

4 J Limited manufactures a single product, a leather suitcase. The following forecast information is available.

Costs per unit	\$
Direct materials	15
Direct labour	8
Variable production overheads	2
Fixed costs per month	\$
Salaries	1450
Rent and rates	650
Advertising	1000
Other fixed costs	1100

The directors calculate the selling price by adding a mark-up of 80% on to the variable costs.

The company has orders to supply 240 suitcases per month. This involves working at 75% capacity.

REQUIRED

(a) State **two** benefits and **two** limitations of break-even analysis.

Benefits

- 1
- 2

Limitations

- 1
- 2

[4]

(b) Calculate the break-even point in **units** per month.

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[3]

(c) Calculate the **monthly** margin of safety

(i) in units;

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(ii) in revenue.

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(d) Calculate the **maximum** monthly profit if the company is working at 100% capacity.

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..... [3]

Additional information

The directors have been approached by Bart, a retailer, who requires a regular monthly order of 150 suitcases. Bart is offering to pay \$42 per suitcase.

The directors are aware that this order will take production over the current capacity and the following would result:

- 1 All suitcases over the current maximum production capacity would incur an additional \$2 per unit direct labour cost to allow for overtime payments.
- 2 Additional storage facilities would have to be found at a monthly rental of \$200.

The directors are also concerned that the target annual profit set by them of \$30 000 is not being achieved.

They have decided to increase by 10% the selling price of all production **except** the new contract. They also plan to increase the advertising expenditure by \$500 per month and are confident that monthly sales to existing customers will remain at 240 suitcases per month.

REQUIRED

- (e) Prepare a statement, in marginal cost format, to show J Limited's maximum forecast **total** profit per **month** if the directors accept the new contract.

[8]

- (f) Advise the directors whether or not they should accept the new contract with Bart and increase the selling price. Justify your answer by explaining **two** benefits and **two** limitations.

Advice

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Benefits

1

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2

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Limitations

1

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2

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[7]

- (g) State **three** financial benefits of a system of budgetary control.

1

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2