BMIH5007
Financial Management

Cost Behaviour & Break-Even

Recap

Last week gave an overview of..

Assessment discussion

The Courtauld commitment

We looked at the sustainability triangle

What were the 3 key areas the 'Courtauld Commitment' is targeting

Cost-driven
Value-driven

	Same as competitors' or easy to imitate	Better than competitors' and difficult to imitate*
Resources	Necessary resources	Unique resources
Capabilities	Threshold Capabilities	Core Capabilities

What do these mean?
Give me an example of a value driven hotel and a cost driven in the chatbox.

Give an example of 'core capabilities' for a hotel.

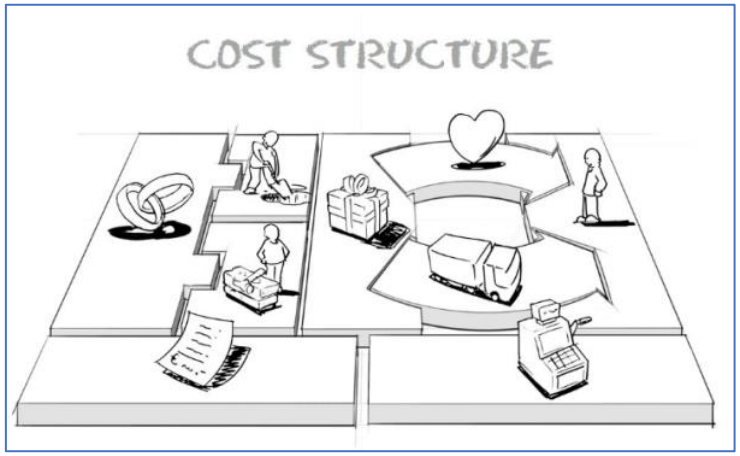
Aims for today

- Cost structures
- Break even

Costs structure

- "The Cost Structure describes all costs incurred to operate a business model"
  - Creating and delivering value
  - Maintaining Customer Relationships
  - Generating Revenue
- Links to
  - Key Resources
  - Key Activities
  - Key Partnerships

Osterwalder and Pigneur, 2010



Cost/Management accounting is:

- Optional, organisations do not have to use it (although most do in some form).
- Information may be approximate.
- More important to be timely than accurate.
- Can be produced for any segment of an organisation.
- There are no prescribed rules.
- Can be for periods in the past, present or future.
- Produced when required.
- Prepared for management.

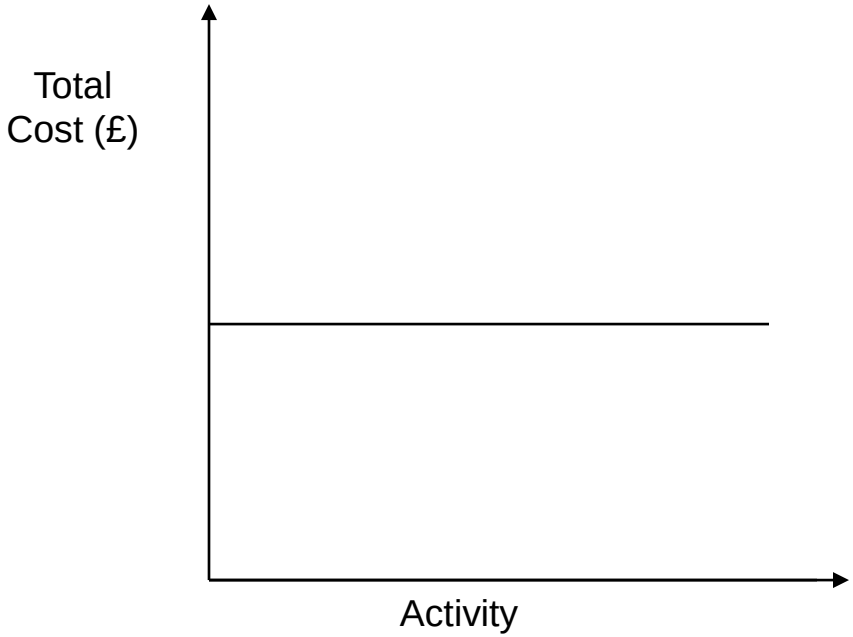
Cost Behaviour

If a business cost £750,000 to run last year, how much will it cost to run this year if business activity is forecast to increase by 25%?

Cost Behaviour

Fixed Cost

This type of cost is incurred for a period and within certain output limits tends to be unaffected by fluctuations in the level of output.

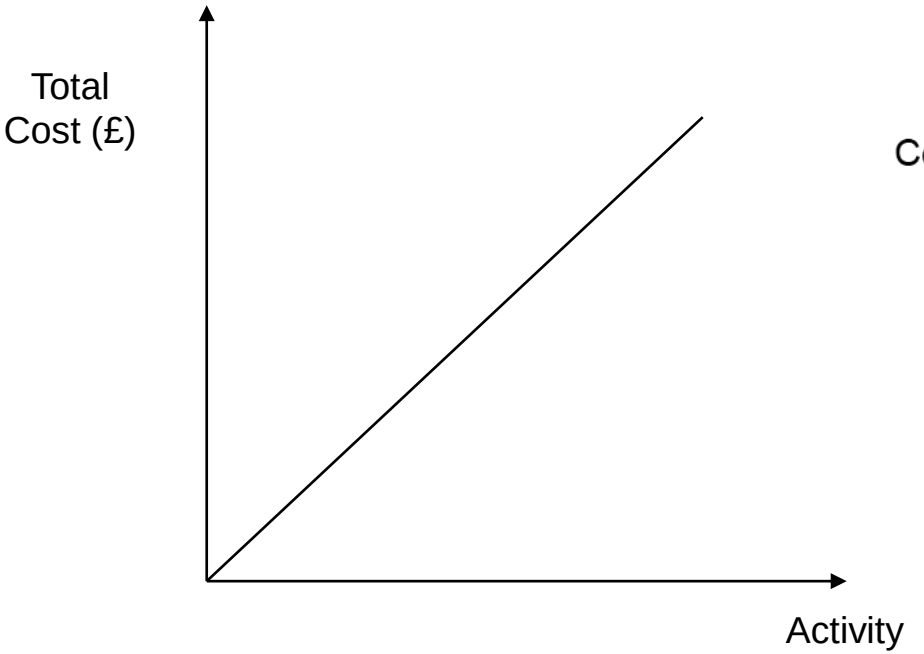


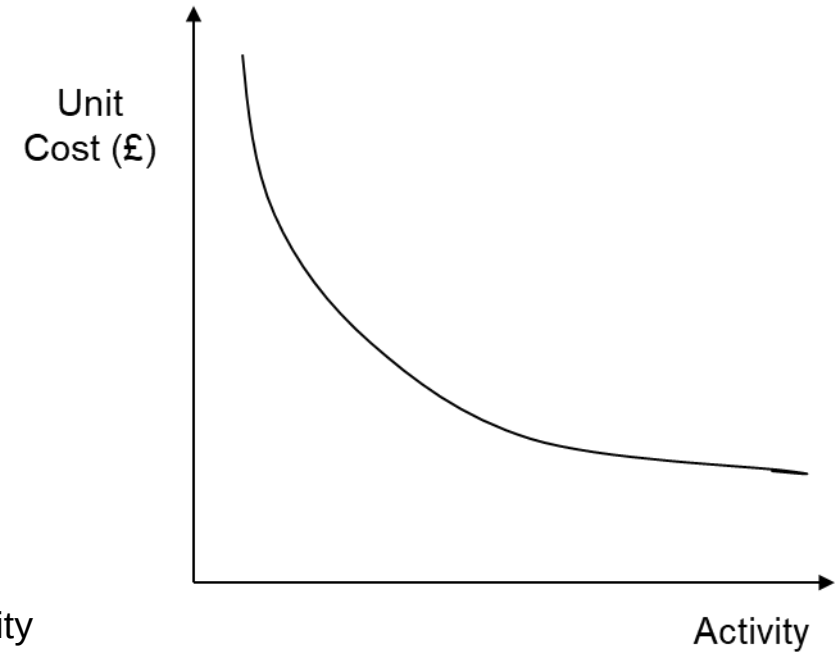
- Fixed Costs are sometimes known as capacity cost, since they result from outlays made for buildings, equipment, skilled professional employees and other items needed

Cost Behaviour

Variable Cost

A cost which varies with the level of activity – the more that is produced the higher the cost.

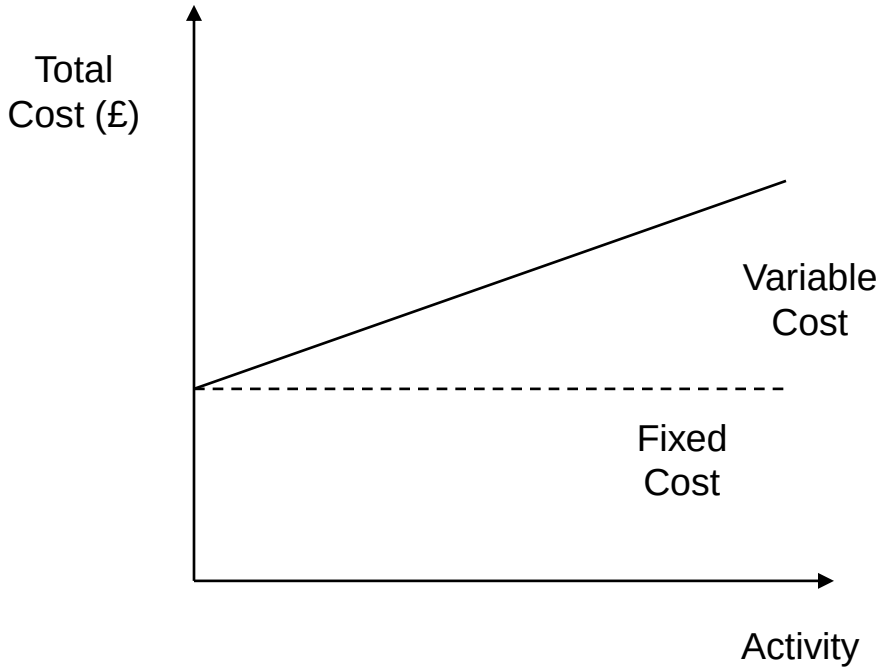




Cost Behaviour

Semi Variable

A cost which has both a fixed and variable element.

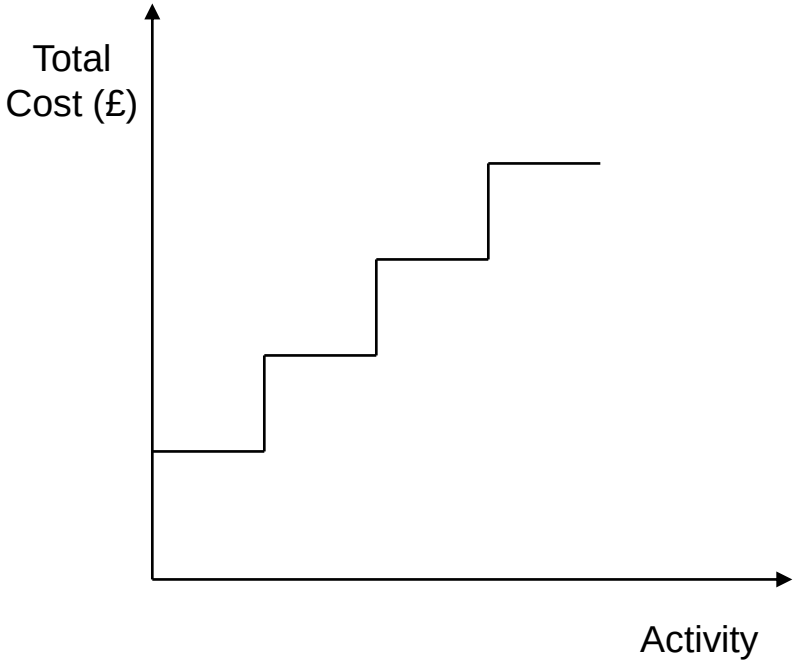


Cost Behaviour

Stepped Cost

A cost which is fixed for a particular range of activity levels, but once the upper limit of that range is passed a new higher level of fixed cost is incurred.

The engaging of resting/hibernating resources



Break-even

- Turnover

The amount generated by sales

- Profit

Sales – costs

- Contribution unit

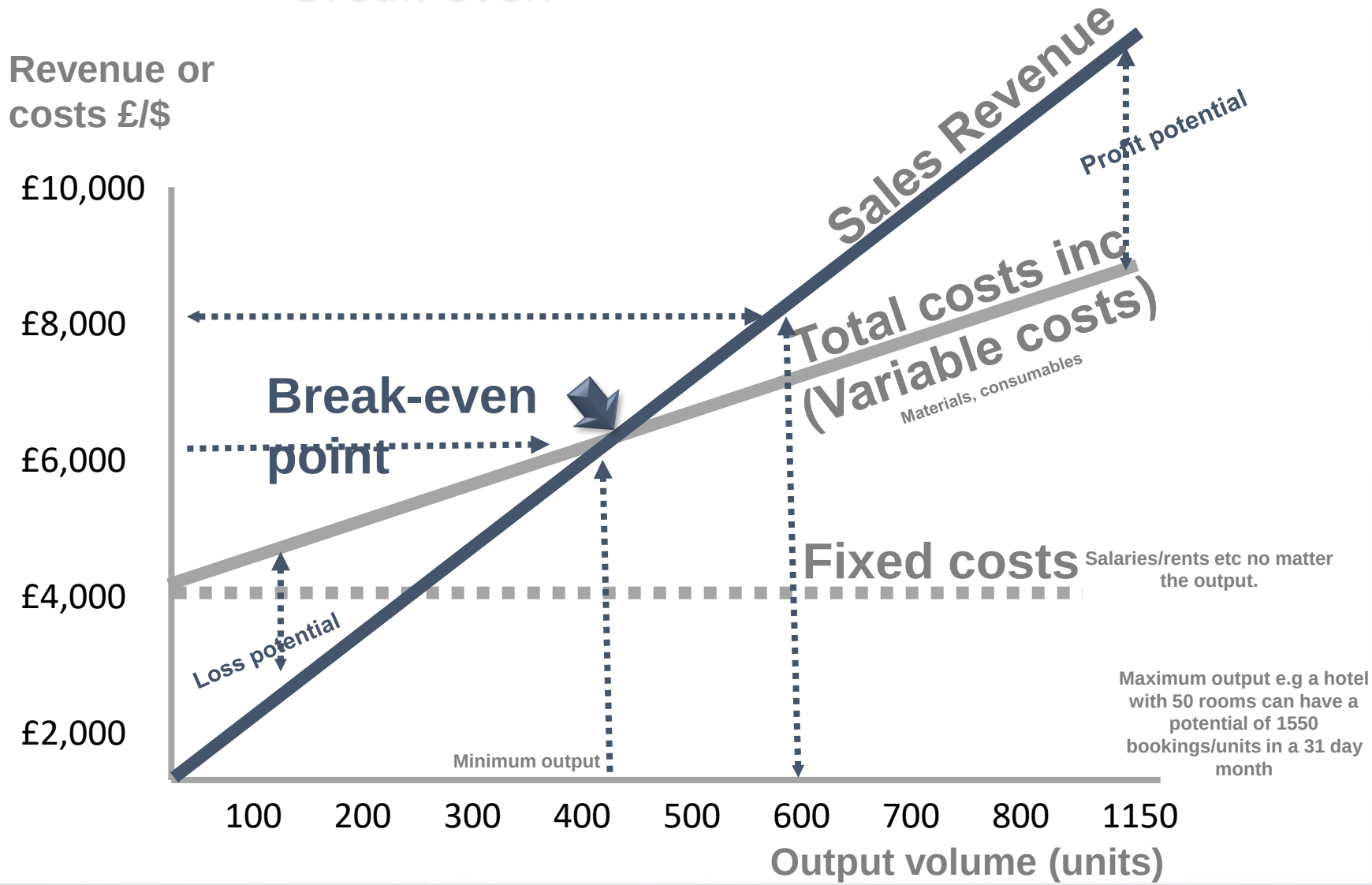
3 things you need to know to perform a breakeven analysis

- Fixed costs
- Variable costs to produce each unit
- Price per unit

Simply-

Breakeven = Fixed costs / Price per unit – Variable costs

Break-even


Revenue or costs £/$
£10,000
£8,000
£6,000
£4,000
£2,000
Sales Revenue
Profit potential
Total costs inc (Variable costs)
Materials, consumables
Break-even point
Fixed costs
Salaries/rents etc no matter the output.
Loss potential
Minimum output
Maximum output e.g a hotel with 50 rooms can have a potential of 1550 bookings/units in a 31 day month
100
200
300
400
500
600
700
800
1150
Output volume (units)

Break-even Activity 45 mins

Let's take the example of an 87-rooms hotel at £84 per room per night The hotel operates 365 days per year and has 58% annual occupancy.

You will need to figure out the fixed costs and variable costs for each department
e.g for sales and marketing the total cost is £58,112 with 50% as variable costs and 50% fixed costs meaning £29,056 for each. (Easy percentages – move the decimal point to the left to find 10% and multiply as needed)

Next figure out the potential maximum occupancy.

Next find the variable cost per room- this is total variable costs divided by the number of rooms sold on 58% occupancy.

Next find the contribution margin (selling price per room – variable cost per room.

Break even point is total fixed costs divided by contribution margin per room.

How many rooms does the hotel need to rent out per year (minimum output) to break even?

Department	Fixed %	Variable %	Total costs
Rooms	20%	80%	£299,763
F&B	20%	80%	£236,858
Other	20%	80%	£23,107
Leisure	20%	80%	£26,478
Undistributed Operating Expenses			
Admin & General	40%	60%	£28,413
Info. & Telecom Systems	100%	0%	£24,520
Sales & Marketing	50%	50%	£58,112
Property Operating & Maintenance	50%	50%	£50,786
Utilities	75%	25%	£50,686

I look forward to seeing you next week.

If you have any questions in the meantime, please send an email from your *student account*

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Next week……

Budgeting

Please have a look at the material on Moodle, which will be made available this Friday.