

# What is the Degree of Operating Leverage?

## Worksheet

DOL = Contribution Margin Operating Income (EBIT), or equivalently the percentage change in EBIT divided by the percentage change in sales.

$$\text{DOL} = \frac{\% \Delta \text{ EBIT}}{\% \Delta \text{ Sales}}$$

## Questions

1. A company has CM = \$50,000 and EBIT = \$25,000. What is its DOL?

- A) 0.5
- B) 1
- C) 2
- D) 5

2. With a DOL of 3, a 4% increase in sales produces roughly what change in EBIT?

- A) 3%
- B) 4%
- C) 12%
- D) 7%

3. Which company likely has the highest operating leverage?

- A) A consulting firm paid per hour of work
- B) A software company with high fixed R&D costs and near-zero marginal cost
- C) A retailer buying inventory per unit sold
- D) A staffing agency paying commissions per placement

4. A high degree of operating leverage means the business is

- A) Immune to sales swings
- B) More sensitive to sales swings, in both directions
- C) Guaranteed higher profit
- D) Using no fixed costs

5. A company has a contribution margin of \$40,000 and operating income of \$10,000. Find the DOL and predict the EBIT effect of a 10% sales increase.

6. A firm has CM = \$60,000 and EBIT = \$20,000. What is its DOL?

7. Sales rise by 5% and EBIT rises by 20%. What is the DOL?

8. Define: What does degree of operating leverage measure?

9. Define: DOL formula?

10. Define: What raises operating leverage?

## Answer Key

1. C)  $2 - DOL = 50,000 / 25,000 = 2$ .
2. C)  $12\% - \%EBIT = DOL \%Sales = 3 \cdot 4\% = 12\%$ .
3. B) A software company with high fixed R&D costs and near-zero marginal cost - High fixed costs and low variable costs per unit create high operating leverage.
4. B) More sensitive to sales swings, in both directions - High DOL amplifies both upside and downside swings in operating income.
5.  $DOL = CM / EBIT = 40,000 / 10,000 = 4$   $\%EBIT = DOL \%Sales = 4 \cdot 10\% = 40\%$  A 10% rise in sales produces a 40% rise in operating income.
6.  $DOL = 60,000 / 20,000 = 3$  Every 1% change in sales moves EBIT by roughly 3%.
7.  $DOL = \%EBIT / \%Sales = 20\% / 5\% = 4$  This company has high operating leverage - EBIT is 4x more sensitive than sales.
8. How sensitive operating income (EBIT) is to a percentage change in sales.
9.  $DOL = Contribution\ Margin\ Operating\ Income, or\ \%EBIT\ \%Sales$ .
10. A higher proportion of fixed costs relative to variable costs.

### Bounlu

All cards, step-by-step solutions and an AI tutor are in the Notek app.  
Promy turns exam dates into automatic reminders.