2.1 Budgeting and Variance Analysis: Favourable and Adverse Variances

AQA 7132 · Calculators not allowed · about 60 minutes · Write-in edition

Total Marks

Name: _____ Date: ____ / ____ / _____

Answer ALL questions in the spaces provided. Show your working for every calculation. Label each variance as 'Favourable' or 'Adverse' where asked. GreenLeaf Catering Ltd, used in this pack, is fictional.

1 GreenLeaf Catering Ltd prepares a budget for May. Budgeted sales are 1,200 meals at a selling price of £8 per meal. Using these figures, calculate the budgeted revenue for May. Show your working.

(Total for Question 1 is 2 marks)

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2 GreenLeaf budgets variable cost per meal at £3. Calculate the total budgeted variable cost for May using budgeted sales of 1,200 meals. Show your working.

(Total for Question 2 is 2 marks)

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3 Calculate the fixed cost variance for May, stating whether it is Favourable or Adverse. Use budgeted fixed costs £4,000 and actual fixed costs £3,900. Show your working.

(Total for Question 3 is 1 mark)

4 Harbour Bakery Ltd budgeted to sell 850 celebration cakes in October at £24 each. It actually sold 790 cakes at the budgeted price of £24. Calculate the revenue variance for October and state whether it is Favourable or Adverse. Show your working.

(Total for Question 4 is 2 marks)

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5 A manager is told that the wages variance for the month was £600 adverse. Which one of the following is the most likely cause, if the business produced exactly its budgeted output?

- ☐ A) Staff were paid overtime rates to meet a deadline
- ☐ B) Two employees left and were not replaced
- ☐ C) Employees worked fewer hours than budgeted
- ☐ D) The business bought cheaper raw materials

(Total for Question 5 is 1 mark)

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6 Actual variable cost per meal was £3.20 in May. Using actual sales of 1,320 meals, calculate the total actual variable cost. Show your working.

(Total for Question 6 is 2 marks)

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7 Calculate the variable cost variance for May, stating whether it is Favourable or Adverse. Use budgeted variable cost £3,600 and actual variable cost £4,224. Show your working.

(Total for Question 7 is 2 marks)

8 Calculate the closing cash variance for May and state whether it is Favourable or Adverse. Use budgeted closing cash £3,500 and actual closing cash £3,936. Show your working.

(Total for Question 8 is 1 mark)

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9 GreenLeaf budgets fixed costs of £4,000 for May. Using your answers to questions 1 and 2, calculate the budgeted profit for May. Show your working.

(Total for Question 9 is 3 marks)

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10 GreenLeaf starts May with a cash balance of £1,500. The budget assumes all sales are received in cash and all costs are paid in May. Using budgeted revenue £9,600 and total budgeted costs £7,600, calculate the budgeted closing cash balance for May. Show your working.

(Total for Question 10 is 3 marks)

11 Calculate the revenue variance for May for GreenLeaf Catering Ltd, stating whether it is Favourable or Adverse. Use budgeted revenue £9,600 and actual revenue £10,560. Show your working.

(Total for Question 11 is 2 marks)

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12 Cove Bakery Ltd budgeted to use 2,000 kg of flour and other ingredients in March at £3.10 per kg. It actually used 2,000 kg but paid £3.37 per kg. The materials cost variance was therefore adverse. Explain one possible reason why the price paid per kg was higher than budgeted and one action the bakery could take in response.

(Total for Question 12 is 4 marks)

13 Actual fixed costs were £3,900 in May. Using actual revenue £10,560, actual variable costs £4,224 and actual fixed costs £3,900, calculate the actual profit for May. Show your working.

(Total for Question 13 is 3 marks)

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14 Using opening cash £1,500, actual receipts £10,560 and actual payments £8,124 for May, calculate the actual closing cash balance for GreenLeaf. Show your working.

(Total for Question 14 is 3 marks)

15 Evaluate how useful variance analysis is for managing GreenLeaf Catering Ltd, using the budget and variance figures provided in this pack. In your answer, consider the advantages and limitations of variance analysis, possible causes of the variances shown, and the corrective or management actions GreenLeaf's managers might take. Use evidence from the budget and variance figures to support your judgement.

(Total for Question 15 is 12 marks)

Mark scheme · 2.1 Budgeting and Variance Analysis: Favourable and Adverse Variances

Question 1

1,200 x 8 seen	**M1**
£9,600 cao	**A1**

Answer: £9,600.

Question 2

1,200 x 3.00 seen	**M1**
£3,600 cao	**A1**

Answer: £3,600.

Question 3

£100 Favourable cao	**B1**

Answer: £100 Favourable.

Question 4

(850 - 790) x 24 seen, or 20,400 and 18,960 seen	**M1**
£1,440 Adverse cao	**A1**

Answer: £1,440 Adverse.

Question 5

A cao	**B1**

Answer: A

Question 6

1,320 x 3.20 seen	**M1**
£4,224 cao	**A1**

Answer: £4,224.

Question 7

4,224 - 3,600 seen	**M1**
£624 Adverse cao	**A1**

Answer: £624 Adverse.

Question 8

£436 Favourable cao	**B1**

Answer: £436 Favourable.

Question 9

profit = revenue - (variable costs + fixed costs) stated or implied	**M1**
9,600 - (3,600 + 4,000) seen	**M1**
£2,000 cao	**A1**

Answer: £2,000.

Question 10

closing cash = opening cash + receipts - payments stated or implied	**M1**
1,500 + 9,600 - 7,600 seen	**M1**
£3,500 cao	**A1**

Answer: £3,500.

Question 11

10,560 - 9,600 seen	**M1**
£960 Favourable cao	**A1**

Answer: £960 Favourable.

Question 12

identifies a plausible reason for the higher price, e.g. the supplier raised its prices, wheat prices rose, or the bakery bought smaller batches and lost a bulk discount	**B1**
explains how the reason leads to a higher price per kg while the quantity used stayed the same	**B1**
identifies an appropriate action, e.g. negotiating with or switching to another supplier, buying in bulk, or reviewing recipes or prices	**B1**
explains why the action would reduce the adverse variance or protect profit	**B1**

Answer: Any valid reason and response, e.g. the supplier raised its prices, so each kg cost more even though the quantity used was as budgeted; the bakery could negotiate a bulk discount or switch supplier to bring the cost per kg back towards £3.10.

Question 13

profit = revenue - (variable costs + fixed costs) stated or implied	**M1**
10,560 - (4,224 + 3,900) seen	**M1**
£2,436 cao	**A1**

Answer: £2,436.

Question 14

closing cash = opening cash + receipts - payments stated or implied	**M1**
1,500 + 10,560 - 8,124 seen	**M1**
£3,936 cao	**A1**

Answer: £3,936.

Question 15

Level 1 Makes simple statements about variance analysis with little or no reference to the GreenLeaf figures and few if any linked conclusions.	**1-3**
Level 2 Describes advantages and limitations of variance analysis and refers to some GreenLeaf figures, but analysis is limited and the evaluation is not well developed.	**4-6**
Level 3 Gives a well developed discussion of the usefulness of variance analysis, applying it to GreenLeaf figures and analysing causes and likely managerial responses, but the final judgement is only partially justified.	**7-9**
Level 4 Provides a thorough, balanced evaluation that uses GreenLeaf figures to analyse causes of variances, considers management actions and limitations, and reaches a justified conclusion about overall usefulness for managing the business.	**10-12**

Indicative content:

- Advantages: variance analysis highlights differences between actual and budgeted performance, for example revenue is £960 favourable and variable costs are £624 adverse, giving managers prompt signals about sales success and cost control.
- Application to GreenLeaf: higher sales volume (1,320 actual vs 1,200 budgeted) produced the favourable revenue variance of £960 and increased profit by £436, suggesting demand is stronger than expected.
- Causes of variances: revenue variance may be due to higher footfall, a successful local marketing campaign or a one-off event; variable cost adverse variance may be caused by supplier price rises, waste, or higher portion sizes, given unit variable cost rose from 3.00 to £3.20.
- Managerial responses: to the favourable revenue variance, managers might plan to increase capacity or negotiate better supplier terms; to the adverse variable cost variance they could seek cheaper suppliers, reduce waste, review portion control, or renegotiate purchase contracts.
- Limitations: variances do not by themselves prove cause, for example revenue could be temporarily high but not sustainable; small businesses may face timing differences in cash receipts that budgets do not capture; some variances mask mixed effects, for instance the £100 favourable fixed cost variance might be due to delayed expenditure rather than permanent savings.
- Practical issues: data quality and the timing of reports affect usefulness; managers need to investigate material variances, not overreact to small, immaterial ones, and should consider both short term and long term implications.
- Judgement: a supported conclusion weighing the benefits of quick feedback from variance analysis for GreenLeaf against its limitations, for example that variance analysis is highly useful as an early warning and control tool provided managers investigate causes, consider materiality and combine variances with other information such as customer feedback and supplier contracts.