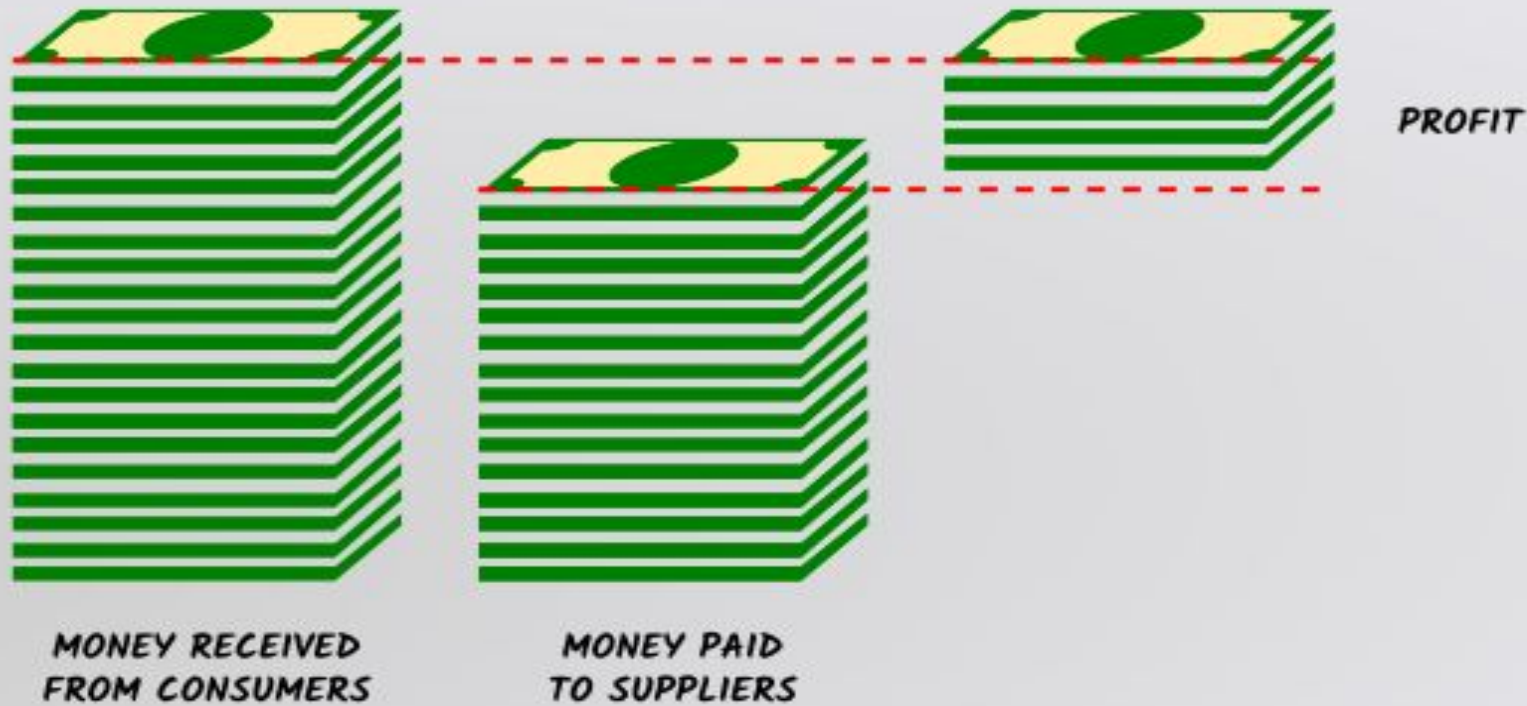
- Expenses incurred by a business once in a while.
- One time/loss
- Examples:
 - Buy Machinery
 - Payment made on account of some lawsuit
 - Loss due to fire/theft, etc.



PROFITS

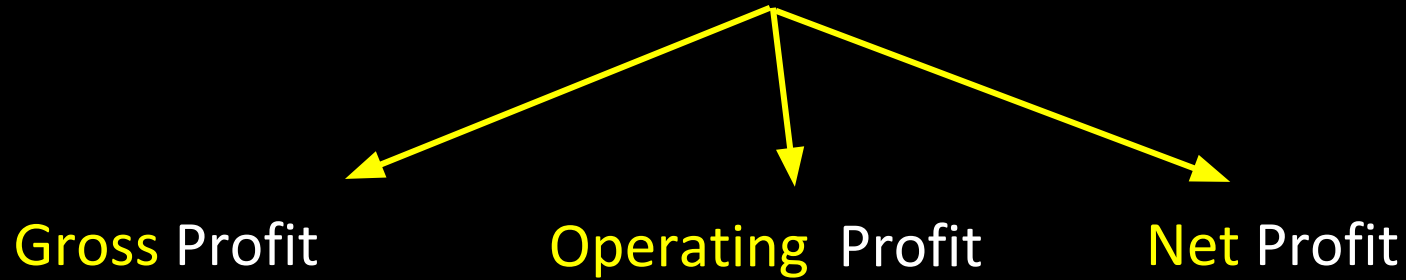


WHAT IS PROFIT?



- Profits is used to denote when **earning exceeds** the expenses incurred to generate those expenses.
- Total revenue **less** total expenses

Types of Profit



Gross Profit

- Profit after deducting the costs of making and selling its products, or cost of providing its services.

$$\text{Gross Profit} = \text{Revenue} - \text{Direct Expense}$$

Operating Profit

- a profit from business operations after deduction of Indirect and Direct Expenses from Revenue.
- gross profit minus operating expenses

$$\text{Operating Profit} = \text{Revenue} - \text{Direct Expense} - \text{Indirect Expenses}$$

Net Profit

- The money one company earns after subtracting all business expenses from revenue.
- Demonstrates the success of the business.
- Indicates the money available to pay to owner or invest in business.

$$\text{Net Profit} = \text{Revenue} - \text{Direct Exp} - \text{Indirect Expense} \\ - \text{Financial Expenses}$$

Gross Margin

- The percentage of revenue that exceeds a company's direct expense.
- The higher the margin, the more effective the company is in generating revenue .

$$\text{Gross Margin} = (\text{Gross Profit} / \text{Revenue}) * 100$$

Operating Margin

- Profit a company makes on sales generated as a percentage of revenue.
- Calculated before paying interest or tax.

$$\text{Operating Margin} = (\text{Operating Earnings} / \text{Revenue}) * 100$$

Net Margin

- Net income or profit generated as a percentage of revenue.
- Most important indicators of a company's financial health.

$$\text{Net Margin} = (\text{Net Income} / \text{Revenue}) * 100$$

Income Statement

- Financial Statement showing company's profit.
- Statement displays:
 - Revenue
 - Expenses
 - Profit

| | |
|---|---------------|
| Revenue | 1,00,000 |
| Less: | |
| Material Cost | 10,000 |
| Wages | 20,000 |
| Gross Profit | 70,000 |
| Rent | 20,000 |
| Utility Cost | 10,000 |
| Supervisor Salary | 5,000 |
| Selling Cost (Advt. expenses) | 5,000 |
| Depreciation | 5,000 |
| Operating Income | 25,000 |
| Interest Paid | 5,000 |
| Profit Before Tax (Taxable Income) | 20,000 |
| Less: Tax @ 30% | 6,000 |
| Net Profit After Tax | 14,000 |

What It Tells Us?

- Provide a representation of the company's current performance to investors.
- Evaluate the overall value of a company.
- Assess company's efficiency
- Helps managers and investors to take financial decisions.

Takeaways!

- Expense is the cost used by company to produce revenue.
- Profits are financial benefit realized when revenue generated exceeds the expenses
- Profit is the bottom line on an income statement and is the motive for running a business.
- Income statement shows result of company's operations.

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References

Sites to Visit:

- <https://www.accountingtools.com/articles/what-is-direct-expense.html>
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THANK YOU!