Management Accounting

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Lecture 24

Flexible Budget & Variance Analysis-I

Welcome students. So, we are in the process of learning about the budgets and budgetary control and in the previous classes, we have discussed in detail, that what is budget, and largely we talked about the master budget. We discussed the master budget conceptually, and then we learned, that how to prepare the master budget, where we did the, say two cases in detail.

And, we try to understand by, say preparing the budgets for the two companies, where we discussed in detail, the concept of the master budget, and I already have told you, that it has two components, operating budget and the financial budget. And, finally we prepare the budget and income statement and the budget and the balance sheet, right. Now, we will move to the next part.

I told you, in the previous class also, that though we have seen it in detail, that the master budget is a very, very important tool for the management decision making, for the cost control, for improving the performance of the company, in all areas, units and sub-units. But, still it has some limitations. So, we have to understand those limitations.

We have to highlight those limitations, and then try to find out what is the solution for those limitations, right. So, the solution to the limitations of the master budget is the-flexible budget and variance analysis, right. So, we will be going ahead today, with the say, detailed discussion on flexible budgets. So, why we need the flexible budgets because of the limitations of the master budget?

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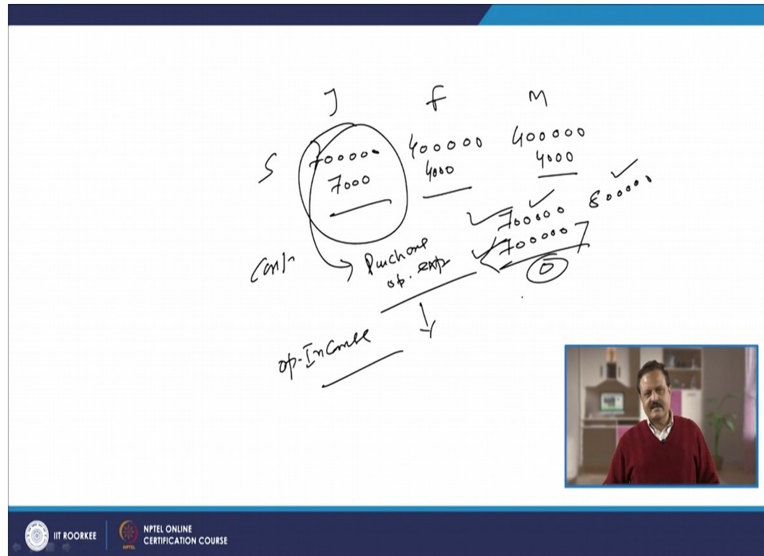

So, in the master budget, for example, what we did, say we were preparing the budgets, and we were given the sales level, we have already forecasted the level of sales and, if you talk about the value of the sales, sometimes we were writing that, say for example, in the three months, we have the sales of say, 7 lakh rupees or dollars, or maybe 4 lakhs, or maybe something like that, for the different months, we were talking about.

So, these are the three months, and we are talking about 7 lakhs, 4 lakhs, 4 lakhs, you can say that, in the month of January, we are anticipating this, in month of February we are anticipating this, and in the month of March we are anticipating this much amount of sales. So, you can convert that, say the number of sales into units also.

Say, for example, here we were planning to manufacture and sell 7 thousand units, here it is 4 thousand units, and then it is, again 4 thousand units. So, the cost or the selling price of one unit be 100, so, we had the total estimation of the sales, to the tune of 700 thousands in the month of January, 400 thousand in the month of February and 400 thousands in the month of March, right.

Now, then we prepare the budget for all this, starting with the sales here and then we subtracted all the cost; means while we were preparing the income statement, budgetary income statement, we took the sales at the top and then we subtracted all cost, and then

we try to find out the operating income, operating income and, at the same time, we anticipated the level of sales, at 7 lakhs, worth of rupees or dollars or whatever it is.

We then found out, that for this much level of production, sales, we have to go for the production and then we anticipated in term of, the purchase expenses. Then, for the operating expenses, and all other things, and finally we went up to the finding out the total, requirement of the cash and other things. But, now you see, the major limitation of this budgets, static budget, the master budget is the, other name of the master budget is the static budget.

So, major limitation of this budget is, that you are anticipating only, one level of production and the performance; only one level of production and performance. That is, sometimes, it can prove to be dangerous, that we are anticipating, that in the month of January, we will sell, in the market, our sales forecasted sales will be how much, 700 thousands rupees or dollars. But, how it is sure? Because, you are talking here, which, something is going to happen in future.

We are only anticipating, we are only planning at this level. Actual performance, will it be actually, 7 lakh rupees? It can be 6 lakh 50 thousands worth of rupees or dollars sales. It can be 7 lakh 50 thousands; it can be 8 lakh rupees, of dollars and sales. So, the moment the amount of sales changes, right, your all other estimates will also change. Your cost will also change in the same proportion, because the total cost of the production is into two parts.

One is the variable cost and second is the fixed cost. So, variable cost, all the time changes, with the level of production and sales. Maybe, the fixed cost remains the same, but to a limited level of production. What if, for example, you had anticipated that our sales in the month of January will be 7 lakh, you, worth of rupees? And, the fix expensive for that will be, some amount say X. But, actually our sales went up to, say increased by 1 lakh rupees more, so, maybe it is possible that the fixed expenses are going to remain fixed up to 7.5 lakhs.

But, if the sales increased beyond that, our fix expensive will also increase. So, in that case, what is happening? You have the budget, only for the one level of production and the sales, maybe the overall performance. But here the, now the actual performance has changed. It can be 6 lakh, worth of rupees; it can be 8 lakh worth of rupees. So, there is a plus minus 1 lakh rupees. Now, how would you use this budget, or this, say budgetary information, which we are prepared here, for exercising the control?

Because, control is possible only, analysis of the variance, only possible, if you plan for 7 lakh, and actual is also 7 lakhs. Then, you can say that my sales were 7 lakh worth of rupees. Actually, we have sold for 7 lakh rupees in the market. So, it means, at the sales level, there is no variance. Now, let us check at the cost of production. Is there any variance? Maybe, what is anticipated is the cost, of production, for selling worth rupees 7 lakhs, have we been able to achieve that level?

Or, the cost was more than budgeted? Or cost was less than budgeted? If, it was more; why it has increased? It was less, then why it has come down? So, that variance analysis, we will be doing but, for example, if the sales level has become now 8, 8 lakhs and, your budget is for 7 lakhs. You are going to compare something that, the budget is for lesser level of production and sales, and actual performance is gone up by 1 lakh, is a very significant amount.

So, how can you compare these figures of the expenses, which were expected to be there for the 7 lakh worth of rupees or dollars of the sales? It means, if you compare that level that, simply your variances are going to be positive; that you are comparing the cost for 7 lakhs, against the performance of 8 lakhs. So, you say that our anticipated cost for the material was this.

Actually, we have, means incurred the less cost, so our profit is increased. So, that is not the way of analysis. We have to have multiple level of budgeting. We cannot have only one level of budgeting, master budget or static budget. You cannot be sure 100 percent that we are planning for a given level of performance and actually also will also be the same level of performance. That is not expected to happen.

So, if that performs changes maybe, it goes up it, comes down or at least it is not the same, what we had planned for, what we had budgeted for, if that happens, then what is going to be the, say use of the budgets? Because, now at that time, when the actual performance will come; when the actual performance will come, for example, actually it is 8 lakhs or 6 lakhs. You have the budget for 7 lakhs.

So, at that time, first you have to prepare the budget for the 6 lakhs or the 8 lakhs, and then you start, the comparing, both the performances. What was the budgeted performance at 6 lakhs? What is actual performance at 6 lakhs? And then, is there any kind of the variance or not? So, it means, whatever the budgeted, budgetary exercise you did, at the level of 7 lakh units, or 7 lakh worth of sales, that is totally useless.

Means, again, you have to prepare the budget. A fresh budget, you have to prepare, equal to the actual performance. Again, you have to back track, that this is my now, the actual performance, 8 lakhs worth of sales. Now, my budget is for 7 lakhs. Now, I have to now, again prepare the budget for 8 lakhs and then, I have to see that for 8 lakh, worth of rupees or dollars of the sales, what was the variable cost expected?

What was the fixed cost expected? How much actually the fixed and variable costs have been? And, what is the level of profits? So, it means the level of, see, the budgeting which we did, the detailed budget. You see, how complex is the budgeting process. We have seen, in case of the static budget you start with the first schedule and in this the small cases, which we discussed, it was only for 3 months period of time, one quarter. The firm was very small, their operations are very small.

But, you talk about the companies, which are multinationals, whose operations are spread all over the world, on the different markets. Even if they have to prepare the budgets for their Indian subsidiary, or the company which is the subsidiary of that multinational operating in India and they prepare the budget for a given level of sales, production and performance and the actual becomes different. So, again preparing the budget for the different levels of, means equal to the actual performance, how complex it is.

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Static Budgets

- *Static budget* is really just another name for master budget.
- A master budget is prepared for only one level of a given type of activity.

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So, what we do is, we do not keep our self limited to the static budget or the master budget. Rather, we take the help of flexible budgets. We take the help of flexible budgets. So, in case of the flexible budgeting, now we are going to discuss today in detail flexible budgets and the variance analysis and in this flexible budget and variance analysis, first we will discuss the limitations of the static budget and then we will try to find the answer, that how the flexible budgets can do away the limitations of the static budgets.

And then finally, after conceptually being very clear about the flexible budgets, their uses, advantages and superiority over the static budget, we will go for preparing the flexible budget or learning about the preparation of the flexible budget, in detail and then means, a mini case we will do, in this case also. And then, we will clarify all the doubts, that if we have to replace the static budget with the flexible budget.

How we will go for the flexible budget? And how the flexible budget can be useful in exercising the management control, financial control, operating control and how it facilitates the, means in a better way, the overall management decision making, right? So, if you look at this, static budget is, it is clearly written here- is really just another name of the master budget. Static means, only one level of production, which is stable, one level of production- 7 lakh worth of sales, 7 thousand units; only one level.

But actually, you are not sure about and it never become sure, even if we plan for anything, means is daily. You are a student and if you maybe planning, that today, say for the whole day, I will be studying for 3 hours. But, in the evening you will find out, either you have studied for the four hours or you have studied for one hour.

So, it means in our daily, say planning process, at the personal level, if we deviate from the budgeted or the, maybe the planned performance, in the real form of the business organizations, deviations from the anticipated or the budgeted performances, all the times anticipated, you cannot ignore it and if it happens then the entire budgetary exercise should not become futile.

So, for that we would have to go for the flexible budget. Another thing is, the master budget is prepared for only one level of, a given type of activity. This is the major limitation. I just discussed with you, that this is only for the one level of the production, one level of the activity and when actual is different, then it has, means hardly any use.

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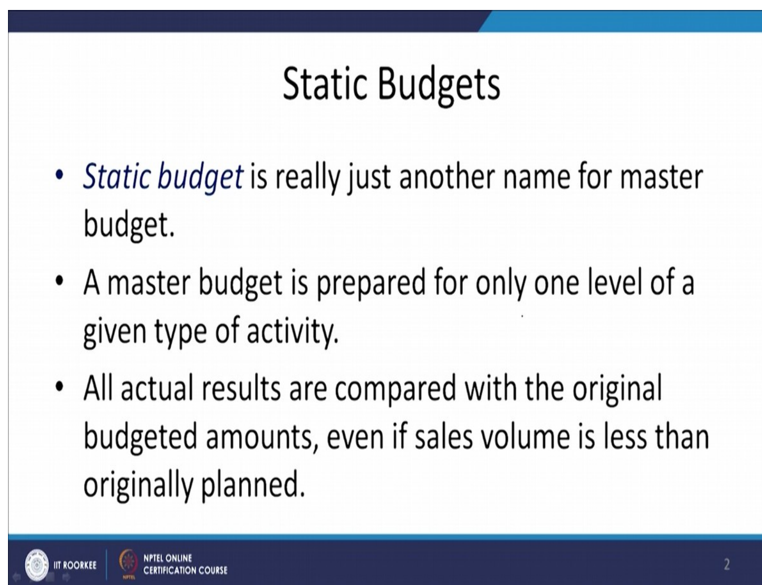

All actual results are compared with the original budgeted amounts, even if sales volume is less than originally planned. I told you that, you plan for 7 lakh and actual performance is 8 lakhs, and if you start comparing, the performance of the 8 lakhs worth of the sales, with the 7 lakhs of the budget estimates, certainly means the, the variances are going to

be there. Largely, it maybe possible, the variances are positive. So, there is no more reason for us to feel happy, that we had planned for 7 lakh units; we have performed it like units or maybe the 8 lakh worth of rupees or dollars of the sales.

So, proportionately now, if we go for the expenses; so, you can say, the sales variance is positive but the expensive variances, will come, become negative, because the raw material requirement for the 7 lakh worth of the sales was less. It has gone up, at the level of the 8 lakh rupees or dollars worth of sales, so the variance will be negative. But ultimately, we are not going to achieve any objective. It is the only the wastage of resources, time and money; so, major limitation of the static budget.

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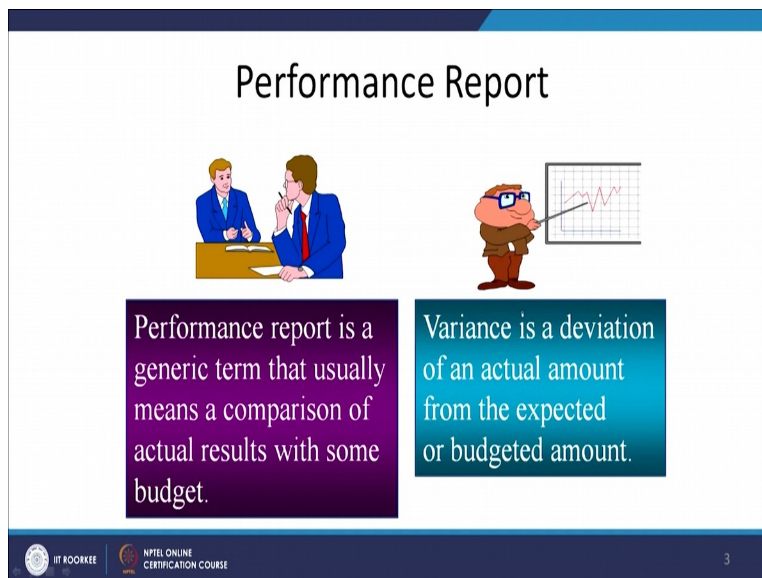

And, on the basis of that, means whatever the information is available with us, we prepare the performance report. And, performance report basically, is a generic term that usually means a comparison of the actual results with some budgets. So, that comparison will be feasible only, if you have the same level, of both the performances, budgeted performance in same with actual; actual is with the budgeted. Then, you can go for, that yes, I plan to sell for 7 lakh rupees, I sold for 7 lakh rupees.

Now, what should have been the cost, at the 7 lakh rupees worth of sales? What actually is the cost at the 7 lakh worth of rupees sales? Is there any kind of the variance; because,

variance is the deviation, of an actual amount from the expected or budgeted amount. It can be both, positive and negative. The cost, maybe the raw material cost ,we anticipated that, for the sales of 7 lakh rupees, will be, say having the raw material cost is, say 3 lakh rupees. But actually, the raw material cost is come down to 2.5 lakh rupees. So, it is a positive variance.

We have to look for that, that how we have been able, to reduce the cost of material at the same level of sales and production, by 50 thousand rupees. So, we have to anticipate it. Now, there can be two reasons, one thing is that variances can be positive, variances can be negative, when anticipated cost at the 7 lakh dollars or rupees of the sales, the anticipated cost of the raw material was 3 lakh rupees.

Actually, we had been able to; we have been able to, buy the raw material or complete the raw material cost, only pay or by paying only 2.5 lakhs. It means we have saved 50 thousand rupees. Why that now the positive variance of 50 thousands has come? There can be two reasons, either your purchase department is very, very efficient. They have found out the material, from some best supplier. It was a good quality material.

So maybe, when we have purchased a good quality material, wastages have been reduced seriously and the actual output, of per unit of the input has gone up. So, the total requirement of the material has automatically got down, right. Or, another reason could be, that actually what we planned, at the level of budgeting or at the time of budgeting, we plan for 3 lakh worth of the material.

But, that was wrong planning, that was a wrong estimation and actually the, the correct estimation should have been 2.5 lakhs. So, if the first thing is there that because of the extra caution efficiency, care of the purchase department, if the cost has come down, it is laudable effort and they should be appreciated for that. But, if actually the cost would have been 2.5, it was a budget estimates which were wrong.

We had anticipated too much high cost that is by 50 thousand extra; then the budgeting team should be, means fired for that- that your budgeting estimates are not correct. So, had this cost been not controlled at 2.5, but had it gone up to 3 lakhs. Because, your

budget says like this, then we could have been shelling out 50 thousand rupees extra, and lowering down our profits.

So, because of whom that variance had occurred. It is a favorable variance, anticipated costs is 3 lakhs. Actual cost is 2.5. We have saved 50 thousand. But, do not feel all the times, that 50 thousand saving is just because of the performance of the production or the purchase department. It maybe because of the wrong estimation of the budget estimates. Actual cost, means should have been estimated as 2.5.

Nobody has taken extra care, nobody has performed extra, and nobody has found out, anything special or done something extra or made any extra efforts. It is just because of the normal operations of the business but the estimation which was done by the budgeting team was wrong, so there is no need to appreciate anybody. Rather, we will have to say, say, mean make the budgeting team aware of, that where have they committed the lapse.

So, in both ways; if there is a negative variance, for example, now, the cost estimated was 3 lakhs. Actually, the cost of material has become 3.5 lakhs then it is a negative variance and that needs to be investigated, why the cost has increased? That is actually, the purpose of budgeting. But, if there is a positive variance, there is no need to feel happy, that there is a positive variance; so we should not, means analyze that variance.

In both ways, the variances, when they cross a minimum level of the analysis; when they cross a minimum level of the analysis, they need to be investigated. Now, what is the minimum of level of analysis? Minimum level of analysis of investigating the variances is, decided in two parts. How, they will decide the analysis level? In case of both, positive and negative variances analysis will be decided in two ways, it can be either in the percentage terms or it can be absolute terms. For example, what is the percentage term?

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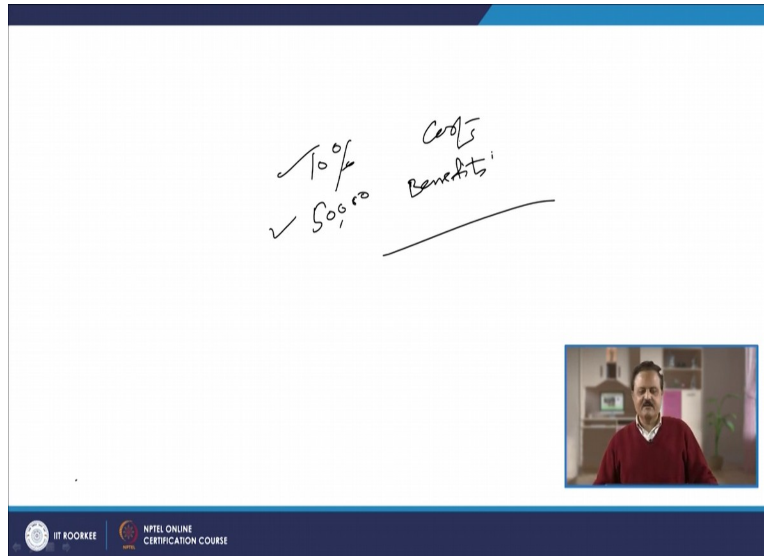

We say that, if the variances are, up to our 10 percent, right, or, say up to 50 thousands, in the absolute value, right. We will not analyze these variances because we all know it, that whatever the budget estimates, we have prepared, they are expected to vary plus and minus 10 percent; by plus and minus 10 percent. Cost of raw material can go up by 10 percent; cost of raw material can go down by 10 percent.

If that variance is within 10 percent of the, say basic amount or the estimated amount, then there is no need for analyzing the variances because we have already made the provisions for that. Similarly, in the absolute terms, for example, we decide our threshold level, that if the variances are plus minus by 50 thousand rupees or dollars, then there is no need to analyze because it is expected to happen.

For example, we have anticipated again, the raw material cost as 3 lakhs. Now actually, it becomes 3.5 lakhs or 2.5 lakhs. It is a variance of 50 lakhs, plus or minus; positive and negative, no need to analyze this variance because we knew it, that this much of the difference will occur, in the budgeted and the actual performances and another reason, doing that is, that because I told you, the basic Mantra of Management Accounting or maybe, the entire this discipline of the management accounting is based upon the two things and these two things are cost and benefit; cost and benefits.

So, when you talk about the cost and benefits, in every management decision making, in every management decision making, we will have to bare this in mind that your benefits always have to be, means more than the cost, or your benefits always have to outweigh the cost. For any management decision, implementation of any management decision, if the cost is more than the benefits, that is not a good management decision. That is not a good business decision.

So, when we have decided this threshold level of 10 percent or 50 thousands, after this if the variance is 15 percent, we will analyze it, if the various is more than 50 thousand, we will analyze it, in both positive and negative variances cases. We know it; one reason is that it is beyond our level of anticipation of 10 percent or 50 thousands, one reason. Second reason is, that if you analyze these variances, which are more than the 10 percent or 50 thousand, the cost of analyzing these variances will be much less as compared to the benefits, we are, say expecting to drive from this analysis.

Because, variance analysis also has the cost, your entire budgeting team or the variance analysis team has to sit down. They have to, means collect the total information budgeted is with us, actual we have to find out, means prepare all the statements. Then, we have to do a detailed analysis, in terms of converting into percentage or maybe the absolute values. So, it takes the time of people and those people are not free. They are expensive people; say analysis team is the expensive people.

So, that should, entire exercise should be done only, if you are expecting that the cost of analyzing the variances, is certainly going to be less than as compared to the benefits we are going to have from this analysis. So, for that reason, this threshold level is decided, 10 percent or 50 thousand is decided, pre-decided, that if it crosses 10 percent, then, yes, we will analyze it and if it crosses 50 thousand in absolute value, we will analyze it.

Otherwise, we will not go for the analysis of any kind of the variances, right. So, variance is the deviation of an actual amount from the expected or the budgeted amount and in this case, we have to have, the multiple level of the budgets; not the one level of budgets, which is the major limitation of the static budget.

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Master Budget Variance: Revenue

The variances of actual results from the master budget are called master (static) budget variances.

Actual	Budget	Variance
Rs 400,000	Rs 380,000	Rs20,000 (F)
Rs 370,000	Rs380,000	Rs10,000 (U)

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So, now for example, if you have the static budget only, the variance, variances of those actual results, from the master budget are called as static budget variances. For example, how do we calculate them? Look at this. Actual, this is the performance. This is the budgeted performance and this is the, you call it, as the say, variance, right. So, for example, you talk about this first one, is that sales value, that is 4 lakh rupees.

This has become, or the budgeted was 380,000. So, now we have the favorable variance of 20,000. We have sold for, by 20,000 rupees more. And, the second part may be the cost; total cost; cost of the goods sold, goods to be sold, was expected to be 380,000. But, actually the, say the cost has come down. So, in this case, you can call it as that, this is another variance.

So, what was the budgeted cost- 3 lakh 80 thousand, actual cost has come down to 3 lakh 70 thousands, so, this is the variance of 10 thousands, right. So, now we have two levels only; one is the budget, second is actual, right. Budgeted level of the sales of the 3 lakh 80 thousands, your cost was expected to be 3 lakh 80 thousands. So, it means, we were expecting the business to be at, the no profit; no loss.

But, actually what has happened? Your actual sales have gone up, cost has come down. So, there is a variance. But, it is only possible to analyze, that your actual performance is

equal to the budgeted performance. So, this is known as a static budget variance or the master budget variances. These are the revenue variances. In this case, because of performance has changed. Budgeted was 3 lakh 80 thousand, actual is 4 lakhs. So, you cannot say that only sales value has gone up, by 20 thousand, and expenses will not go up by the same amount.

It is not going to happen. If, the sales are going to increase, cost is also going to increase, but, is the cost increasing proportionately? Means, what should have been the cost of the production at 3 lakh 80 thousands of the sales level and what now, the cost has gone up for the 4 lakh rupees of the sales. Has it proportionally gone up? Or there has been something more than or less than the proportions that analysis is required.

So, you have now the cost information for 3 lakh 80 thousands level of the sales and actual performance has gone up to 4 lakhs. So, how do you analyze the variances? You have to now, convert the total cost of goods sold, in the same proportion as the, there is the change, in the value of the sales. So, for that, you do not have the budgets; because you have only static budget, for one level. So, for that we need the flexible budget.

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Master Budget Variance: Expenses

Actual expenses that exceed budgeted expenses result in unfavorable expense variances.

Actual expenses that are less than budgeted expenses result in favorable expense variances.

Similarly, you talk about, now the expenses. This, we are talking here about the, expenses part; master budget variance, in case of the expenses. Actual expenses that exceed

budgeted expenses result in unfavorable variances. Actual expenses that exceed the budgeted expenses result in unfavorable expenses, now, 3 lakh 80 thousands of the budgeted sales.

Actual sales have gone up by the 4 lakh by 20 thousands so 4 lakhs. So, how the cost has increased? Proportionately it has gone up? What was expected at 4 lakh rupees of the sales or the cost of production? Has it gone up in the same proportion or it has gone up more or less? That is again called as the variance. And, if actual expenses, that are less than the budgeted expenses, result in the favorable expenses or the favorable expense variances.

So, either way it can be possible. But, in both the cases, if it is beyond the threshold level, we will have to analyze those variances. Now, to remove all those limitations, as I told you that whatever the limitations of the one level of budgeting and the one level of the sales; if they do not match with each other, that is the limitation of the static budget. How we have to away? The answer is the flexible budget.

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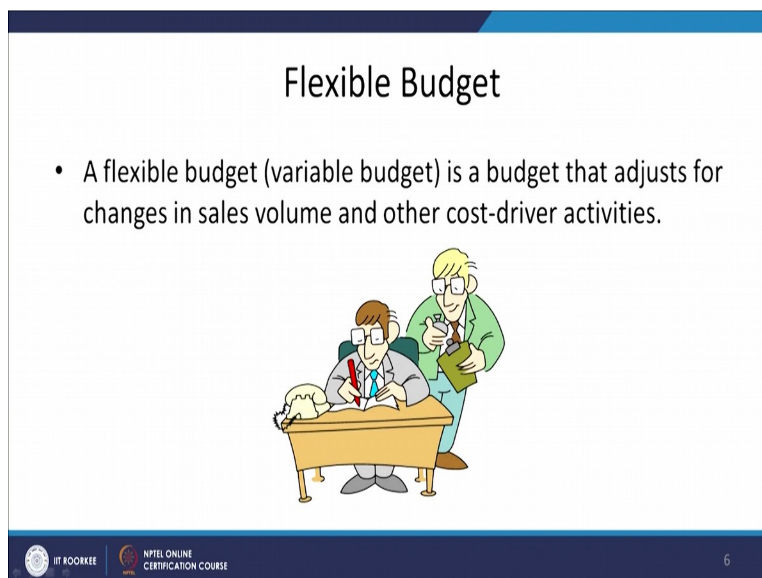

What is a flexible budget? A flexible budget or a variable budget is a budget that adjusts for changes in sales volume and other cost drivers activities. Means, a budget that adjusts for, automatically that adjusts for changes in the sales volume and the other cost driver

activities. So, what we do in this case, because, these days, you know that we prepare the budgets on systems, on the computers, so in the computers when we prepare the budget for one level, of the activity, for example, 8 lakhs worth of rupees sales.

So, what will do there? We will now convert that budget. For example, sales are 8 lakh rupees or they go up to 9 lakh or they come down to 7 lakh rupees sales; then how proportionately the cost will change? So, we calculate the cost, for all three levels 7, 8 and 9 lakh worth of rupees sales and then, we put the formulas in place, in the system, in the excel and we say that if the sales are 8 lakhs, this is going to be the cost of raw material.

If, they come down to 7 lakhs, then the percentage of the raw material is this much, so automatically, the system should adjust the cost of raw material. If they go up to 9 lakh, automatically the system should, means convert that into the 9 lakhs. So, what you have to do is? For that, you have to do this entire exercise, well in advance while preparing the budget and prepare the proper formulas and put the formulas in place.

So, that tomorrow whatever the actual level of performance, we have the budgets for that. If, you do not have the budget for that, you can within; I think in a few minutes, you can prepare the budget, because you have already put the things in place in the system. All the formulas are change, the moment you change, the top value of the sales, you are able to change or automatically, the other figures, or the other values, are changed automatically; you get the budgeted cash flow statement.

You get the budgeted income statement. You get the budgeted balance sheet, for the changed level of the sales. That will only happen, if you have been, means already doing this flexible or the variable budgeting exercise, where all the formulas are put in place. Everything is there in the system and that will also; we have to do at one point of time.

So, do not only rely upon the static budget. It is possible to give you the broad estimates. But, if you want to have the real management control system, then you have to go for the flexible budgets. What we do in case of the flexible budget formulas? Means, we have to put the formulas in place in the computer.

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Flexible Budget Formulas

The flexible budget is based on the same assumptions of revenue and cost behavior (within the relevant range) as is the master budget.

The flexible budget incorporates effects on each cost and revenue caused by changes in activity.

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The flexible budget is based on the same assumptions of revenue and the cost behavior with the relevant range as the master budget is. Relevant range means? We know that variable cost is proportionally changeable, when the sales level change. When the production is 7 lakhs, your variable cost will be this much. Because, if you, say require 10 units of raw material to manufacture 1 unit of the finished product.

So, if you manufacture the 2 units, you require 20 units. If, you manufacture 3 units, you require 30 units. So, proportionately it is changing. Now, we talk about the fixed cost. Fixed cost is a machine, for manufacturing, means, say, 10 thousands units, there is one machine. There is a maximum capacity of that machine or that plant for manufacturing the 10 thousand units. That is the maximum capacity of the plant.

Now, you manufacture 10 thousands units, by using that plant or you manufacture 8 thousand units by using that plant or you manufacture, say, 9 thousand units by using that plant, your fixed cost is going to remain the same; that is, whatever the costly we have incurred to install the plant and annual depreciation, will be calculated accordingly. It is not going to change, that if you are going to manufacture, the 9 thousand units, not 10 thousand units, then your fixed cost is going to come down, no.

Total fixed cost remains the same, per unit changes. If, you manufacture 10 thousand against the installed capacity of 10 thousand, your fixed cost is the optimum. But, if it is less than 10 thousand productions and sales, your fixed cost per unit increases, because the total fixed cost will be divided by the less number of units produced. So, that happens, in case of the fixed cost.

So, fixed costs remains the same at the given level of production, that changes beyond, when the production increase is beyond, say for example, in this case, 10 thousand units. But, the variable cost, means remains same; per unit it remains the same. One unit you are manufacturing, 10 units of the raw material are required. 2 units you are manufacturing, 20 units of the raw material are required. 3 units you are manufacturing, 30 units of the raw material are required.

So, variable cost changes but the fixed cost remains the same to a certain level of production. So, it means, we can have those assumptions in mind, convert that into the standard formulas, put them into the computers and, we can say, that if you manufacture and sell 10 thousand units, this much units of raw materials are required and if you reduce it to 9 thousand, this much units of raw material are required and if you reduce it to 6 thousand, this much units of raw material are required.

So, the moment, you change the level of sales and production, or production or sale; production and sales, automatically the raw material cost is going to change. So, that is called as a flexible budgeting system. The flexible budget incorporates effects on each and each cost and revenue, caused by the changes in the activity. The moment, the revenue changes, sale change, cost automatically changes.

So, you have put that system in place, in the computer, so that is going to very-very useful; very-very helpful and that is not the static budget. But that is called as the variable or the flexible budget. We will, practically prepare the practical budget, then you will come to know, that how it facilitates- better management decision making or the better management control.

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Now, in this case when you go for the flexible budgeting system, what you do here is that we again, prepare the performance evaluation reports by using the flexible budgets. Comparing the flexible budgets to the actual results, accomplishes an important performance evaluation purpose because you have actual performance 10 thousand units. Budget is also, is easily available with us, for the 10 thousand units then you make the comparison.

At 10 thousand units of production and sales, how much cost was expected? So, if you do not have, but you have the formula in the system, automatically, the moment you change the sales level, you will be able to change the cost performance also and even the system itself, will automatically work out the variances. In the last column, system will say, that material cost has the favorable variance or the unfavorable variance.

Labor cost has a favorable or unfavorable variance or similarly, the other cost variance will automatically be calculated. So, within no time that entire variance will be available with us. In the cases were the variances have crossed the minimum threshold level, in that case, we will analyze it, in detail. But, the variances which are within threshold level of 10 percent or 50 thousand, for example, that we will not analyze the variance and we will close the report.

So, this is something the beginning discussion, just a discussion I have initiated on the flexible budgets and their positives, say values, points and properties and remaining further more discussion, with some, say you can call it as the exhibits that how we go for the preparation of the flexible budget that I will discuss with you in the next class. Thank you very much.