Marginal Cost

Formulas to calculate Marginal Cost

Marginal Cost = Prime Cost + All Variable Overheads

OR

= (Direct material + Direct Labour + Direct Expenses) + All Variable Overheads

OR

= (Total Cost) – (All Fixed Overheads)

OR

= (Total Cost) – (Fixed Work Expenses + Fixed Office Expenses + Fixed Selling and Distribution Expenses)

Calculation of Marginal Cost

1. Equation Method

In two periods, total costs amount to Rs 40,000 and Rs 50,000 against production of 15,000 units and 20,000 units respectively. How much is marginal cost per unit and how much is fixed cost?

Sol: Refer to attached video

Contribution

The difference between selling price and variable cost (or marginal cost) is known as `contribution’ or `gross margin’. It may be considered as some sort of fund from out of which all fixed costs are met. The difference between contribution and fixed cost represents either profit or loss, as the case may be.

Contribution is calculated thus:

Contribution = Selling Price – Variable Cost

= Fixed Cost + Profit Or – Loss

It is clear from the above equation that profit arises only when contribution exceeds fixed costs. In other terms, the point of ‘no profit no loss’ will be at a level where contribution is equal to fixed costs.

Marginal cost equation

- $S - V = F + P$
- $S - V = C$
- $C = F + P$

And In Case Of Loss

- $C = F - L$

Where:

S = Sales

V = Variable Cost

C = Contribution

F = Fixed Cost

Thank You

*In case of any query you are free to ask