Activity 2: CVP Analysis for Sports-Strength

Name

Course

Instructor

Date

**A).** Sports-Strength’s breakeven point

**Breakeven point in Units= Fixed Costs ÷**contribution margin per unit

190,000 ÷ 4 = 47,500 units

**Breakeven point in dollars = sales per unit × breakeven point units**

$20\*47,500 units =$950,000

**B)** Margin of safety

In dollars

Margin of safety =Actual sales – Breakeven point

= $1,039,500 - $950,000

=$89,500

In Units

Margin of safety = (Actual sales- breakeven point) **÷** selling price per unit.

= $89500 ÷ $20 = 4475 units

Percentage margin of safety

= (Actual sales- breakeven point) **÷** Actual sales \*100

$89,500 **÷** $1,039,500= 0.086099

= 8.7%

8.7% represents the buffer zone in terms of percentage sales. Sports-Strength should use this metric for analyzing and forecasting sales and ensure that sales will not fall below the safety percentage (Lawrence., 2016).

C). since J&B plans to increase soccer jersey prices by $0.50 and with other factors remaining equal, the adjusted operating income would be -$8087.5. This is calculated by subtracting $25,987.50 (which is the total increase in price of the sold units) with the operating income.

Adjusted operating income = operating income – {(sales ÷ unit price) \*0.50}

$17,900- {($1,039,500/20)\* 0.50}

$17,900- $25,987.50= -8087.5

**D).** expected operating income under each proposed sales and marketing plan.

**The first plan**

Sales $1,065,488

Less: variable expenses

Cost of goods sold $795,217.5

Sales commissions $63,929.28

Total variable expenses $859,146.78

Contribution margin $206,341.22

Less: fixed expenses

Selling $116,500

Administrative $73,500

Advertisement $15,000

Total fixed expenses $205,000

Operating income $1,341.22

**Second plan**

Sales $1,205,820

Less: variable expenses

Cost of goods sold $922,452.3

Sales commissions $59,875.2

Total variable expenses $982,327.5

Contribution margin $223,492.5

Less: fixed expenses

Selling $138,500

Administrative $73,500

Advertisement $10,000

Total fixed expenses $205,000

Operating income $1,492.5

E). the reduction in the operating income that is greater than the projected additional $15,000 for advertisement is caused due to the inclusion of an increase of sales commission ($1,559.28). An increase in sales revenue results to a corresponding increase in sales commission which further increases variable costs and reduces the operating income.

MEMORANDUM

To: Sports-Strength Management

From:

Date: 5/5/19

Subject: Recommendation of a business plan.

I recommend the management to adapt the second business plan. This plan comprises of numerous benefits to Sports-Strength. Firstly, Sports-Strength will generate more returns based on this plan as compared to the first plan. Secondly, the second plan is based on a new advertisement campaign which includes a new dataset which provides Sports-Strength with more potential customers than it had before. Therefore, Sports-Strength will increase its customer base by attracting new customers and retaining the existing ones. Additionally, consumers are always looking for affordability and quality before purchasing goods and since Sports-Strength does not intend to raise prices or reduce jersey quality consumer will consider its products.

Thirdly, the second plan is believed to more successful than the current incentive-based marketing and sales plan in generating new sales. This provides Sports-Strength with a competitive advantage over its competitors by having a more superior advertisement campaign than before. Also, the proposed advertisement campaign incurs lower cost than the one proposed by the first plan. Fourthly, the recommended plan reduces sales commission by 2% which is great boost for the firm considering that Sports-Strength sales are expected to increase and therefore, the company will have less variable cost regardless of the increasing sales revenue. Lastly, despite the decrease in sales commission, the plan proposes an increase in salaries which acts as a motivation to employees to perform better.

Regards

References

Lawrence. (2016). Margin of Safety. Retrieved from https://www.myaccountingcourse.com/financial-ratios/margin-of-safety

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Solomons, D. (2011). Breakeven Analysis under Absorption Costing. *The Accounting Review*, *43*(3), 447-452.