METHODS FOR VALUING STOCKS

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Abstract

Inventories are current assets, i.e. working capital that directly affect the increase or decrease of the working capital of the enterprise. They are an integral part of everyday work. Data on them are very important indicators in the functioning of the production process. One of the most important issues for achieving economy and rationality in the operation of business entities is determining the optimal amount of storage.

Due to the different types of inventory, as well as determining which is the smallest and which is the largest amount of inventory that a company should have, the management of each individual business entity is faced with a difficult decision.

Here, the accounting records are of particular importance for the perception of operating costs of companies. The value of inventories includes the cost of procurement, conversion costs and other costs incurred in order to bring inventories to their current location and current condition. All products that are not sold are presented by the companies as inventories in the balance sheet.

In the future, when the same products are sold, inventory costs are converted into expenses (cost of sales) and are shown in the income statement. Furthermore, these expenses are deducted from net sales. The additional expenses are deducted and the net profit is obtained.

All this, due to the possibility of assessing the profitability of business entities which is perceived through the gross profit presented in the financial statements.

Keywords: current assets, optimal quantity, production process, costs, gross profit.

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1. Introduction

Beginning from the term inventories, they represent, from both accounting and economic points of view, significant assets in the balance sheet.
According to the International Accounting Standard (IAS 2) Inventories are defined as assets that can be:

- Products intended for sale,
- Ongoing production,
- Raw materials intended for the production process or provision of services.

Namely, according to this definition, stocks can be classified as:

- Stocks of finished products, trade goods, intended for sale,
- Inventory of unfinished production,
- Inventories of raw materials.

These assets are working capital that is ready to be included in the production process or to meet the needs of consumers.
That is, analytically speaking, these assets are treated based on the importance of the continuity of reproduction. They need to ensure continuity of operations because a lack of inventory can cause downtime and certain disruptions in the overall functioning of business entities.
All stocks are of great importance, but here we will emphasize the following:

- Finished products in stock,
- Goods in stock,
- Raw materials in stock,
- Spare parts in stock,
- Small inventory,
- Packaging and tires in stock.

Raw materials are objects in the production process and their participation is seen in the creation of new values. This means that the raw materials analyzed from the aspect of the production process represent a dialectical connection between the means of labor and labor.
Namely, the stocks should observe the principle of continuity in the operation of the enterprises. At no time should a gap be created, ie lack of inventory that will cause an interruption in operation. This situation is specific and can cause cost increases, loss of suppliers, discontinuity, and loss of markets and consumers. But, there is also the opposite case, where the companies accumulate huge stocks and thus cause again increase of costs, tied financial assets in the stocks themselves, increased engagement for their accumulation and storage, and so on.

2. Storage of stocks of raw materials, spare parts and small inventory

Inventories of raw materials, spare parts, and trade goods are valued at their purchase cost. Inventories are an important segment of the assets of the business entity and therefore their accurate records, valuation and spending are of great importance. Purchase value is the sum of invoice value plus dependent costs.

The net invoice value is the invoice value that is reduced for the discounts by the supplier (rebates, bonuses, etc.). While the dependent costs include all direct costs incurred in the process of procurement of inventories, up to the moment of their final storage.

Namely, keeping stocks of raw materials, spare parts, and small inventory has certain disadvantages no matter what type of organization it is. For every company, trade company, etc. (production, sales, service) it is necessary to store a certain amount of inventory, which generates costs. Furthermore, all inventories represent non-current assets. And we know that money and cash are the lifeblood of every business. It is therefore important that inventories are converted into cash within a reasonable period.

Also, each stock requires space and conditions for its storage If the company does not have its own warehouse space, there is a need for rental which generates additional costs that will be further multiplied throughout the process. The specificity of each stock needs a space that offers complete protection of the same, while a certain type of product requires storage following the prescribed dimensions and the like. Also, security needs to be guaranteed from theft, damage, etc.

Additional conditions that can negatively affect the operation of companies can be supplemented through natural disasters, market closures, competition with lower prices, outdated goods, expiration date, durability, untimely disposal, ie sale of stocks, etc.

Therefore, inventory management requires competent managers who are ready to meet all the needs of the operation of a particular company. Excessive inventory and mismanagement cause costs such as:

- Obsolescence and unusability of inventories,
- Unprofitable operation (lost profit),
- Insurance costs,
- Rearrangement, manipulation and transfer costs,
- Warehouse space costs,
- Costs caused by uneconomical production,
- Costs of losing trust with suppliers,
- Costs from unused benefits in the procurement,
- Other costs.

That is, from this aspect, as well as their importance for the course of production, it contributes to more objective accounting records of the purchases and deliveries of raw materials to the business entities.

3.Determinants of the value stocks

The determination of the value of inventories under IAS 2 is made according to the cost of acquiring them. They should be measured at cost or net worth, whichever is lower. Or to put it more clearly, the procurement of raw materials is accounted for following the invoices delivered by the suppliers. This means that the procurement can be done by suppliers in the country or abroad.

According to the performed procurements from different suppliers, appropriate accounting records are performed. When purchasing raw materials, it is necessary to emphasize that certain costs are incurred, which are expressed in appropriate accounting accounts. The value of inventories includes procurement costs, conversion costs, and other costs incurred during the procurement until the moment of their storage. The determination of the production, ie the determination of the value of the stocks of the unfinished production and the stock of the finished products, is done by determining the value of the costs, which constitute the production as a process.

Inventories are of great importance to all business entities and therefore their real valuation is necessary. Valuation is a complex process and it is necessary to take into account certain factors, such as: goods on the road, goods in consignment, goods for special sales contracts, then, determining the costs to be taken as inventory costs, as well as determining the method used to determine the cost of the product.

Inventory costs include purchase price, import duties, and other taxes, costs that can be borne by the finished product, materials, and services. The cost of inventories comprises all expenses related to the purchase, preparation, and preparation of inventories for sale.

Conversion costs are those costs that directly or indirectly relate to the production process. These costs are directly related to production and such are direct wages distributed on a systematic basis, fixed and variable costs related to production, which are incurred by conversion, ie conversion of materials into finished products. Fixed overheads are indirect costs that remain relatively constant regardless of the volume of production (depreciation and maintenance of buildings and equipment, as well as management and administration costs). These costs should be allocated to the cost of the final products on a systematic and rational basis, as well as based on normal capacity and by the accounting policy of the enterprise.

Variable overhead costs of production are those indirect costs that directly depend on the volume of production (indirect materials and indirect wages). These costs are allocated in proportion to one of the keys used to allocate fixed overheads. Conversion costs include direct manufacturing costs, fixed overheads, and variable overheads that are related to production and are allocated to production benefits.

Other costs or expenses of the period are included in the cost of inventory only to the extent that they are incurred in bringing them to their current location and current condition.

4.Analytical records and methods for measuring stocks

Given the importance of this type of asset, business entities need to organize appropriate analytical records. This means that through such records it is necessary at all times to accurately know ~~exactly~~ and to have information about each receipt and issuance of funds in the process of production or sale. The analytical records provide individual data on the condition and dynamics of each type of item, ie stocks during the operation of the enterprises. The most important task in inventories is their estimation. The method of estimation, ie the method by which the consumption of inventories is estimated, depends on the value of the

total assets, presented in the balance sheet, ie the number of costs, expenses, and the financial result for the accounting period.
To determine the price of stocks and the price of products sold, four methods are used, namely:

- Specific identification method,
- (FIFO method), First input, first output,
- (LIFO method), Last input, first output,
- Weighted average method.

Each method applies certain steps to how much cost is incurred in inventory. Each of these four methods is permissible, regardless of whether the actual physical product flows follow the assumption of cost flows. The physical flow of products depends on the type of product and the way it is stored (products with a short shelf life - fruit) use one method (FIFO). Or in the case of oil and oil derivatives, decorative stones, etc., another method is used (LIFO), etc.
International Accounting Standard 2 - Inventories provides for several methods of measuring inventory. Specific identification method used when procuring specific goods, ie items that have a high value (cars, expensive equipment, etc.). It can also be noted that this method is the only approach based on the physical flow of inventory units in determining the cost of sales performance.
Namely, this method can be applied in practice in the case when based on the procurement invoice, the specific unit of the stock that has been procured can be directly identified.

Also, for the correct application of the method of specific identification of great importance with each invoice for sale, it is necessary to accurately identify the specific unit and the time when it was sold. In IAS 2 Inventories, methods for measuring inventory expenditure are set out following this Standard. individual costs ".
"the costs of individual types of inventories that are not regularly exchanged and the goods or services produced and allocated to specific projects should be determined using a specific identification of their individual costs."

5.Conclusion

From the content of this paper, it can be concluded that the standard allows an alternative approach to the use of methods, except for stocks where the method of specific identification is applied.

Namely, the weighted average method, or otherwise called the average price method is calculated by dividing the total amount of products for sale by the total units of sale and thus obtaining the average cost price that is applied to the final stock. This method offsets the effects of decreasing and increasing the cost of final supplies. While the FIFO method is based on the fact that the cost of inventories that are first procured, they first enter the production process. According to this method, the flow of material to the output is calculated according to the price of the first purchased material, as long as that material is in stock. After the completion of that material, we move on to the next procurement material, then the next one, etc. The FIFO method measures the final inventories according to the latest cost prices and includes the initial input targets for procurement in the cost price of the products sold. In case of price increase, this method contributes to higher profit, because the cost price of the sold products includes the prices of the initial purchases. In conditions when prices fall FIFO has the opposite effect, therefore the main disadvantage of the FIFO method is that it emphasizes the determination of higher profits.

That is, the LIFO method is an alternative method, which is based on the fact that the last procurements come out first in the production process. When prices rise the Lifo method underestimates stocks and makes lower profits. In conditions when purchase price is constant, each method has an equal impact on the value of inventory and the cost of sales performance. When the opposite is the case, the purchase price changes, depending on the change in the purchase price each method has a different impact on the net profit. The choice of inventory measurement method can have a crucial impact on the amounts presented in the income statement and the balance sheet. Therefore, all business entities under IAS 2 must disclose the methods used to calculate inventories in their financial statements or footnotes to the financial statements. This is mandatory because the methods used may have certain repercussions on the financial and tax reporting of the business entity.

From the aspect of proper analysis of the financial statements, it is extremely important to know and understand the methods for measuring and calculating inventories due to their impact on the real expression of the profit of the business entity. Therefore, when using inventory measurement methods, it is necessary to start from the principle of consistency, which should be applied to all four types of methods. This principle requires the business entity to use the same accounting-analytical method for a longer period, which makes the financial statements comparable for several years so that the users of financial statements can compare the statements of the company from past and future periods.

Over time, due to certain circumstances, stocks often become obsolete or damaged which results in the reduction in their selling price. In such a case, it is necessary to reduce the value of stocks of finished products to their net realizable value, and the value of raw materials to the level of replacement costs. In such a case, it is necessary to partially write off the inventory at a price lower than the cost price.

It is also necessary to prepare a stock plan at the end of the year. This plan refers to the direct materials of the finished products.

Namely, the plan for the stocks of direct materials is prepared based on the procurement plan.

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