RAMA UNIVERSITY

www.ramauniversity.ac.in

FACULTY OF COMMERCE AND MANAGEMENT

COURSE: MBA III SEM..

SUBJECT: WORKING CAPITAL MANAGEMENT

SUBJECT CODE: MBAFM02

LECTURE: 28

NAME OF FACULTY: DR. PALASH BAIRAGI

LECTURE-28

Average Cost Method:

Under this method, all items in the stores are mixed up in such a way that consumption of materials or sale of finished goods cannot be recognized from any particular lot of purchases. As a result, closing inventories are valued at the average cost of all the lots acquired under each type during a particular period.

The average cost may be:

(i) Simple Average Cost; and

(ii) Weighted Average Cost

(i) Simple Average Cost:

Under this method, averages of different prices are only considered without having regard to the quantities involved. The simple average cost is calculated by adding the different prices and thereafter divided by the total number of purchases. This method is applicable where there is a wide fluctuation in prices.

Illustration:

In a factory, stores are issued and accounted for on Simple Average Method. If the stock of a particular material on 1st Jan. 1992 is 1,000 units valued at Rs. 5 per unit and the particulars of purchases and issues during the month of Jan. 1992 are as follows, prepare a statement showing how the value of issues should be arrived at:

Dates			
Jan.3.	Purchases	200 units	at Rs. 5.50
9.	Issues	1,000 units	
15.	Purchases	1,400 units	at Rs. 6.00
17.	Issues	1,000 units	
21.	Purchases	800 units	at Rs. 6.50
23.	Issues	1,000 units	

Solution:

Store Ledger Account
Simple Average Method

Name of Material –
Specification –
Code No –
Unite of Measurement —

Bill No –
Location –

Folio No -
Maximum level –
Minimum level –
Re-ordinaring level –

	Receipts				Issues				Balance			
Date	G.R. No.	Quantity	Rate	Amount	S.R. No.	Quantity	Rate	Amount	Quality	Rate	Amount	Rem-arks
1992				Rs.				Rs.			Rs.	
Jan. 1.									1,000	5	5,000	
3.		200	5,5	1,100					1,200	—	6,100	
9.						1,000	5.25	5,250	200	—	850	
15.		1,400	6	8,400					1,600		9,250	
17.						1,000	5.75	5,750	600	—	3,500	
21.		800	6.5	5,200					1,400		8,700	
23.						1,000	6.25	6,250	400	—	2,450	

Notes:

1st Issue Price = (Rs. 5 + Rs. 5.50)/2 = Rs. 5.25

2nd Issue Price = (Rs. 5.50 + Rs. 6)/2 = Rs. 5.75

3rd Issue Price = (Rs. 6 + Rs. 6.50)/2 = Rs. 6.25