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MANAGEMENT ACCOUNTING 2

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Introduction

Management accounting is the process of determining financial information to assist in the understanding of a business performance. It comprises of the preparation of management reports and statements for the maintenance of sound decision making. This study sheds light on the financial performance analysis of Amana Ltd, a company which sells souvenirs to tourists in England. The study includes a monthly control report, performance analysis report and recommendations to Amana Ltd in areas of improvement. Moreover, Mr Amana's decision to go online and advice to set up its own online shop or sell on Amazon has been assessed in this study.

Part A

(i). Monthly control report showing original budget, flexed budget and variances

Monthly control reports aim to review and assess a company's financial and operational performance on a monthly basis. The monthly control comprises the development of original, flexed and actual budget of a venture. It aids in understanding a variable performance (Wellersaccountants.co.uk, 2021). The monthly control reports of Amana Ltd have been made as per cost breakdown structure for 2020.

Control Report for Amana Ltd					
Items	Cost per unit	Original (£)	Flexed (£)	Actual (£)	Variance
Units		100000	80000	80000	
Selling price	£25	£25	£25	£20	£5 UF
Revenue		2500000	2000000	1600000	(400000) UF
Variable costs:					
Materials	2.5	250000	200000	280000	(80000) UF
Labour	4	400000	320000	440000	(40000) UF
Overhead	1.5	150000	120000	120000	0

Contribution	17	1700000	1360000	760000	(600000) UF
Fixed overheads:					
Warehouse rental		200000	200000	170000	30000 F
Insurance		100000	100000	100000	0
Full time supervisor salary		50000	50000	35000	15000 F
Profit		1350000	1010000	455000	(555000) UF

Variance investigation is a subject of management accounting that facilitates and influences decision making (Budde, 2009). Amana Ltd has a relatively high variance due to a reduction in performance during 2020. The venture had been successfully operating for 40 years and understands the dynamic nature of the tourism industry. However, the Covid-19 pandemic created imposition of restrictions on movement and travel by the English Government. It has severely impacted the tourism industry. Comparing the original, actual and flexed performance, unfavourable variance has taken place in Amana Ltd. Three stages of variance analysis include variance calculation, problem identification and understanding the causes of the variance (Emsley, 2000). In Amana Ltd, unfavourable variance has been identified in revenue and variable cost. Unfavourable variance indicates the declining performance of Amana Ltd in the tourism industry and the reason behind unfavourable variance is government's restrictions due to the global pandemic. The monthly control reports of Amana Ltd indicate a reduction in cost power unit and sale unit in its actual budget as compared to the original budget. Also, variable costs in the flexed budget are higher than in the original budget, which further demonstrates the unfavourable variance in performance. The fixed expenses of the venture show favourable variance in actual budget of the company. The overall performance of Amana Ltd has declined in 2020 due to the pandemic situation.

(ii). Report on Amana Ltd.'s performance during year 2020 using control report

The performance report addresses the outcome of monthly control report. As per Pradhan *et al.* (2018), performance report is developed for defining the performance of an organisation in a particular time period. In order to analyse the performance of Amana Ltd, monthly control

reports for 2020 have been used. The performance of Amana Ltd has been discussed through an analysis of the following topics:

Unfavourable variances for revenue, materials, labour, contribution and profit

Maintenance of higher revenue, contribution and profit can take place in business by ensuring lower variable cost. Variable cost of venture includes material, labour and overhead expenses (Drury, 2018). Amana Ltd has reduced revenue, contribution and profit due to an increase in its variable costs. An unfavourable variance of approximately -£400,000 in revenue, -£600,000 in contribution and £-555,000 in profit has taken place as labour cost increased by £40,000 and material cost by £80,000. As per Alegre and Sard (2017), price strategy is a long-term framework that facilitates the setting of the initial prices of products and services. As variable cost of Amana Ltd enhances, inadequate price strategy of venture has been analysed. So, inappropriate performance of Amana Ltd has been found in 2020.

Reduction in price for increasing sales

Revenue generated by an organisation is heavily influenced by the quantity of product sold and the price at which it was sold. As per Guizzardi *et al.* (2017), a higher quantity sold at higher sale prices tend to increase business revenue. Reducing the sale price helps a company to increase its sales and gain a competitive advantage (Alegre and Sard, 2017). Consequently, in an attempt to increase sales Amana Ltd has suffered a decline in its sale price from £25 to £20. The strategy of Amana Ltd does not appear to be sustainable in the long-term as maintaining reasonable prices of products helps in generating long-term revenue and growth in market. As Amana Ltd reduced its sale price and sales units, it was unable to gain growth.

Reason behind the increment in cost

Amana Ltd's monthly control reports denote an increment in the cost of materials and labour. Material cost has been increased by £80,000 and labour cost by £40,000. This increase in expenditure has been a cause of the £555,000 reduction of profit. The Covid-19 outbreak has presented significant issues for tourism industry. Government has imposed restrictions on travel and movement of tourism sector. Thus, the cost of managing business in the tourism sector has increased. Consequently, the economic recession has caused a net increase in Amanda's costs. For dealing with this issue, E-Commerce platform for operating in tourism industry can be used. As opined by Priambodo *et al.* (2021), E-Commerce adoption is process

of transferring, buying and selling products and services through information via computer networks.

Sustainability of lower warehouse and supervisor salary

The monthly control report of Amana Ltd shows slight reduction in warehouse rental, insurance and full-time supervisor salary in flexed budget as compared to original budget. It indicates favourable variance in performance of Amana Ltd. Maintaining lower fixed costs has helped in slightly improving the actual profit figure. Lower warehouse and supervisory salaries seem to be sustainable for Amana Ltd. However, an excess reduction in fixed expenses may adversely impact the production process of Amana Ltd. Using a digital mode of business establishment or E-Commerce may be helpful for maintaining fixed cost (Tolstoy *et al.* 2021). So, Amana Ltd needs to maintain consistency in fixed expenses.

(iii) Recommendations to Amana's CEO on areas of improvement

An analysis of monthly control report and performance report of Amana Ltd indicates a reduction in performance of 2020. To turn around that reduction, the following recommendations are provided to Amana Ltd:

Long term contracts with warehouse owners

Mr Amana is required to enter into long-term contract with owners of warehouses in order to ensure that rentals are not increased significantly in near future. In 2020, Amana Ltd was able to maintain a reduction in rent of warehouse by £3000. However, due to an absence of a contract, that cost is susceptible to future increase. This increment would adversely impact the profit of Amana Ltd. Therefore, a longer-term contract is advisable.

Increment in material cost

Amana Ltd is a production-based business and the cost of material has significant impact on its cost structure. As a result, monitoring the costs of material is necessary for Amana Ltd. Souvenirs are key products of Amana Ltd and increment in cost structure took place in 2020. So, Mr Amana is required to make sure that costs of material are under control without compromising with quality of product. As per Weustink *et al.* (2020), maintaining good quality of material tends to enhance the quality of final product produced. Thus, Mr Amana is required to control increment in material cost for boosting profitability.

Reducing prices may not be sustainable strategy

Monthly control reports of Amana Ltd show a reduction in price per unit from £25 to £20. Such reduction was conducted to make significant sales of souvenirs during the pandemic situation. However, reducing prices may not be sustainable strategy for Amana Ltd as it is not helpful for promoting business profitability. As per Alegre and Sard (2017), maintaining adequate sale prices helps an organisation in ensuring competitive position in the market. So, prices should be reviewed by Mr Amana for ensuring that adequate prices are imposed on sale. This would help Amana Ltd to generate sustainable growth.

Outsourcing production to low-cost countries

This paper has already outlined, an increment in the cost structure of Amana Ltd in 2020 is evident. This increment took place due restrictions imposed by the Government in the pandemic situation. As the company mainly operates in England and souvenirs are manufactured in China, this may decline profit margin of company. China is a low-cost country but the pandemic has caused the cost of manufacturing products in China to increase. Therefore, outsourcing production to low-cost countries would help Amana Ltd in maintaining sound business performance. Along with China, Mr Amana can outsource production in Brazil, Russia, Mexico or China which are considered as lower cost countries compared to the US, UK, Canada and Australia. It would help Mr Amana in boosting contribution on sale by minimising operating costs.

Switching suppliers as cost of materials have gone up

The key suppliers of Amana Ltd are China-based as Souvenirs are produced by Chinese manufacturers, according to designs made by the Amana team. However, Amana Ltd must switch suppliers to compensate for the increased cost of materials. This adversely impacts the profit figures of the company in 2020. Also, operation must be made by Amana Ltd in both physical and online market for increasing growth in tourism industry.

Part B

Introduction

The effectiveness of business decisions can be analysed through relevant costing. Amana Ltd has used relevant costing to identify whether selling their product directly online or through selling their product through Amazon is more beneficial.

Profitability analysis for implementing new strategies

In the Books of Mr Amana		
Estimation of Annual Budget for online sales		
Particulars	Units	Amount
Sales Revenue	100000	£ 25,00,000.00
Operating cost		
setting delivery network cost		£ 1,50,000.00
Website Upgrading cost		£ 50,000.00
Programmer's salary		£ 35,000.00
Total cost		£ 2,35,000.00
Profit		£ 22,65,000.00

This above table indicates value of profit worth £ 2,265,000.00 after considering their setting on delivery network cost, website up-gradation cost. In this calculation, it has been assumed that if the selling price per unit of product is £25. Selling the product directly from their websites carries certain benefits, including price control benefits. Amana Ltd can process their pricing of their product after understanding the market segment and demand for their product by maintaining minimum and maximum pricing policy. Besides that, there will be a benefit of the return policy of their product which they can set by considering their own requirements. Creating customer bases after understanding the market segment will increase their sales unit and help to sustain more profitability (Filippas *et al.* 2019). In addition to this, direct sales online will increase their goodwill which helps to increase their sales volume. Considering the

cost structure for selling products online, requires up gradation of their websites and delivery network cost. It also requires the salary of programmers to develop websites and network channels to improve sales and profitability.

In the Books of Mr Amana		
Estimation of Annual Budget for product sale through Amazon		
Particulars	Units	Amount
Sales revenue	65000	£ 16,25,000.00
Amazon fulfilment fees		£ 50,000.00
Profit		£ 15,75,000.00

Another strategy is to increase sales unit and profitability, Amana can buy their product through Amazon and it will incur a profit of £15,750,000.00. The disadvantage of selling products via Amazon is to eliminate control pricing policy and return policy. Amana will not be able to adjust their pricing policy as Amazon will not permit them to control their pricing policy. According to Omran *et al* (2021), price control policy is a process of controlling minimum price and maximum price of product after considering required legislation of Government. Since Amazon will not permit them to control their pricing policy, management of Amana is not able to set prices of specific products as well as essential products. In the long-term period, it has been reported that lack of control in pricing leads to disruption for an organization as it causes inferior quality of goods, shortage of goods and rationing. Amazon has maintained their return policy period of 10 days from delivery period and in this respect, Amana cannot implement their own return policy. Making sales through Amazon can affect Amana's return policy. However, Amazon already has a good customer base which helps this organization to increase their sales unit. In order to sell their product via Amazon, it requires Amazon fulfilment fees of £ 50,000.00, which is included as a very minimum cost.

In this situation, Amana should make decisions over directly selling their product online strategy to increase their sales unit and profitability. Using online retail platforms, such as Amazon will create difficulty as there will be no control in their pricing and return policy. Furthermore, it has been shown that online selling incurs a sales unit of 1,00,000 whereas Amazon is only able to increase sales unit of 65,000.

Making decision after analyzing risk of Amana

Implementing a new strategy such as 50% of product selling directly from their own website or through Amazon increases some certain risk. Due to the outbreak of corona virus, the company has already suffered from financial losses and for this reason management of Amana needs to make decisions after analyzing those certain risks.

Risk of cost ineffectiveness

Implementing new strategies like selling products online needs to create a strong customer base as its objective is to increase sales units (Chen *et al.* 2019). This strategy increases the chances of cost ineffectiveness if Amana will fail to create customer attraction in an online platform. Since, selling online products needs to incur some certain cost such as website upgradation cost, delivery network cost. It also needs to provide a salary to website developers to bring innovation in their company. In this respect, the management of Amana Company may face financial stress if this company fails to achieve their desired sales unit and this cost will have no benefit for the future. Selling through Amazon increase the risk of cost ineffectiveness if their product failed to gain enough customers attention and failed to create a strong customer base in this huge retailing market. Directly selling product through own online website can threaten sustainability of this organization as well as it increases the risk of financial losses. However, selling directly in online will help to increase their sales unit as well as profitability.

Risk of data breaching in online

Online website upgradation can breach data confidentiality such as cost, profit, budget and sales price. Inefficiency of technicians and web developer can lead to this disruption and for this reason company may faces financial stress as well as managerial conflicts such as collaboration and coordination affect this organisation's growth. In this situation, company needs to secure their network and operational performance for updating websites. However, making sell through Amazon provides a secure network which reduces the risk of data

breaching but this strategy has no cost benefit for the future as it minimum increases their sales unit and profitability.

Conclusion

From this above report, it can be concluded that Amana selling its product through its own website carries cost effectiveness and profitability as it increases proportionally with the sales units. Relevant costing helps to gain competitive advantage for an organization by attracting customer in this market volatility. Addressing risk for implementation for making decisions, it has been found that, management should make decisions that this can be actually cost beneficial for this company.

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