

# **MANAGEMENT ACCOUNTING**

## **LCBB5002**

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## Introduction.

It is generally accepted that the words "Accounting" and "Management" are adopted individually. The truth is, none of these words matter. Governance covers the entire spectrum of administration of an organization. Still, organizations can vary and take different forms and be from the private and the public sectors and non-profit organizations. Accounting, in turn, covers activities that try to assess the organization's effectiveness and plan its presentation in the future. In the current competitive business environment and the public sector, the focus is increasingly on efficiency and price-quality, all organizational actors take responsibility for both accounting and management. From this point of view, each participant in the organization affects the final results of the organization as a whole. At some times, the management accounting we could define, such as the preparation of useful information for managers, will help manage the organization (Weetman, 2013).

The deviation analysis seeks to understand the difference between the planned and targeted level of implementation and actual effectiveness and is a basic form of organizational feedback. The study of deviations is a three-step process in which variations are calculated in the first stage. The second stage identifies the problems that led to their occurrence, and the third stage identifies the causes of these problems. However, while the accounting documents describe the calculations in detail, they do not provide sufficient information on the last two stages and, more specifically, on the third (Duchac, 2007).

## Part A: Variance analysis.

By examining the deviations, sufficient information can be obtained to understand the problems that caused these deviations. This information is used to show the senior management staff the right steps to solve them. In our report, we look at the UK-based cleaning company XLG. The production it produces is two chemical agents, the chemicals X, and Y. Due to force majeure caused by the spread of Kovid-19 and the subsequent lockdown, there were deviations in the supply, the selling price, and the main ingredient's price.

## Sales and Contribution:

### Sales price variance:

Sales price variance = (actual price – standard price) × actual volume

| Description | Actual Price | Standard Price | Difference | Actual Volume | Sales Price Variance |
|-------------|--------------|----------------|------------|---------------|----------------------|
|             | £            | £              | £          |               | £                    |
| Chemical X  | 45           | 35             | 10         | 850           | 8500                 |
| Chemical Y  | 37           | 30             | 7          | 750           | 5250                 |
|             |              |                |            | Total         | 13750                |

Favorable

### Sales volume contribution variance:

Sales volume contribution variance = (actual sales volume – budgeted sales volume) × standard margin

| Description | Actual sales volume | Budget sales volume | Difference | Standard margin | Sales volume variance |
|-------------|---------------------|---------------------|------------|-----------------|-----------------------|
|             |                     |                     |            | £               | £                     |
| Chemical X  | 850                 | 595                 | 255        | 25              | 6375                  |
| Chemical Y  | 750                 | 595                 | 155        | 20              | 3100                  |
|             |                     |                     |            | Total           | 9475                  |

Favorable

## Material price:

### Material planning variance:

Material planning variance = (original target price – general market price) × quantity purchased

| Description | Target price | Market price | Difference | Quantity purchased | Material planning variance |
|-------------|--------------|--------------|------------|--------------------|----------------------------|
|             | £            | £            | £          |                    |                            |
| Chemical X  | 2.50         | 4.50         | - 2        | 850                | - 1700                     |
| Chemical Y  | 2.50         | 4.50         | - 2        | 750                | - 1500                     |
|             |              |              |            | Total              | - 3200                     |

Unfavorable

### Material price operational variance:

Material price operational variance = (General market price on the time at purchase – actual price paid) × quantity purchased

| Description | Market price | Actual price paid | Difference | Quantity purchased | Material price operational variance |
|-------------|--------------|-------------------|------------|--------------------|-------------------------------------|
|             | £            | £                 | £          |                    |                                     |
| Chemical X  | 4.50         | 3.70              | 0.80       | 850                | 680                                 |
| Chemical Y  | 4.50         | 3.70              | 0.80       | 750                | 600                                 |
|             |              |                   |            | Total              | 1280                                |

Favorable

Critical analysis of the advantages and disadvantages of using dispersions in evaluation performance of managers.

The management team gets a real idea of what changes have occurred since the lockdown from the tables above. There has been an increase in sales, which is expected in this situation. From the beginning of the quarantine in March 2020, sanitary products' demand has increased several times. This was due not only to the fact that people wanted to provide the drugs they needed but also to an intense psychological moment caused by supermarkets' empty stands failing to meet the increased demand. Due to the situation and the impossibility of using standard transport, there is an increase in the main ingredient's price. As a small reassurance, we can note that due to the use of aircraft, it arrives on time and thus creates an opportunity to maintain the growing production pace. Increasing the price and quantity of products sold

also helps maintain balance, but most likely, managers will have to reconsider the budget set for the supply of the main ingredient.

The process we explained above can also be called the feedback process. Its main advantage is that it gives a clear signal when something goes wrong or changes and provides a quick opportunity to return operations to the rails. However, let us now consider the advantages and disadvantages of using variance analysis. The following factors can be noted as advantages:

- Easy to follow information. The visually presented information allows the monitoring to be carried out even by the junior management staff, as the senior managers can find out about what is happening at the moment through a quick review of the tables.
- Prepared information helps to make quick decisions and quickly plan future changes, which is especially useful in situations related to force majeure, such as epidemics, natural disasters, and wars.
- Managers can monitor events under constant control, which allows us to consider deviations as a control mechanism, which is appropriately designed to give us the necessary weekly, monthly, or annual information.

Even though this type of analysis has its advantages, it is good to note some of their disadvantages, which are essential to take into account to ensure their proper use:

- First of all, we must note a very interesting psychological moment. As the cost of necessary materials or the cost of labor rises, many managers are looking for options to buy cheaper materials or, as we see in multinational companies, move production to countries with cheaper labor.
- Encouraging the so-called "blame culture" leads us to the next drawback. Seeing the data, the heads of different departments can blame each other for specific results or decisions.
- The last drawback I would like to mention is the time it takes to prepare these analyzes, calculate all the data and deviations. On the other hand, with the advancement of technology, the use of more and more artificial intelligence in data processing, I believe this problem will be insignificant. This may become an advantage and allow even automated decision-making.

Deviation analyzes helps managers in a company to have a clear view of the budget and its changes. The shortcomings we mentioned are rather behavioral and could generally be avoided.

## Part B: Decisions based on the data obtained.

Coronavirus has fundamentally changed the world, and many company decisions that until recently seemed normal and even recommended are now totally rejected. The exporting production policy to countries with cheaper labor over the last few decades has played a bad joke in highly developed countries. Left without control over the supply of such essential products as medicines and medicinal products, they realized that they had to make a U-turn to resume production in their own countries. At the height of the KOVID-19 crisis, much of the production of medicines, sanitary preparations, and masks took place in countries such as India and China (Anon., 2020)

Let's look specifically at the situation with XLG and the main ingredient FamaQ for the two products of the company. What would be the best solutions given the radically changed situation on a global scale? To begin with, let's look at the facts:

- First of all, we need to highlight the problems that arise from international deliveries. The fact is that more and more people are shopping online. This naturally makes air and sea transport more expensive. In particular, maritime transport, the restrictions imposed due to KOVID-19, threaten the free movement of vessels and their crews. No one can say for sure what measures will be taken in a month, for example. The closure of international borders and ports may make it impossible to deliver. Some of the companies are facing bankruptcy (Smith & Hale, 2020)
- The next important point is the price increase. As an essential ingredient for the company's products is made in Brazil, its price would be difficult to control. Given the transport circumstances, the price is unlikely to decrease. Brazil, too, could hardly be called a stable country from a geopolitical point of view. Its president's attitude to international agreements, his contempt for the epidemic, which has led to many infections and casualties and ranked the country among the world's worst victims, makes it clear to any sober-minded investor that this is a country where any investment would be risky (Harris, 2020).

- Naturally, the situation surrounding leaving the European Union should not be overlooked. The United Kingdom has yet to sign trade agreements with the rest of the world as an independent state. However, it is not clear what these agreements will be and whether a possible deal with Brazil will not lead to new duties and taxes that would increase the price of the imported product. On the other hand, the trade agreement signed with the Community clearly describes the regulations on imports from third countries, so that the ingredient imported from Brazil at some point could be an obstacle if the company grows and decides to export some of its products to the European market.
- As noted in the analyzes, the demand for the company's products has increased by 45%. It will continue to grow, which will lead to a reduction in the cost of products, with non-existent transport costs from overseas, this could further increase profits from products. We should not overlook that delivery times will also be reduced and under control, without possible worries about lockdowns and delivery delays. It should also be noted that almost every company carrying out production outside the country has established costs for the team carrying out quality control, training of the local team, and organizing the work.

To justify all that has been said so far, we must answer a few questions:

1. Are the costs related to the business goals? - Definitely, as FamaQ is the main ingredient for the production of both XLG preparations. From this point of view, all costs related to the production and delivery of FamaQ are related to the business objectives
2. Do the costs have anything to do with the future? - To expect an increase in sales. And in the foreseeable circumstances, the search for such preparations will continue.
3. Does the price change with the decision of where to produce the preparation? -Yes, it changes because the production of FamaQ in the UK will reduce the price by 3 pounds and shorten the delivery time by 15 days, which in itself is a unique achievement.

It is, therefore, advisable to take the following decisions:

If the company wants to continue to grow, especially in a crisis, it would be better to build a plant in the United Kingdom. Although the construction of a new enterprise and staff training will take some time, in the long run, the

investment will pay off many times over. As the great Adam Smith said, demand determines supply (Smith, 2018). There are several reasons for this:

1. First of all, the crisis will not pass in a few months, and the country is already in the third lockdown in just one year. Due to the imposed measures, the use of cleaning products has increased significantly not only in households but also in hospitals, clinics, businesses, shops, restaurants, bars, gyms, libraries, and all public enclosed spaces.
2. From a psychological point of view, even after the end of the pandemic, when the measures are eventually relaxed, the population will continue to take strict hygiene measures. The fact is that every crisis is reflected in people's minds long after it is over.
3. Developing production on the territory of the country will be able to respond quickly to customer needs. The fact is that in the first lockdown in March 2020, for the first week alone, products were sold for more than 60 million pounds more than usual, 17.9 million of which were for toilet paper and cleaning products. In the production of the main ingredient in a distant country and dependent on supplies, the company would find it challenging to respond quickly.
4. With increasing production, the product's cost will decrease, and in the event of import, the cost of delivery will increase.
5. Full control of the production process is carried out. An essential ingredient in creating both of the company's products is produced in the United Kingdom. It is not affected by movement restrictions or lockdowns in other countries that may stop or slow down production.

## Conclusion.

Time is an essential feature for making investment decisions. In today's dynamic world, speed is vital. The costs, which are usually a single large amount, precede the benefits we receive in installments for a much more extended period. For the proper conduct of investment processes and the successful operation of a company, accounting analysis and management are essential. The concrete presentation of the information, its visual appearance, and structure contribute to the right management decisions.

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