

B-24.02

Pure Comfort manufactures and sells mattresses with adjustable air chambers. Pure Comfort has been producing and selling approximately 500,000 units per year. Each unit sells for \$600, and there are no variable selling, general, or administrative costs. The company has been approached by a foreign supplier who wishes to provide the air compressor component for \$90 per unit. Total annual manufacturing costs, including air compressors, is as follows:

| | |
|---------------------------|---------------|
| Direct materials | \$ 50,000,000 |
| Direct labor | 80,000,000 |
| Variable factory overhead | 16,000,000 |
| Fixed factory overhead | 35,000,000 |

If Pure Comfort outsources the air compressor, it is expected that direct materials will be reduced by 20%, direct labor by 30%, and variable factory overhead by 25%. There will be no reduction in fixed factory overhead.

- (a) Should Pure Comfort outsource the air compressor?
- (b) If outsourcing the air compressor will free up capacity, and enable Pure Comfort to increase production and sales to 600,000 units per year, would it make sense to outsource?