SUMMARY

Fixed and Variable Costs

Costs are not simply costs. Differentiating between fixed and variable costs can be decisive when calculating an additional order.

Fixed costs always stay the same within given capacity limits (capacity utilisation), no matter whether the firm is closed or works to full capacity. Thus the amount of fixed costs is independent of the respective capacity utilisation (= operating rate)of the firm.

Examples of typical fixed costs: rent, lease payments, costs for permanently employed personnel, insurance premiums, etc.

The positive aspect of fixed costs is: if you produce more, no additional costs will be incurred. The fixed costs will be spread over a larger number of units, which thus leads to lower costs per unit (= **Fixed cost degression**).

The negative aspect of fixed costs (also called continuing or ongoing costs) is: even if the firm produces nothing - e.g. because it is closed temporarily – the fixed costs have to be paid.

Variable costs will change immediately when a company produces more, less,or nothing at all. The amount of variable costs depends on the respective capacity utilisation (= operating rate) of the firm.

Examples of typical variable costs: consumption of materials, merchandise used (sales input), consumption of raw and auxiliary materials, supplies, electricity, etc.

The pleasant aspect of variable costs is: if the company produces nothing, it will incur no costs either.