MANAGEMENT ACCOUNTING

POWER PRESENTATION

PRESENTED BY: PROF. (DR.) JAI KUMAR SHARMA

MAHARAJA AGRASEN SCHOOL OF MANAGEMENT

INTRODUCTION

MEANING AND DEFINITION

“Management accounting is concerned with accounting information that is useful to management”. J.Batty defines “ Management accounting is the term used to describe the accounting methods, systems and techniques which, coupled with special knowledge and ability, assist management in its task of maximizing the profits or minimizing losses”. “Management accounting is the presentation of accounting information in such as way as to assit management in the creation and in the day-to-day operations of an undertaking” - I.C.M.A. Institute of Costs and Management Accountants.

According to H.M. Treasury, Management Accounting is “the application of accounting knowledge to the purpose of producing and of interpreting accounting and statistical information designed to assist management in its functions of promoting maximum efficiency and in formulating and co-ordinating future plans and subsequently in measuring their execution”.

NATURE OF MANAGEMENT ACCOUNTING

- Though Management Accounting is the latest branch in the accounting arena, it may be regarded partly as a Science and partly as an Art. It is the science of 'Quantifying and summarizing' and Art of 'Interpreting' accounting data. Management Accounts derives its conclusions through collection, processing and objective analysis of data Quantified in figures. Thus it depends upon "Objectification and Quantification of progress and problems". From this point of view Management accounting may be regarded as a Science. However, Management Accounting also involves human judgement, impulses, whims and prejudices as evidenced in interpretation of data, deductions and conclusions drawn from analysis.

SCOPE OF MANAGEMENTACCOUNTING

1. Financial Accounting
2. Cost Accounting
3. Budgeting and Forecasting
4. Statistical Methods
5. Inventory control
6. Interpretation of Data
7. Internal Audit
8. Tax Accounting
9. Methods and Procedures
10. Office Services

FUNCTIONS OF MANAGEMENT ACCOUNTING

- Helps in Planning and Policy formulation
- Helps in the interpretation process
- Helps in Decision-making
- Helps in Controlling performance
- Helps in Coordination operations
- Helps in organizing
- Helps in Expansion, Diversification and Strategic business problems
- Helps in Communication of Management policies
- Helps in Motivating employees
- Helps in Reporting

FINANCIAL STATEMENT

Financial Statements are the collective name given to Income Statement and Positional Statement of an enterprise which show the financial position of business concern in an organized manner. We know that all business transactions are first recorded in the books of original entries and thereafter posted to relevant ledger accounts. For checking the arithmetical accuracy of books of accounts, a Trial Balance is prepared. Trial balance is a statement prepared as a first step before preparing financial statements of an enterprise which record all debit balances in the debit column and all credit balances in credit column. To find out the profit earned or loss sustained by the firm during a given period of time and its financial position at a given point of time is one of the purposes of accounting. For achieving this objective, financial statements are prepared by the business enterprise, which include income statement and positional statement.

BASIC FINANCIAL SATATE MENT

These two basic financial statements viz:

(i) Income Statement, i.e., Trading and Profit & Loss Account and
(ii) Positional Statement, i.e., Balance Sheet portrays the operational efficiency and solvency of any business enterprise. The income statement shows the net result of the business operations during an accounting period and positional statement, a statement of assets and liabilities, shows the final position of the business enterprise on a particular date and time. So, we can also say that the last step of the accounting cycle is the preparation of financial statements.

Income statement is another term used for Trading and Profit & Loss Account. It determines the profit earned or loss sustained by the business enterprise during a period of time. In large business 3 organization, usually one account i.e., Trading and Profit & Loss Account is prepared for knowing gross profit, operating profit and net profit.

OBJECTIVES OF FINANCIAL STATEMENT ANALYSIS

1) To interpret the profitability and efficiency of various business activities with the help of income statement.
2) To aid in important decision making investment and financial decision.
3) To gauge the financial position and financial performance of the concern.
4) To identify areas of mismanagement and potential danger.
5) To ascertain the investment pattern of the resources.
6) To ascertain the maintenance of financial leverage.
7) To determine the pattern of movement of inventory.

TOOLS OR TECHNIQUES OF FINANCIAL STATEMENT ANALYSIS

- Comparative financial statement
- Common size financial statement
- Trend analysis
- Ratio analysis
- Funds flow statement
- Cash flow statement

RATIO ANALYSIS

Analysis and interpretation of financial statements with the help of ratios is termed as Ratio analysis. It involves the process of computing, determining and presenting the relationship of items or groups of items of financial statements.

A ‘ratio’ is a mathematical relationship between two items expressed in quantitative form. Ratios can be defined as “Relationships expressed in quantitative terms, between figures which have cause and effect relationships or which are connected with each other in some, manner or the other”.
“The analysis of financial statement data is an attempt to determine the significance and meaning of the financial statement data so that the forecast may be made of the future prospects for earnings, ability to pay interest and debt (both shot and long term) and profitability”.

ADVANTAGES/BENEFITS OF RATIOS ANALYSIS

- Forecasting
- Managerial Control
- Facilitates Communication
- Measuring Efficiency
- Facilitating investment decisions
- Useful to measure financial solvency
- Inter firm Comparisons

CLASSIFICATIONS OF RATIOS

Under this classification, ratios are grouped as follows:
 Profitability Ratios: *These ratios are intended to measure the end result of business operations. Examples: Gross profit ratio, Return on capital employed and operating ratio.*

 Turnover or activity ratios: These ratios enable measurement of the effectiveness of the usage of resources at the command of the concern. Examples: Fixed assets Turnover ratio, Stock turnover ratio. These ratios would also indicate the profitability position of the business

 Solvency ratios:
 Liquidity ratios - These ratios are used to measure the abilities of the firm to meet its maturing obligations or current liabilities examples: Current ratio, Acid test ratio. Leverage ratios - These ratios help to measure the financial contribution of the owners compared to that of creditors as also the risk of debt financing. They are also known as capital structure ratios. Example: Debt to Equity ratio, fixed assets to Net worth, Inter coverage ratio.

CASH FLOW STATEMENT

Under cash flow analysis, all movements of cash, rather than the inflow and outflow of working capital would be considered. In other words, cash flow analysis, focuses attention on cash instead of working capital. When the movements of cash (i.e., cash inflow and cash outflow) is depicted in a statement, it is called Cash Flow Statement. Thus, a cash flow statement summarizes the causes of changes in cash position of a business between two balance sheet dates. The flow of cash may be inflow or outflow. When cash inflows are more than the cash outflows, there would be an increase in cash balance. On the other hand, if cash outflows are more than the cash inflows, there would be decrease in cash balance. The term cash includes both cash and bank balances.

SOURCES AND USES OF CASH

The change in the cash position is computed by considering 'Sources' and 'Applications' of cash which are as follows:

Sources of cash

The sources of cash includes:

1) Cash from Operations
2) Issue of Shares
3) Issue of Debentures
4) Long term Loans Raised
5) Sale of Fixed Assets

Application (uses) of cash

Application of cash includes the following: 1) Redemption of Preference Shares

2) Redemption of Debentures
3) Repayment of Loans
4) Purchase of Fixed Assets
5) Payment of Dividends
6) Payment of Taxes

NEED FOR CASH FLOW STATEMENT

The primary objective of the statement of cash flows is to provide information about an entity's cash receipts and cash payments during a period. The net effect of cash flow is provided under different heads namely cash flow from operating, investing and financing activities. It helps users to find answers to the following important questions: a) Where did the cash come from during the period? b) What was the cash used for during the period? c) What was the change in the cash balance during the period?

THANK YOU