



Prifysgol Cymru
Y Drindod Dewi Sant
University of Wales
Trinity Saint David

Kristina Kushlova

1909417

MANAGEMENT ACCOUNTING

Assignment 2

Report

Lecturer

Rexon Nting

Table of Contents

Introduction.....	3
Part A	3
Question one: Flexed budget and variances from actual budget	3
Question two: Performance report of Amana's in the year 2020 based on the above budget	5
Question three: Recommendations to Amna' CEO on areas of improvement	6
Part B	7
Question one: Deciding to sell products on Amazon or own online shop	7
Conclusion	10
References.....	11

Introduction

A budget is an important planning and control tool for every business. It estimates the organisation's revenues and expenses over a specified period which enable the firm to make essential business decisions (Shim, Siegel and Shim, 2011). A major decision that the firm manager needs to make is to determine whether to allow the budget to change throughout the reporting period. A budget that does not change is known as static while that one that changes with the course of the reporting time is known as a flexible budget. This report intended to shed light on flexible budget and the variances that arise from the original budget using Amana Ltd financial information as the case study. Besides, the report will analyse Amana's performance depending on the results of the budgets where various recommendations on areas of improvement shall be provided.

Part A

Question one: Flexed budget and variances from actual budget

According to Patty Graybeal (2019) a flexed budget changes with the changes in volume or the activities of the business. However, in the original /static budget amounts do not change even if any changes of output occur. A flexible budget is an essential tool for measuring managers' efficiency in the firm as it analyses and shows the variances from the estimated and actual values.

Below is Amana's original budget, flexed budget and variances for the year ending 2020

Table one: Amana Ltd Original Budget

units sold	100,000	
sales price	25	
sales		2,500,000
	per unit cost	
costs of goods sold		
direct material	2.5	250,000
direct labour	4	400,000
variable overheads	2	200,000

Fixed overheads

rent	200,000		
Insurance	100,000		
salary	50,000		
Total cost of goods sold		1,200,000	
Gross profit			1,300,000

Table two: Amana Ltd flexed budget

unit sold	80,000		
selling price	20		
sales	160,000	1,600,000	
Cost of goods			
direct material	280,000		
direct labour	440,000		
variable overheads	120,000		
Fixed overheads			
rent	170,000		
Insurance	100,000		
salary	35,000		
total cost of goods sold		1,145,000	
Gross profit			455,000

Table three: Variances in the two budgets (original and flexed budgets)

Amana Ltd Original Budget

	Original budget		Actual budget	Variances	favorable/unfavorable
units sold	100,000		80,000	20000	unfavorable
sales price	25		20	5	unfavourable
sales	2,500,000		1,600,000	900,000	unfavorable
	per unit cost				
costs of goods sold					
direct material	2.5	250,000	280,000	30,000	unfavorable
direct labour	4	400,000	440,000	40,000	unfavourable
variable overheads	2	200,000	120,000	80,000	favorable
Contribution margin	1,700,000		760,000	940,000	Unfavorable
Less; fixed overheads					
rent		200,000	170,000	30,000	favorable
Insurance		100,000	100,000	0	
salary		50,000	35,000	15,000	favorable
Total fixed costs		(350,000)	(305,000)	45,000	favorable
Gross profit	1,300,000		455,000	845,000	unfavorable

Question two: Performance report of Amana's in the year 2020 based on the above budget ii). As seen from the two budgets above there is a huge variance. Amana ltd had a bad year whereby the business faced major overruns starting from production to expenses. Both units produced and the selling price reduced from the original estimation which led to unfavourable variances as indicated in table three above. Besides, Amana's computed identified unfavourable variances in the direct material, and in the direct labour which increased the cost of sales. The static budget production estimates were to be 100,000 units for 25 however; in the actual budget only produced 80,000 units at 20 per unit which resulted in an unfavourable variance of 900,000 in total sales. The decreased production could be a result of the increased cost of production or due to inefficient production process and incompetent employees (Berger, 2011).

Even though Amna could have reduced their selling price by 5 to increase sales, this strategy is only successful in the short-run however, in the long run, the business may fall into huge financial

losses. According to Berger (2011) the business may enter into losses as the operating income will not be able to cover the cost of production in the business.

Moreover, from the budget, the cost of direct labour and material increased than the original estimates whereby material increased by 30,000 while direct labour increased by 40,000 leading to unfavourable variance which increased costs of goods sold. Only variable overheads had a favourable variance where they reduced by 80,000. The increase in labour and material could be economic market conditions such as inflation which causes prices of raw material and labour to raise (Patty Graybeal, 2019).

Fixed overheads had a much favourable variance as rent and salary reduced while insurance cost remained the same. The total flexible budget variance for fixed overheads is 45,000 favourable since the actual fixed overheads of 350,000 were less than the flexed budget of 305,000. However, due to increased costs of variable overheads and a decrease in the estimated production units along with a decreased selling price in the market Amana Ltd had a huge unfavourable variance in the total income/gross profit of 845,000.

Question three: Recommendations to Amna' CEO on areas of improvement
whether variances are favourable or unfavourable, budget variances need monitoring and being analysed if a business such as Amana wants accurate financial reporting. Besides analysing the variances will help the firm to have a reliable cash flow and for developing short and long term planning and spending strategies for the business (Bragg, 2013). Thus, after analysing Amna's budget variance the following suggestions can be used to monitor both favourable and unfavourable variances to ensure the business remains competitive and profitable.

Amna needs to conduct a price review and analysis in the market. As seen from the budget above in table one and two the company had used price reduction as their strategy to increase sales. However, a price reduction is not a sustainable strategy in the long run as increased sales will only be generated in the short run while in the long run, the business may be incurring huge losses as a result of this strategy. Thus, Amana should conduct market research, identify the price of their competitors which will help to charge their products using competitive based pricing (Berger, 2011). Besides, Amana can opt to increase the quality of their products by coming up with unique designs from their products then price them at a premium pricing strategy. Using such a strategy will help the business generate long term revenue and success.

Switching to a cheaper supplier- as noted in the budget raw material increased than the estimated costs thus increasing labour costs too. Thus, Amana should conduct a good market survey and identify suppliers who are cheaper and that have good track records. The firm should not rely on one supplier, they need to have several trustable suppliers where they can always switch to the cheaper one. This will help the business to avoid running into high variable costs which increase the cost of goods sold (Bragg, 2013). Besides, switching to a cheaper supplier will not only save on production costs but also will help the firm to purchase in bulk and make sustainable profits.

Process improvement- after analysing on price and locating a cheaper supplier, Amana requires to ensure their production processes and systems are effective and operating efficiently. This can be done by ensuring the production team is well trained on the latest designs and modelling of Souvenirs. Besides, the firm can ensure all equipment and tools used in the production of goods sold are operating well to maximise quality (Bragg, 2013). If Amana can produce high-quality products, the probability of customer retention and loyalty also goes high which promotes repeat purchase and continuity of increased revenue generation in the firm.

Include advertising expenses- from the budget, it's evidence that Amana has not set aside cash for advertising its offering into the market. An advertising budget is part of the firm's overall sales and marketing efforts (Shim et al., 2011). Each pound spent on advertising should be seen as an investment in growing Amana. Through advertising, Amna can successfully reach out to a large number of tourists who are their main customers. Creating brand awareness is very important as in the end it generates an increased customer base, market share, increased sales and brand equity. Hence, it recommended for Amna to consider allocating cash for advertising activities to increase its brand awareness and sales.

Part B

Question one: Deciding to sell products on Amazon or own online shop

In considerations of the costs factors and revenue estimates projected for Amana in making decisions between selling their products either through their online shop or sell the product through Amazon. It would be favourable for the company to sell its products through Amazon. The reason to choose to sell its offerings through Amazon is due to the following factors;

Benefits of using Amazon shop to sell the company products

Easier to avoid relevant costs- the costs of setting up a delivery network if Amana was to sell through its online shop is very high. Besides, the firm will be forced to further incur costs of upgrading their current websites to handle a large volume of sales and also pay salary for a full-time IT programmer. These relevant costs are very high which can be avoided by Amana if they buy the idea of selling their products via Amazon. Moreover, comparing to the sale estimated to be generated annually through the online shop is 100,000 units with no guarantee whether the business will perform well or not. On the other hand, by choosing Amazon as their online site for selling their products Amana, is guaranteed a sale of 65,000 units annually with a high potential to increase with the increase in demand.

High customer reach and acquisition- Amazon Amana will have a great and easier customer reach on both international and local levels. Amazon being the world's largest e-commerce platform the probability of reaching many shoppers in particular the tourists is very high. Unlike a new online shop that is establishing itself, Amazon features more than 300 million user accounts thus, Amana will have high chances of gaining a larger market share and increased sales in its targeted markets such as the US, UK and Europe at large (Berry, 2020). Besides, there is a high chance of customer acquisition. Through Amazon, and Amana being new in the online store will have a great advantage to attract new and unique customers. The likelihood of creating brand awareness in almost an entire world in Amana is increased.

Convenience- Amazon is more recommendable than starting its online shop as it is very convenient compared to selling products through Amana own website. This is particularly when it comes to maintenance and management costs associated with running an e-commerce site (Berry, 2020). Thus, Amana will minimise production costs that could be incurred to manage and maintain its website where the money can be used to improve the quality of the product. Amana will only be required to pay the Amazon fulfilment fees of 50,000 which is relatively cheaper compared to the costs of starting its online stores.

Limitations of using Amazon shop to sell the company products

However, selling in Amazon does not only comes with benefits but also have few limitations for a new business that wish to sell their products on this eCommerce platform. The following are some of the cons that Amana should be prepared for when deciding to trade its products in Amazon;

Increased competition- there will be stiff competition between Amana souvenirs and other sellers on the platform. There are thousands of seller selling the same products where most will sell at a cheaper price thus Amana may fail to meet its sales targets in the end (Bain, 2021). Besides, Amazon also sells its product in their products thus as a direct competitor it becomes difficult to compete in this market and effective marketing and advertising strategy is required. Therefore, Amana will need to develop an effective advertising strategy to increase its brand awareness to online shoppers across various online platforms. Hence, it will require Amana to conduct good market research on competitor's price and identify the effective pricing strategy for its products depending on the market factors.

There is a charged fee. Although Amana has a high chance to expand in terms of revenue while selling at Amazon, there is a cost to be incurred. Amana is required to pay Amazon fulfilment fees of 50,000. The subscription fees paid to Amazon will naturally grow as the company Amana gets bigger and continue collecting more revenue which will a reduction of generated revenues if the company had opened its online shop (Dowsett and Fares, 2019).

Less control since this a rented platform- Moreover, Amazon is a rented platform which means that Amana will rent the site for selling online. Thus, by renting and not owning Amana will have less control over the business presence on the website. Thus, if Amana objective was to increase its presence on the online platform its will then become difficult to achieve such an objective with a rented website (Berry, 2020).

Final decision

However, Amana should settle with the decision of selling its products through Amazon platforms as the benefits of using the eCommerce platform are more than the disadvantages. The disadvantage includes stiff competition from both Amazon and other competitors. The other challenge includes lack of control on how frequent to display its products on the site as well as incurring some fee charge. Cost and competition will also be incurred if Amana decided to sell its product through its online shop. Thus, it will be better to choose Amazon a renowned eCommerce platform where customer reach and acquisition is easier and faster.

Conclusion

To sum up, this report has demonstrated and analysed how budgets are useful in planning and making complex business decisions. The report has calculated variances using the original and flexed budget and suggested various areas of improvement to reduce huge variances in a business. Also discussed in the report is how relevant costs can be avoided while making business decisions by eliminating unnecessary data that could complicate the whole process of decision making.

References

- Bain. M. (2021). The pros and cons of putting your small business on Amazon [Online]
Available at: <https://qz.com/1957408/the-pros-and-cons-of-putting-your-small-business-on-amazon/> [Accessed on 3rd May, 2021].
- Berger, A. (2011). *Standard Costing, Variance Analysis and Decision-Making*. GRIN Verlag.
- Berry. S. (2020). Should You Sell on Amazon or Your Own Website? [Online] Available at:
<https://www.webfx.com/blog/marketing/sell-on-amazon-or-own-website/#:~:text=For%20many%20companies%2C%20Amazon%20is,about%20web%20hosting%20or%20redesigns.> [Accessed on 3rd May, 2021].
- Bragg, S.M. (2013). *Accounting best practices*. John Wiley & Sons.
- Dowsett. S. and Fares. M. (2019). Selling with the enemy: Why rival retailers embrace Amazon.com [Online] Available at: <https://www.reuters.com/article/us-amazon-com-brands-apparel-idUSKCN1RL0E7> [Accessed on 3rd May, 2021].
- Patty Graybeal, M.F. (2019). Principles of Accounting, Volume 2: Managerial Accounting. *MF Patty Graybeal, Principles of Accounting, 2.*
- Shim, J.K., Siegel, J.G. and Shim, A.I. (2011). *Budgeting basics and beyond* (Vol. 574). John Wiley & Sons.