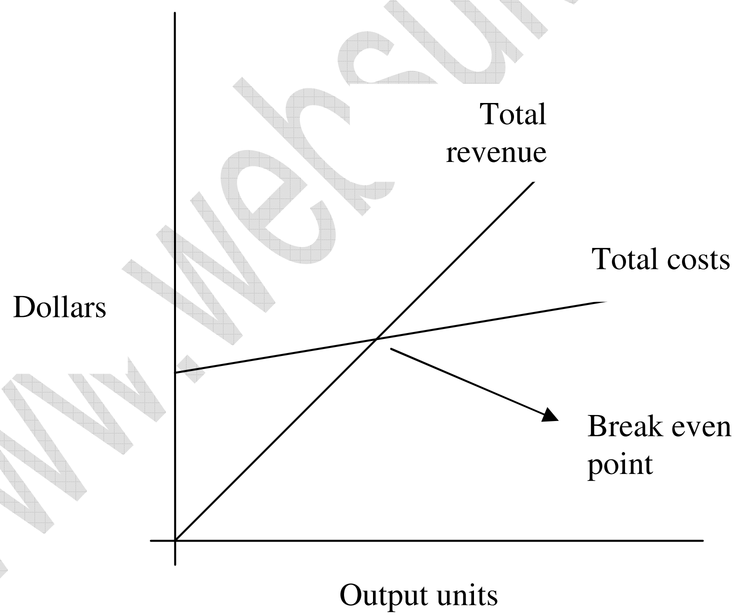
Break even point

It is the point at which the company neither makes a profit nor suffers a loss. A company's break-even point is the amount of sales or revenues that it must generate in order to equal its expenses. This information can be used in making a wide range of business decisions, including setting prices, preparing competitive bids, and applying for loans.

Figure shows the standard break-even analysis framework. Units of output are measured on the horizontal axis, whereas total revenue (both revenues and costs) are the vertical units of measure. Total revenues are zero if no units are sold. However, the fixed costs provide a floor for total costs; above this floor, variable costs are tracked on a per unit basis. Without the inclusion of fixed costs, all products for which marginal revenue exceeds marginal costs would appear to be profitable.



In Figure, the break-even point illustrates the quantity at which total revenues and total costs are equal; it is the point of intersection for these two lines (Total cost and total revenues line). Above this quantity, total revenue is greater than total costs, generating a profit for the company. Below this quantity, total costs will exceed total revenues, creating a loss.

To find this break-even quantity, the manager uses the standard equation to calculate the profit, where profit is the difference between total revenues (TR) and total costs (TC). When TC - TR = 0, there is no profit which is the break even point.