

MANAGEMENT ACCOUNTING
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Introduction

The purpose of this assessment is to prepare a monthly control report containing an original budget, a flexed budget, and variances of Amana Limited, then prepare an income statement of the company and relevant recommendations required for Amana Limited. In the next part, an analysis will be done to advise Amana Limited on whether the company should have its shop or they should sell online.

In Accountancy, management accounting takes into account the relevant decisions that the company has taken regarding the finances and other performance-related topics the company. The information gathered in management accounting is essential for the investors to make relevant decisions regarding the financial positioning and performance of the company (Business News Daily, 2022).

Part-A

Monthly report of Amana Limited

A monthly control report of a company is prepared to assess the financial and operational performances of the company. If a company wants to see its past performances and make relevant decisions accordingly, these reports are needed. Internal stakeholders or the company's hired accountants often prepare these control reports every month to remain consistent with the regular changes happening to the company.

A monthly control report mainly has three components- original budget, flexible budget, and variance analysis. For Amna Limited as well, these budgets will be assessed for further analysis.

The original budget of Amana limited

The original budget is one type of detailed and rationally consolidated budget in which guarantors and borrowers' relevant transaction performances are taken into account. Most of the time in an original budget the gross profit and net profit, liabilities, assets, and net cash flows of the last 24 months are considered (Law Insider, 2022).

In the books of Amana limited

Original budget

Particulars	Unit	Amount (£)
sold (Unit)	1,00,000	
Selling price		25
Generated amount from revenue (1,00,000*25)		2500000
Variable cost		
Cost of materials = 100000*2.50		250000
Labour cost = 100,000*4		400000
Overhead = 100,000*1.50		150000
Total variable costs		800000
Contribution		1700000
Fixed overhead		
Warehouse rental Cost		200000
Insurance expenses		100000
warehouse supervisor salary (full-time)		50000
Fixed cost (Total)		350000
Net Profit		1350000

Table 1: Original Budget of Amna Limited

(Source: Self-report. 2022)

Here, the original budget of Amna Limited shows that 1,00,000 units of goods are sold at a rate of £25 to earn total revenue of £25,00,000. Also, variable costs are considered to be the cost of capital, cost of labor, and other overheads. Fixed costs don't change for any quantity of goods sold. Therefore, gross profit is evaluated by subtracting the cost of goods sold from the total

revenue. And the net profit of £1350000 is evaluated from the difference between gross profit and total operating expenses.

Flexible budget of Amana Limited

A company's flexible budget is used to determine the adjustments of the activity or volumes of the company. The main difference between an original budget and a flexible budget is that the particulars of an original budget cannot change but for a flexible, the volumes can change (Krumer-Nevo, 2020). For new start-ups, a flexible budget is used as the market demand-supply scenarios, the behavior of the consumers toward the company can't be estimated. The production level in different scenarios and different markets can be done following this type of budget.

In the books of Amana limited		
Flexible budget		
Particulars		Amount (£)
Selling unit	80000	
Selling price		20
Amount generates from revenue (80000 * 20)		1600000
Variable cost		
Labour		440000
Cost of Materials		280000
Overhead		120000
Total variable cost		840000
Contribution		760000
Fixed cost		
Warehouse rental		170000
Insurance		100000

Fulltime warehouse supervisor salary		35000
Total fixed costs		305000
Net profit		455000

Table 2: Flexible budget of Amna Ltd.

(Source: Self-report, 2022)

The flexible budget of Amna Limited shows that the company has sold 80,000 units at a lower selling price £20 to earn a revenue of £16,000,00. Following this trend, the company has earned a lower net profit of £4,55,000 as well.

Variance analysis of Amana Limited

The deviations of the particulars of a flexible budget from the original budget of a company are assessed in the variance analysis of management accounting (Osei and Eum,2018). In this analysis, the relevant information is provided regarding the cost structure. If a variance analysis is followed, the stakeholders find it difficult to form a flexible budget.

In the books of Amana limited			
Analysis of variances			
Particulars	Budgeted amount (£)	Actual Amount (£)	Variances
Unit sold= 100,000			
Selling price= 25			
Amount generates from revenue	2500000	1600000	900000
Variable cost			
Cost of Materials = 100000*2.50	250000	280000	-30000

Labour = 100,000*4	400000	440000	-4000 0
Overhead = 100,000*1.50	150000	120000	30000
Total variable cost	800000	840000	-4000 0
Contribution	1700000	760000	94000 0
Fixed overhead			
Warehouse rental	200000	170000	30000
Insurance	100000	100000	
Fulltime warehouse supervisor salary	50000	35000	15000
Total fixed cost	350000	305000	45000
Net Profit	1350000	455000	-8950 00

Table 3: Table to analyze the variances between the flexible and original budget

(Source: Self-report, 2022)

The variances in sales revenue are £9,00,000 which is 36% lower than that stated in the original budget. On a contrary, variable costs have increased significantly. The fall in sales revenue has resulted in a reduction of net profit by £8,95,000 which means the variance in net profit is 66% lower than the original budget.

Income statement of Amana Limited to assess the financial performance

From these reports, Amna Limited's financial performance for 2020 will be assessed by preparing an income statement.

An income statement is one category of the financial statements that the company uses to review its income and expenditures for a financial period (Say 1 Year). The respective profitability of the company is measured from an income statement (YATBAZ and ÇATIKKAŞ, 2019). Also, the statement is useful in guessing whether the undertaken strategies are useful or not. An income statement is used by the investors of the company to see the profit and loss statistics of the company, its sales, expenses, etc. There are relevant decisions made based on this income statement. Company owners also understand whether their strategies are paid off or they need better solutions.

Amana limited	
Income statement for the year 2020	
Sales revenue	2500000
Variable costs	
Cost of materials	250000
Cost of labor	400000
Other overheads	150000
The total cost of goods sold	800000
Gross profit	1700000
Other expenses	
Warehouse rental cost	200000
Insurance expenses	100000
Warehouse supervisor salary (full-time)	50000
Total fixed expenses	350000
Net profit	1350000

Table 4: Income statement of Amana Limited

(Source: Self-report, 2022)

This income statement of Amana Limited for 2020 is prepared based on the original budget of Amana Limited. The particulars considered in this income statement are mostly taken from the given original budget of the company.

Calculations and workings of the income statement

Sales Revenue: Sales revenue means the total amount the company earns by selling its goods. The more quantity of goods the company sells, the more revenue will be generated. As per the records of the original budget, the total number of units sold= was 1,00,000 and the selling price of each unit is £25. Therefore, the evaluated sales revenue is= $£25 \times 1,00,000 = £2,500,000$.

Total variable costs: Variable costs are those costs that vary with the number of units sold. To sell 1,00,000 units, the total cost of material is £250,000. Similarly, total labor cost and other overheads are taken to be £400,000 and £150,000 respectively. Therefore, total variable cost is = $£250,000 + £400,000 + £150,000 = £800,000$.

Gross profit: The gross profit is evaluated by differencing the variable costs from the total revenue (Nariswari and Nugraha, 2020). Here, the total revenue is £25,000,00 and the total variable cost is £800,000. Therefore, the gross profit is $£25,000,00 - £800,000 = £1,700,000$.

Net profit: Net profit's calculation formula is the difference between gross profit and operating expenses (Nariswari and Nugraha, 2020). Here, the total fixed costs will be subtracted from the gross profit to evaluate the net profit. The total fixed costs are recorded as £350,000 and the gross profit is £1,700,000. Therefore, the net profit= $£1,700,000 - £350,000 = £1,350,000$.

Relevant recommendations for Amana Limited:

The budgets, variances, and income statement of Amana Limited all have been assessed in detail and the first thing that will be recommended to the company is to control the expenses. In the flexible budget, the company's fixed costs have been reduced but the variable costs have increased by a good amount. This has resulted in a reduced in gross profit as well as net profit. So, the company should try to limit their expenses as they are not selling more units than what is proposed in the original budget but the cost of variables like materials, labor, and overheads per unit have increased. So, the company is not earning more than what is proposed but the expenditures are higher. Therefore, the company should undertake relevant strategies to control

the variable costs like applying Lean management principles, use of direct labor and materials, etc. (Camino Financial, 2022). so that the costs are constrained and the overall profitability of the company gets better.

Gross profit margin (%)	2020 (Original)	2020 (Flexible)
Gross Profit (£)	1700000	760000
Total sales (£)	2500000	1600000
Gross profit margin	68	47.5

Table 5: Gross profit margins of Amana Limited

(Source: Self-report, 2022)

The Gross-profit margin is computed by dividing the gross profit by the total value of sales into 100. The gross profit margin is lower in terms of the actual budget than the original budget. Also, the operating profit margin is almost half following the actual budget of the original budget.

Net profit margin	2020 (Original)	2020 (Flexible)
Net profit (£)	1,350,000	450000
Total sales	2500000	1600000
Net profit margin (%)	54	28.125

Table 6: Net profit margins of Amana Limited

(Source: Self-report, 2022)

Quite similar to the gross profit margin, the net profit margin is evaluated from the division of net profit from the total number of sales (Nariswari and Nugraha, 2020). Net profit margin as well is lower for the actual budget than the original budget. All these profitability ratios suggest that the actual performance of the company is not quite good according to the original budget.

Part-B

In the current world scenario, the online market is one of the most sorted marketing strategies in the world. In this selling strategy, there is no physical existence of the market and all products are exchanged through an internet-based system. Different types of digital, and electronic methods are undertaken by the companies when they sell their products online (Kreutzer, 2018). The company can have its website or it can sell through social media as well. Also, some costs of the company are constrained as well like advertisement costs, labor costs, etc. Applications like email, WhatsApp, or a blogging page can be opted by the companies as well for online marketing (The Balance Small Business, 2022).

Amana Limited has recently thought of promoting the business and selling the goods through online platforms. The company has mainly decided this because of the outbreak of the corona pandemic which is one of the prime reasons behind the sudden increase in the online selling of products. The company has thought of two options- one is the company's online website and another is selling through Amazon which is currently one of the best platforms for online marketing.

Start-up requirements for option 1- have your website

Option 1: If Mr. Amana develops his website for selling products	
Expenses	Amount (£)
Setting up a new delivery network	150000
Salary of IT programmer	35000
Upgrading website and handling charge	50000
Total expenses	235000
Estimated Sales, Mr. Amana can get	
Units = (1,00,000)	
Selling price (per unit)	20

“Total Sales amount”	2000000
“Net profit = Sales - expenses”	1765000

Table 7: Start-up requirement and estimated sales from having an own website

(Source: Self-report, 2022)

The company has predicted that £150000 will cost to set-up a new network. The estimated wage of an IT programmer is taken as £35000, website upgradation and handling charges are taken to be £50,000. So, total expenses are $£150,000 + £35,000 + £50,000 = £235,000$. The company expects to sell around 100,000 units at a rate of £20. Therefore, the earned revenue is estimated to be $100,000 * £20 = £20,00,000$. Hence, the evaluated net profit that the company expects from the sales of 100,000 units is $= £2,000,000 - £235,000 = £1,765,000$.

Option 2-Selling products on Amazon

2nd Option: selling through Amazon	
Expenses	Amount (£)
Fulfillment fees of Amazon	50000
Estimated sales	
Unit = 65000	
Price per unit	20
Number of sales	1300000
Net profit= Amount of Sales - Expenses	1250000

Table 8: Cost estimates and expected profit by selling through Amazon

(Source: Self-report, 2022)

The company estimates that a royalty charge of £50,000 has to be paid to Amazon to own the rights to sell products through Amazon. And, it is expected that at least 65,000 units will be sold through Amazon at a selling price of £20 per unit. Therefore, total sum of sales= $£20 \times 65,000 = £1,300,000$. So, evaluated net profit is valued at $£1,300,000 - £50,000 = £1,250,000$.

The price of the company's shares can be affected by the income statement of a company. The profit earned by the company from classifying the revenue and accrued expenses during a particular period is summarized easily in the income statement. But these are not income statements, rather these can be called profit and loss proformas. Profit and loss proforma is a bit different from the Income statement as the latter recognizes the performance while the before one only predicts the probable profitability of the company for a particular period.

Relevant recommendation for Amana Ltd.

Assessing the start-up requirements and expected net profit of both options, it can be seen that both options are quite relevant for Amana Limited. The company will earn a profit on both occasions and there is not a huge difference between the profits if the expectation analysis works. If the company opts for having its website, the net profit will be higher than the other option which is quite natural as well (Salehoo, 2022). But also, it will require a higher cost to set up a new website and sell products through that website. If the company sells through Amazon, the profit will be less as the company expects that number of units sold will be dropped because there are other competitors as well. But Amazon will give a surety about the selling of the products while if the company sells through its website, the selling of the products will not increase straight away. It will take time as people are not aware of the new website. Therefore, the company has to work hard regarding the advertisements and promotion of the new website and provide regular feedback and respective suggestions from the customers, the server loading issues need to be managed as well. On the other hand, if the company ties up with Amazon, all these issues will be looked over by Amazon itself (Rheude, 2022). Therefore, Amana Limited can focus on other aspects like the quality improvement of the products, production performance, cost control, etc. If Amana Limited wants to be risk averse, then they can go for selling through Amazon and if they want to be a risk-taker, then they should develop their website for the sale of products and a larger profit will be enjoyed by the company as a reward of taking the risk.

Conclusion

The relevant topics of Management Accounting are studied considering the scenario of Amana Limited. The original budget and flexed budget of Amana Limited do not match as the company has not estimated that it will sell 80,000 units for £20 than selling 100,000 units at £25 as stated in the original budget. Therefore, the contributions and net profit have varied from the actual one as well. The profitability ratios resemble that the company has not done well in the actual sense. Now the company plans to opt for online marketing because of Covid-19 effects and trying to remain its sales. The company can sell through Amazon or have its website to sell products.

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