

Hector's Income Statement	The Math
A. Sales	\$100 (25 ties × \$4 per tie = \$100)
B. Less Total Cost of Goods Sold	\$ 50 (25 ties × \$2 per tie = \$50)
C. Gross Profit	\$ 50 (A - B = C)
D. Less Operating Costs	
D1. Fixed Costs \$ 24	
D2. Variable Costs <u>+0</u>	\$ 24 (\$24 for flyers)
E. Profit Before Taxes	\$ 26 (C - D = E)
F. Taxes	\$ 6 (Taxes = \$6)
G. Net Profit/(Loss)	\$ 20 (E - F = G)

Hector's business is profitable.

BREAK-EVEN ANALYSIS

When sales and costs are equal, the income statement shows no net profit or net loss. The total at the bottom of the income statement is zero. This condition is called the **break-even point**. Many new businesses lose money in the beginning, but, to survive, a business must at least break even. It is vital for you to know how many units the business must sell during a month to cover costs and break even. Break-even analysis allows you to determine this number.

Unit of Sale

First, though, you must define your **unit of sale**. If you are selling ties, one unit of sale can be defined as one tie. If you are selling word processing, you can define one unit of sale as one hour of word processing. It's up to you.

Once you've defined a unit of sale, figure your **gross profit per unit**. This is the first step toward determining how many units you will have to sell to break even. Gross profit per unit is the selling price of the unit minus its cost of goods sold.

$$\text{Selling Price per Unit} - \text{Cost of Goods Sold per Unit} = \text{Gross Profit per Unit}$$