Budget

Business

A budget is a plan that comprises a number of values such as net profit, production costs, production volume in conjunction to other factors that incorporates the specific period under which a performance is evaluated.

It is divided into static and flexible budgets; a static budget is constant while the volume changes while the flexible budget adjusts line values in relation to the level of activity. The static budget projects a specified level of output, input, and the net income prior to the budgeting period although the values estimated may vary in relation to the final result. The flexible, dynamic budget, takes into consideration the fact that the variable production costs and per-unit fixed change based on the output level. The flexible is useful for the businesses that operate in a volatile area or a business environment that is uncertain. The static budget variances are the discrepancies that result from the initial budgeting errors or fluctuating costs of the raw materials. They are included at the end of budgeting to ensure a balanced financial report.

In flexible budgeting the variants are part of the actual budget since the final drafting takes place at the end. The core reason behind price variance for direct material is as a result of fear of spending money on quality material but rather choosing very cheap material of lower quality thus, this will result into an equivalent inferior product due to the lower or inferior quality of the materials used. This can therefore lead to high chances of a higher rate of waste and spoilage. Unfavorable efficiency variance for direct manufacturing labor is always caused by unskilled or semi-skilled person performing duties that are totally beyond their knowledge or what they have learned. Ideally, the duty of a semi-skilled worker is mainly to deal with relatively narrow jobs.

Raw materials which are used during manufacturing also matters a lot; in this case the inferiority of the raw materials used is another reason. Timing or scheduling of the entire process of manufacturing plays a vital part however the poor process of scheduling during the manufacturing process is another big reason Generally, there are two reasons why the flexible budget variable in their cost. Basically, there is a difference between the budgeted inputs and the real input prices for instance a company can pay more on a certain material than it was earlier anticipated, on the other hand the same company can also pay less than it was earlier budgeted or rather planed. The second instance is when the same company bought the budgeted material but it ended up using more material while manufacturing a certain product therefore interfering with the previous budget basically the company can also use lesser material on its products than expected. On the other hand direct labor is drastically affected by the sum price due to the setting of the standard cost. Cost standards works on the basis of identification of how much each input should cost, therefore the real cost are always compared to the standards.

Direct cost in standard costing plays a very vital role in the decision made by the managers especially in the efficiency rate of the workers and the productivity of the workers on the other hand most companies note reasons for variances, they make concrete conclusions and take actions accordingly. On the other hand management work hand in hand with the accountants in determining a good reason for the occurrence of the variance and therefore they come up with a final decision of either taking another action or not.