

## Tennessee Small Business Development Center at Volunteer State Community College



A public service program of the Division of Continuing Education & Economic Development

### **May's Newsletter Topic:** **The Break-Even Point for Small Businesses**

What is break-even? I could give you a multitude of different definitions and formulas that could make your head spin. However, I think I will opt for the down-to-earth definition. Break-even is the point at which you are not making any money and you are not losing any money. You are simply breaking even.

Knowing your break-even point is one of the most important pieces of information that a business owner should know. Whenever I ask someone if they know what their break-even is, I always get the answer of "I have a ballpark idea of what it is". This is not good enough to make important decisions in your business such as hiring additional personnel, buying a piece of equipment, or offering a new product or service. You need to know exactly how much money it takes to break-even.

There are a variety of different ways to calculate your break-even point. For the sake of this article, let's use the simplest one, which is:

$$\text{Breakeven} = \text{Fixed Costs (FC)} / \text{Gross Margin (GM)}\%$$

Fixed costs are any costs that your business incurs whether you make money or not, such as, rent, utilities, insurance, executive salaries, office expenses, etc.

Gross margin percentage is what you make after you pay immediate expenses associated with the product or service you offer. This could be materials to make the product, payroll for the service, and even other costs associated with creating or delivering the product or service. For example, if your gross margin is 70%, then for every \$1 you generate, you will immediately use \$.30 to pay for immediate expenses and the gross margin will be \$.70. You can then use the \$.70 to pay for your fixed costs.

Let's take a look at the example below to calculate break-even for Ava's Landscaping Inc.

$$\text{Fixed Costs} = \$4,000$$

Rent, utilities, insurance, office expenses, executive salary (Ava's salary)

$$\text{Gross Margin}\% = 50\%$$

Covers costs of gas, mulch, direct personnel (person that landscapes the yard)

$$\text{Break Even} = \$4,000/50\% \text{ or } .5 = \$8,000$$

This means that Ava's Landscaping Inc. will have to generate \$8,000 every month just to pay the bills. So how many yards will Ava's Landscaping Inc. have to service to break-even? Divide the break-even point by the unit cost. In this case, the break-even is \$8,000 and the average service fee is \$50 per yard.

$$\$8,000/\$50 = 160 \text{ yards to service}$$

This means it will take 160 yards a month to break even. This will now equip Ava with the information she needs to be successful in making business decisions, such as pricing, when it is time to hire more personnel, marketing needs, etc.

### **Small Business Tip of the Month:** *Break-Even Calculator*

If you would like to take a more in depth look at calculating your break-even use the link below. You will be able to identify the number of units that it will take to break-even. Units could be the number of products or services you have to sell to break-even.

<http://www.dinkytown.net/java/BreakEven.html>

### **May Small Business Workshops**

Sign up for any of these workshops online at [www.tsbdc.org](http://www.tsbdc.org).

#### **How to Start a Small Business** ✓

*Tuesday, May 12, 2009 4:00 PM to 6:00 PM*

This workshop provides basic information on starting a small business. It will also discuss services provided by the TSBDC. Reservations are required.

Location: [TSBDC @ Volunteer State Community College, Gibson Hall, Gallatin, TN](#)

#### **Developing a Business Plan** ✓

*Wednesday, May 20, 2009 2:00 PM to 5:00 PM*

This workshop provides information about sections of a business plan, information needed for each section, how to gather information, and how to compile it for your plan. Participants will complete a rough draft of the narrative portion of their business plan during the workshop. Reservations are required.

Location: [TSBDC @ Volunteer State Community College, Gibson Hall, Gallatin, TN](#)

The TSBDC also offers free and confidential one-on-one counseling for existing and start up small businesses. To register for go to [www.tsbdc.org](http://www.tsbdc.org).

**Other contact information - Phone (615) 230-4780 [www.volstate.edu/tsbdc](http://www.volstate.edu/tsbdc)**

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