BREAKING DOWN THE NUMBERS

4 Calculations to Know When Financing Equipment

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equipment financing solutions

An Introduction to Breaking Down the Numbers

Whether you've financed equipment before or considering it for the first time, you probably noticed calculations and terms being thrown around in the industry. If the idea of calculating gross profits and cash flow makes your head spin, don't worry. We can break it down for you.

This eBook breaks down major calculations to help your business, so you can set yourself up for success with equipment financing.

Table of Contents

Breakeven

Breakeven is one of the more useful and informative calculations to know about your financing and business planning. Simply, breakeven is the amount of income you need to earn from your equipment to match the amount of your monthly payment. This is useful when determining your return on investment (ROI) because it tells you how much profit your equipment can eventually bring in.

Terms To Know

Fixed Cost: The cost of your monthly payment.

Variable Costs: Any cost that depends on the sales volume (expenses from your equipment).

Selling Price: Your sales price for the service or product.

EXAMPLE

Let's take an example of a tow truck business.

In this example, a tow truck has a fixed monthly financing payment of $1,600.

Their variable cost is $20 to pay for gas and expenses per tow. They charge $80 per tow.

Fixed Cost: $1,600
Variable Cost: $20
Selling Price: $100

fixed costs / (price - variable costs) = breakeven

$1,600 / ($100 - $20) = 20 tows

$1600 / ($100 - $20) = 20 tows required per month to breakeven on their fixed monthly financing payment.

Depreciation

A key part of determining whether the equipment you're considering to finance makes sense for you is calculating its depreciation.

Depreciation is a way to calculate your equipment's useful life and helps evaluate the cost over its active years of use. By determining the depreciation of your equipment, you will better understand its value and the potential tax deductions it provides.

To calculate depreciation, take the initial cost of your equipment and subtract its estimated residual value (i.e., the estimated value of your equipment at the end of its useful life).

Then, take that number and divide it by the number of years your equipment will be put to use.

EXAMPLE

You purchased a tow truck for $80,000 in 2022. You estimate that you'll receive 10 years of use out of the truck. After ten years, the truck is estimated to be worth $35,000.

(initial cost - residual cost) / years of usefulness = depreciation

($80,000 - $35,000) / 10 = $4,500

The truck will depreciate $4,500 each year it is in use for 10 years. That $4,500 is tax deductible each year.

Net Income & Gross Profit

Net Income

Similar to gross profit, net income offers a good look into the financial stability of your company. To be able to accurately calculate it, you'll need to have a solid grasp on your total expenses including cost of production, SG&A (selling, general, and administrative expenses), etc.

Once you understand all of the expenses related to your business, you can determine net income by subtracting them from your total revenues.

Gross Profit

The gross profit of your business is a clear indicator of how things are going financially, and it's often used by financing companies to get a quick overview of your ability to afford new equipment. Luckily, once you have a grasp of your expenses and sales, calculating gross profit is easy.

EXAMPLE

You discover that by adding another piece of equipment could increase the gross sales of your business by $25,000 per month. You will need $15,000 to complete those $25,000 of sales. After the cost of goods sold, you will have a gross profit of $10,000.

gross sales - cost of goods sold = gross profit

$25,000 - $15,000 = $10,000 Total Gross Profit

Liquidity & Cash Flow

Liquidity

Liquidity is often a huge factor in determining a business's financial situation and an important part in its success. Liquidity refers to a business's ability to use liquid assets (cash) to pay for expenses or other needs.

Liquid Assets: Cash
Hard Assets: Equipment

Cash Flow

As a business owner, knowing your cash flow can help determine your buying potential and know how much you need to start financing your equipment.

For Example: If you determine your business can generate $5,000 each month after expenses, you can determine when you have enough capital to make a $20,000 down payment for a $100,000 truck. By determining your business's cash flow, you will have enough cash in 4 months.

EXAMPLE

Current Assets: $5,000
Current Liabilities: $5,000
To determine your liquidity ratio the simplest way is to divide your current assets by your current liabilities.

currrent assets / current liabilities = liquidity ratio

$5,000 / $5,000 = 1

Now You Know

Although there are a few more things that come into play when determining your business's financial well-being and ability to finance equipment, these calculations are great for getting started.

With these calculations, you now have a better understanding of important terms that come along your way while growing your business with equipment financing.

You Aren't on Your Own

Still feel a little overwhelmed with the formulas? You aren't alone. Rather than calculating these numbers on your own, you can use Beacon Funding's Equipment Financing Calculator to determine your monthly payment, Section 179 tax savings, and breakeven estimate!

beaconfunding.com/calculator

**To the best of Beacon Funding's knowledge, these formulas and calculations are correct. The numbers used in all formulas are not representational of any business and should not be used to gauge your business' financial health. All information is intended for educational purposes only and is not to be taken as financial advice. For detailed look at your business financials, speak with your accountant. Use this information at your own discretion.*

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