

MODULE CODE: LCBB4001
ACCOUNTING FUNDAMENTALS

Lecturer name: Miss Widin Bongasu Sha'ven

Student name: Velko Angelov Chakalov

Student ID: 1917352

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Ans. to the Question No. 01

(a) Break-even point calculation for Sandals of Solent Ltd.

$$\begin{aligned}\text{Total variable cost per unit} &= (\text{Direct labour} + \text{Direct Materials} + \text{Other direct costs}) \\ &= (£1.35 + £1.75 + £0.40) \\ &= £3.5\end{aligned}$$

$$\text{Selling Price per unit} = £5.75$$

$$\text{Fixed cost of production} = £180,000$$

$$\begin{aligned}\text{Break-even point (in Units)} &= \frac{\text{Fixed Expenses}}{(\text{Per unit selling price} - \text{per unit variable cost})} \\ &= \frac{180,000}{(5.75 - 3.5)} \\ &= 80,000\end{aligned}$$

$$\begin{aligned}\text{Break-even point (in terms of revenue)} &= \text{Break-even sales (in unit)} * \text{selling price per unit} \\ &= 80,000 * £5.75 \\ &= £460,000\end{aligned}$$

(b) Profit made on selling 90,000 units

	£
Revenue (90,000* £5.75)	517,500
(-) Costs:	
Variable cost (90,000*£3.5)	315,000
Fixed cost	180,000
Total cost	495,000
Net Profit	22,500

c) New profit figure with improved Sandals

New variable cost per unit = (Direct labour+ Direct Materials+ Other direct costs)

$$= (£1.40 + £1.90 + £0.40)$$

$$= £3.7$$

New Selling price = £5.75 + £0.25 = £6.00

New sales units = 90,000*(1+0.05)

$$= 94,500$$

	£
Revenue (94,500*£6.00)	567,000
(-) Costs:	
Variable cost (94,500*£3.7)	349,650
Fixed cost	180,000
Advertising cost	12,500
Total cost	542,150
Net Profit	24,850

(d) Limitations of break-even analysis

Despite being a very useful analytical tool, break-even analysis has its own set of shortcomings.

Firstly, it inherently assumes price will always maintain a linear relationship with demand.

That means, no matter how a small or how large quantity is sold, price will remain constant.

Secondly, this approach does not consider the possibility of stock getting piled up or being held for a long time. Also, break-even analysis does not allow the inclusion of semi variable costs.

In a company that deals with multiple variation of products, the model assumes equal weightage for each product being produced & sold.

Lastly, fixed costs are not always constant regardless of the quantity. Rather, it could change depending on the level of activity.

Ans. to the Question No. 02

(a) Why managerial accounting is important despite preparing financial accounts

Management accounting's main goal is to generate valuable information for the internal use of a business. It helps business managers to gather knowledge that facilitates strategic planning, enables them to set ambitious targets, and ensure an effective management of company resources.

On the other hand, financial accounting also has some internal applications, but it has far more to do with informing those outside of a corporation. Final reports or financial statements produced by financial accounting are intended to reveal the economic results and financial health of the company. While managerial accounting is created for the management of a business, financial accounting is created for its investors; regulatory bodies or any other stakeholder.

While financial accounts paints a picture of the performance of a certain company as a whole, managerial accounting reveals information about a specific department/section performance. It can help to eliminate various types of wastages of company resources. It is also regularly used for planning and controlling activities. The management can set attainable goals by using the tools of management accounting.

The internal performance statistics is invaluable for checking the feasibility of a newly launched product. In some cases, underperforming product variant can be easily identified & corrective measures could be taken before its too late. Better information about the different cost of components enables the management to cut down cost wherever possible, which translates to a better service experience of the customer as they can avail the product at a lower cost.

Managerial accounting could be beneficial for the HR department as well. With the collected information they can realize whether or not the company can afford additional staffs. It can also help to decide which employee deserves a promotion based on their performance data.

(b) Techniques used by management accountant to achieve the objectives mentioned above

Managerial accountants tend to evaluate relevant incidents and organizational metrics to convert data into valuable knowledge that can be leveraged through their decision-making phase by the management of the business.

Some of the most popular techniques used by managerial accountant are discussed below:

First of all, margin analysis is a tool that helps identify incremental benefits of producing each additional unit. Breakeven point analysis falls under this category which is a crucial tool to optimize company's sales mix.

Secondly, product costing and inventory valuation techniques are utilized to properly measure the actual cost associated with different inventories. This helps to identify products that must be sold immediately for significant inventory cost reduction.

Management accountants also regularly use standard costing methods to identify deviation from ideal scenario. That means they can pinpoint the underlying reasons and take remedial actions so that it might not happen again. Revaluation tools ensures the management whether or not company's capital is properly maintained and preserved.

Through cash flow statement, management accountants identify the sources of cash flow & its destination while maintaining a proper liquidity position for the company. Through cash management they find ways how to defer payments for as long as possible without hampering the relationship.

Trend analysis, another important tool, allows the user to recognize patterns and trends among the historical data, so that future matrices could be estimated. It also separates unusual variances from data, so the user does not get misguided by an accidental change.

Lastly, through capital budgeting techniques such Net Present Value (NPV) and Internal Rate of Return (IRR), the project manager could easily choose the investments(s) that can generate highest value for the organization. This protects the firm from committing a large amount of fund for a very long time in a unworthy project.