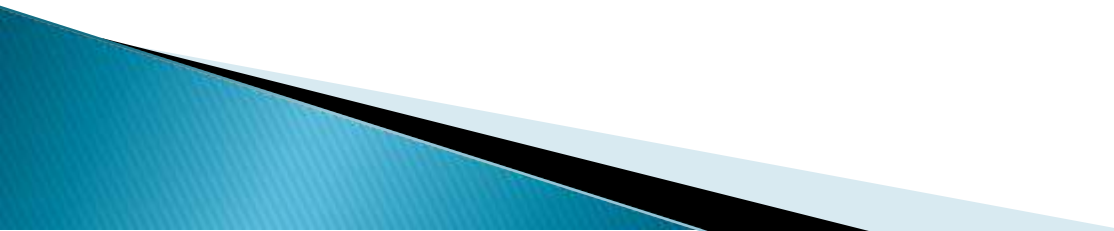


ECONOMIC ANALYSIS

PRESENTED BY
C. VEERALAKSHMI,
ASSISTANT PROFESSOR,
PG & RESEARCH DEPARTMENT OF
COMMERCE (SF- WOMEN),
JAMAL MOHAMED COLLEGE
(AUTONOMOUS),
TRICHY – 20.





Ways of classification of costs on the basis of their common characteristics are:

- 1. By nature or element
- 2. By functions
- 3. By identifiably
- 4. By variability
- 5. By controllability
- 6. By normality
- 7. Other Costs

1. BY NATURE OR ELEMENT



MATERIAL COST

Cost of materials used for the manufacture of a product, a particular work order, or provision of a service.

Example: Cloth for making a dress, stores used for maintaining machines and buildings such as lubricants, cotton waste, bricks etc.



LABOUR COST

Labour cost is defined as the total expenditure borne by employers in order to employ workers. Labour costs include the direct costs linked to remuneration for work carried out such as direct remuneration, bonuses and ex gratia payments not paid at each pay period, payments for days not worked, severance pay, benefits in kind. They also include indirect costs linked to employees, independently of the remuneration paid by the employer, such as direct social benefits, vocational training



EXPENSES

Expense is defined as money expended or cost incurred in a firm's efforts to generate revenue, representing cost of doing business. They may be in the form of actual cash payments (such as wages and salaries), a computed 'expired' portion (depreciation) of an asset, or an amount taken out of the firm's earnings (such as bad debts).

Whereas all expenses are costs, not all costs (such as those incurred in acquisition of income generating assets) are expenses.



2. BY FUNCTIONS

1. Production
Cost

2. Selling Cost

3. Distribution
Cost

4.
Administrative
Cost

5. Research
Cost

6.
Development
Cost

7. Pre-
production
Cost

8. Conversion
Cost

9. Product
Cost

PRODUCTION COST

The cost of the sequence of operations which begins with supplying materials, labour and services and ends with primary packing of the product. Thus it includes the cost of direct materials, direct labour, direct expenses and factory overheads.

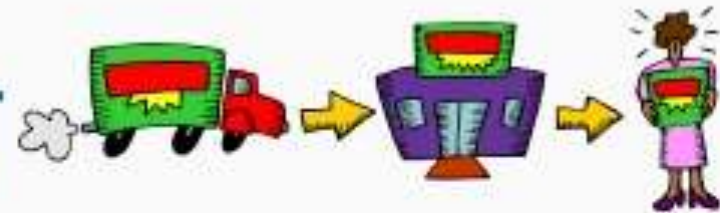


SELLING COST

The cost seeking to create and stimulate demand (sometimes termed 'marketing') and of securing orders.



DISTRIBUTION COST



The cost of the sequence of operations which begins with making the packed product available for dispatch and ends with making the reconditioned returned empty package, if any available for re-use.

It also includes expenditure incurred in transporting articles to central or local storage as well as in moving articles to and from prospective customers as in case of goods on sale or return basis. In gas, electricity and water industry distribution means pipes, mains and services which may be regarded as the equivalent of packing and transportation.

ADMINISTRATIVE COST

The cost of formulating the policy, directing the organization and controlling the operations of an undertaking which is not related directly to a production, selling & distribution, research or development activity or function.



RESEARCH COST

The cost of researching for new or improved products, new applications of materials, or improved methods.



DEVELOPMENT COST

The cost of the process which begins with the implementation of a decision to produce a new or improved product or to employ a new or improved method and ends with commencement of formal production of that product or by that method.



PRE-PRODUCTION COST

The part of development cost incurred in making a trial production run preliminary to formal product.

This term is sometimes used to cover all activities prior to production including Research & Development, but in such cases the usage should be made clear in the context



CONVERSION COST

The sum of direct wages, direct expenses and overhead cost of converting raw materials to the finished stage or converting a material from one stage of production to the next.

In some cases this also includes any excess material cost or loss of material incurred at the particular stage of production.



PRODUCT COST

These are inventoriable cost. These are the costs which are assigned to the product. Under marginal costing variable manufacturing cost and under absorption costing, total manufacturing cost constitutes product cost.



3. BY IDENTIFIABLY

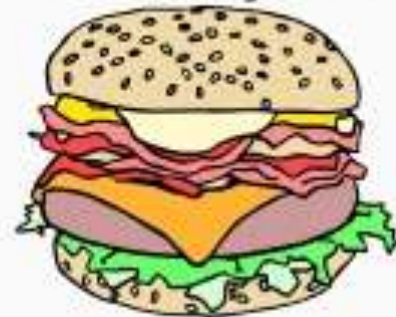
Direct Cost

Indirect Cost

DIRECT COST

The expenses on material and labour economically and easily traceable to a product, service or job are considered as direct costs. In the process of manufacture or production of articles, materials are purchased, labourers are employed and the wages are paid to them, certain other expenses are also incurred directly. Since all these take an active and direct part in the manufacture of a particular commodity, hence are called direct costs.

Example: Cost of meat in a burger



INDIRECT COST

The expenses incurred on those items which are not directly chargeable to production are known as indirect costs. Example: In production, salaries of timekeepers, storekeepers, foremen are paid, certain expenses for running the administration are incurred. All of these cannot be conveniently allocated to production and hence are called indirect costs.

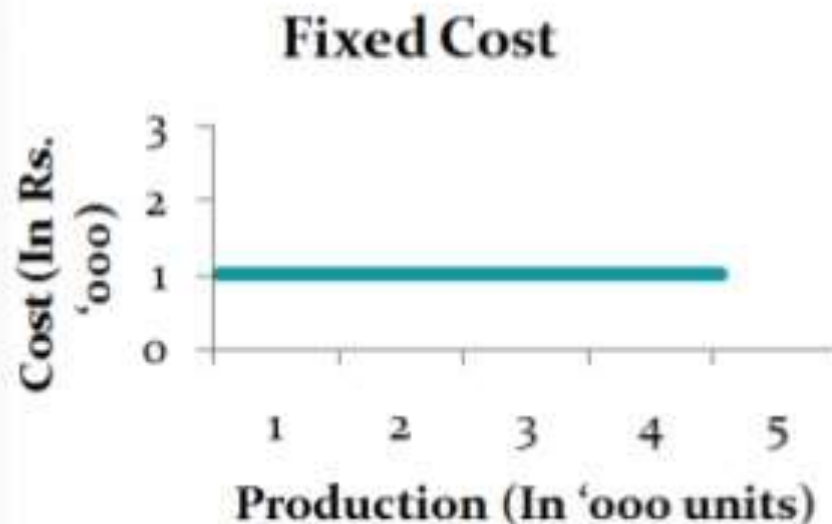


4. BY VARIABILITY



FIXED COST

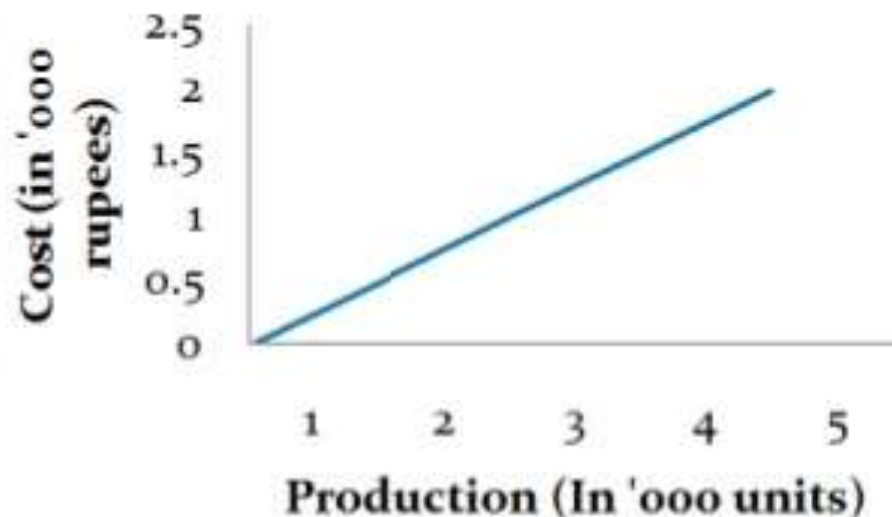
The cost which does not vary but remains constant within a given period of time and range of activity in spite of the fluctuations in production, is known as fixed cost. Example: rent, insurance of factory buildings etc. remain the same for different levels of production.



VARIABLE COST

These costs tend to vary with the volume of output. Any increase in the volume of production results in an increase in the variable cost and vice versa.

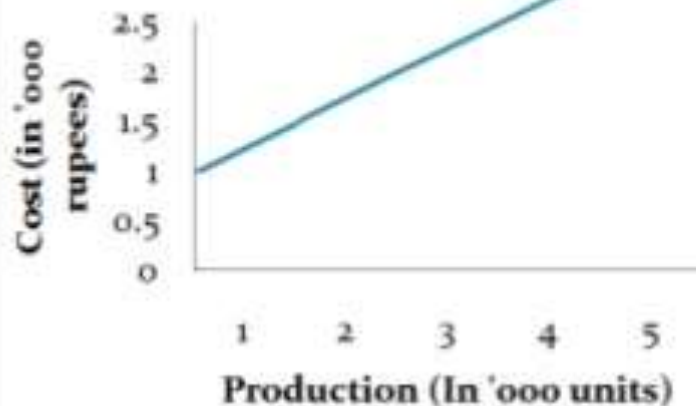
Example: cost of material, cost of labour etc.



Semi-variable Cost

The cost which does not vary proportionately but simultaneously cannot remain stationary at all times is known as semi variable cost. It can also be called as semi-fixed cost.

Example: Depreciation, repairs etc.



STEP COSTS

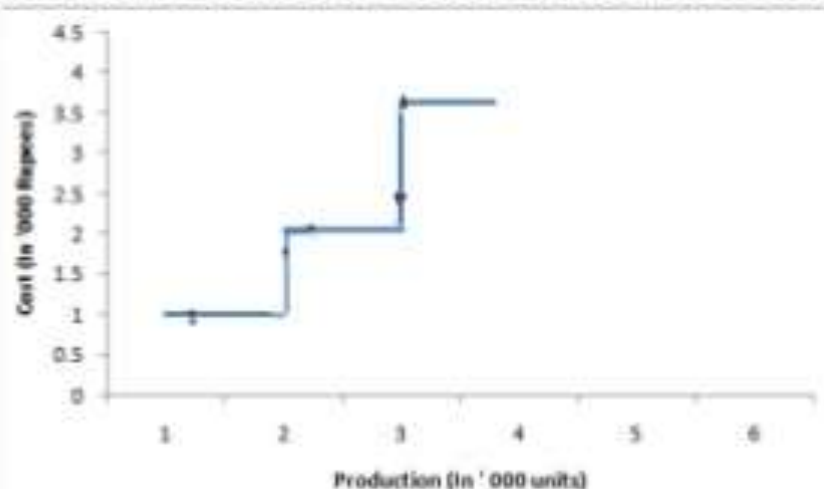
Fixed cost can be further classified into committed fixed costs and discretionary fixed costs.

- Committed fixed costs are unavoidable in the short term if the organization has to function. Examples are depreciation, rent, pay etc,
- Discretionary fixed costs are those which are set at a fixed amount for specific time periods by management . Examples are research and development costs, advertisement and market research expenses

STEP COSTS

Certain costs remain fixed over a range of activity and then jump to a new level as activity changes. Such costs are treated as “Step Costs”.

Example: A foreman is in a position to supervise a given number of employees. Beyond this number it will be necessary to hire a second then a third and so on.



5. BY CONTROLLABILITY

Controllable
Costs

Uncontrollable
costs

CONTROLLABLE COSTS

These are the costs which can be influenced by the action of a specified member of an undertaking. A business organization is usually divided into a number of responsibility centres and each centre is headed by an executive. The executive can thus control the costs incurred in that particular responsibility centre.



UNCONTROLLABLE COSTS

Costs which cannot be influenced by the action of a specified member of an undertaking.

Example: Expenditure incurred by the tool room is controllable by the foreman in charge of that section but the share of the tool room expenditure which is apportioned to a machine shop is not to be controlled by the machine shop foreman.



6. BY NORMALITY

Normal Costs

Abnormal costs

NORMAL COSTS

It is the cost which is normally incurred at a given level of output under the conditions in which that level of output is normally attained.

ABNORMAL COSTS

It is the cost which is not normally incurred at a given level of output in the conditions in which that level of output is normally attained. This is charged to Costing P&L A/c



7. OTHER COSTS

- Product Costs and Period Costs
- Decision making Costs and Accounting Costs
- Relevant and Irrelevant Costs
- Shutdown and Sunk Costs
- Avoidable / Escapable and Unavoidable / Inescapable
- Imputed or Hypothetical Costs
- Differential, Incremental or Decremental Cost
- Out of Pocket Costs
- Opportunity Cost
- Traceable, Untraceable Costs
- Joint Costs and Common Costs