

Big company with a  
large amount of  
inventories marketing  
essay



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Nestlé (Malaysia) Berhad started in Malaysia in 1912 and was listed on Bursa Kuala Lumpur on 13 December 1989. The company manufactures a wide range of products including instant beverages, milk product, ice cream, cereals, chilled products and many more. Meanwhile, Nestlé (Malaysia) Berhad has a lot of brand names. For instance, MILO®, NESPRAY®, NESCAFÉ®, MAGGI® and KIT KAT® (Nestlé Berhad, n. d.). Like other trading and manufacturing company, Nestlé (Malaysia) Berhad purchases raw materials as the input for production of final goods. It is then to be sold to the customers with the intention of earning profits. The valuation of inventories used by Nestlé (Malaysia) Berhad is first-in first-out (FIFO) method. Since it is a big company with a large amount of inventories, it has been proved that a ‘good control over inventory must be maintained’ (Reeve, Warren and Duchac, 2007, p. 308). A little mistake made will have a significant impact on the financial statements.

## **2. CONTENTS**

### **2. 1 Types of Inventories**

Nestlé (Malaysia) Berhad manufactures various types of products and has several categories of inventories. It includes raw and packaging materials, work-in-progress, finished goods and spare parts (Nestle (Malaysia) Berhad, 2012).

Finished goods

Work-in-progress

Raw materials

Nescafe

Milo

Smarties

Kit Kat

Haagen-Dazs

Nestea

Roasted coffee beans

Chocolate crumbs

Skim milk powder

Cocoa paste

Sugar

Coffee beans

Vanilla

Palm oil

Salt

Milk

## 2. 2 Process of Manufacturing the Goods

Nestlé (Malaysia) Berhad produces many types of goods to be sold to the customers. The process of manufacturing the goods is from raw materials to finished goods. One of the examples of process of manufacturing the goods is from 'cherries' to NESCAFE.

NESCAFE (coffee)

Grinded coffee beans

Roasted coffee beans

'Cherries'

Coffee beans

The first process of manufacturing the Nestle NESCAFE is harvesting the fruit of the coffee beans. The coffee trees have a fruit that are called 'cherries' and it contains two coffee beans in each cherry. The great taste of NESCAFE is born from these beans.

The second process of manufacturing the Nestle NESCAFE is drying the coffee beans. The coffee beans need to be separated from the skin, pulpa and parchment to get at the coffee beans inside each cherry. The cherries are dried under the sun or by soaking the cherries in the hot water to achieve the coffee beans.

The third process of manufacturing the Nestle NESCAFE is roasting the coffee beans. The beans need to be roasted to release the aroma and taste we know as coffee after the green coffee beans have been selected.

The fourth process of manufacturing the Nestle NESCAFE is grinding. The beans are ready for grinding after roasting. The brewing method and equipment used can determine the particle size of the grind; whether coarse or medium, fine or very fine.

Lastly, the process of manufacturing the Nestle NESCAFE is processing. The ground coffee put into an industrial percolator containing hot water under pressure that brew a highly concentrated liquid coffee that called coffee liquor to make NESCAFE Pure Soluble Coffee (Nescafe, n. d.).

## **2.3 Valuation of Inventories Used by the Company**

Inventories are valued by comparing between the cost and net realisable value (NRV). The lower value one will be the amount of closing inventories. This is based on the Lower Cost Method (LCM) rule which is the lower of cost and market value (WebFinance, 2012).

There are two types of methods commonly used by most of the companies to calculate cost of inventories:

First-in first out (FIFO)

Weighted Average COST (WAC)

The NESTLE company uses the first-in first-out (FIFO) method to evaluate their company's inventories. This is because it is simple to understand and

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easy to operate. The FIFO method means that whichever goods that are purchased first will be sold first to the customers. In another words, the oldest goods will be sold first. Hence, the goods most recently purchased are the closing inventories at the end of the year and made up of most recent costs (Murray, 2012).

By using FIFO method, the closing inventories consist of most recent purchase prices which show the current market price. For big company like NESTLE Berhad, this method enable the company to have fewer amount of obsolete inventories. However, this method may lead to errors if the prices fluctuate frequently. The cost of sales will also be understated during inflation and causes profit to be overstated. This contradicts with prudence concept where the profits and assets should not be overstated while losses and liabilities should not be understated (Rabi Gupta, 2012).

### **2.3 Valuation of Inventories Used by the Company (cont'd)**

Based on the Nestle (Malaysia) Berhad Financial Report 2011 (2012, p. 34), the value of raw and packaging materials in 2011 is RM 219, 608, 000.

Meanwhile, the value of work-in-progress inventories is RM 21, 139, 000. The finished goods are worth RM 258, 968, 000 and the spare parts are worth RM 517, 573, 000. The financial report shows that the value of inventories has increased in 2011 compared to 2010. In 2010, the value of raw and packaging materials is RM 144, 263, 000 while the work-in-progress inventories are RM 16, 558, 000. The finished goods are worth RM 202, 828, 000. Meanwhile, the spare parts are worth RM 380, 539, 000.

## **2. 4 Amount of Closing Inventories as Reported in the Financial Statement**

In group, the amount of closing inventories as reported in the Nestle (Malaysia) Berhad Financial Report 2011 (2012, p. 10) is RM 517, 573, 000 in year 2011 and RM 380, 539, 000 in year 2010. This shows an increase in the value of inventories in year 2011 compared to year 2010. The financial statements are attached in the appendix on page 13 to 16.

## **2. 5 Definition of Relevant Information Relating to Inventories**

### **i) Inventories**

The merchandise, raw materials and processed and unprocessed product of a company which are still remain unsold. Inventory is considered an important asset that is owned by a company for generating revenue. In another word, inventory is called liquid assets. The accuracy of the inventory counting is very important so that the company's profit and loss can be determined accurately (Investopedia, 2012).

### **ii) First-in First-out (FIFO)**

FIFO is the short form of First-in First-out. FIFO can be assumed as a processing and retrieving data method. The way that a FIFO system works is the first units out, is the first units in or purchased. In another word, the first units sold are assumed to come from the beginning inventory. So, the inventories will always have the latest purchased goods. The first-in first-out method also functions to value inventory under purpose of taxation. Hence, inventories will value at the latest cost (Murray, 2012).

### iii) Weighted Average Cost (WAC)

When weighted average cost (WAC) method is used, the average unit cost for each type of item is calculated each time a purchase is made. It is then used to determine the cost of each sale. When another purchase is made, a new average unit cost is calculated (Investopedia, 2012).

### iv) Cost of Inventories

Cost is the historical cost. It is the original purchase price that is calculated either using the First-in First-out method or the Weighted Average Cost (WAC) method. Based on the Accounting Standard (AS) 2 Valuation of Inventories (n. d., p. 10), cost of purchase, cost of conversion and other cost incurred in bringing the inventories to their present place and condition are all included in the cost of inventories.

### v) Net Realisable Value (NRV)

According to the Accounting Standard (AS) 2 Valuation of Inventories (n. d., p. 10), Net Realisable Value (NRV) is the value after the selling price or the market value minus any other expenses used to sell the goods such as transportation and insurance.

## **3. CONCLUSION**

In the process of completing this assignment, we have learned that accounting for inventory is a very important topic especially for us who study accounting. We gain a lot of experiences and know the importance of teamwork in finishing a task before the deadline. As accounting students,



this research teaches us that a trading business must record, retain, and report information about the purchases and sales of its goods. Apart from that, it is very important that the valuation of inventory is accurate to ensure that the profit or loss calculated in the financial statements is accurate too. This understanding will help us in our work in the future.