Accounting- Merchandising

Our topic this lecture is Merchandising. By definition, it is just a company where items are purchased and resold to others. This differs from the Service Companies that we have previously discussed. An example of a merchandising company would be Macys! They buy clothes and goods from many sources and turn around to sell them in their stores.

Video Alert

Here is a great video that explains how merchandising accounting works!

http://www.youtube.com/watch?v=139NEANvig4

The financial statements for these differ. There are now sales revenue, cost of goods sold and a gross profit. The company starts by purchasing some inventory of goods, then selling the goods and collecting cash. This cycle repeats on a consistent basis.

Merchandising companies keep inventory. So it is important to understand more about this. There are two main systems for keeping inventory: Periodic and Perpetual. There are times when we receive the goods for a discount if we pay early. Those are called purchase discounts and are great to take advantage of. Some key ratios that are useful for merchandising are covered in this discussion.

Gross Profit Percent: Gross profit/Net sales revenue

We use this ratio to keep a good handle on profits.

Inventory Turnover: Cost of Goods Sold/Average Inventory

We want this amount to be high. A successful company is turning over its inventory very frequently. Stale goods that do not sell can end up being useless.

Days in Inventory: 365 days/ Inventory Turnover Ratio

We prefer this number to be low. A successful company will be moving/ turning over the inventory quickly!

Ratios are a useful and easy way to see how our company is doing. It is used to compare our company to how we did last period OR to compare it to our competition!

Web Site Alert

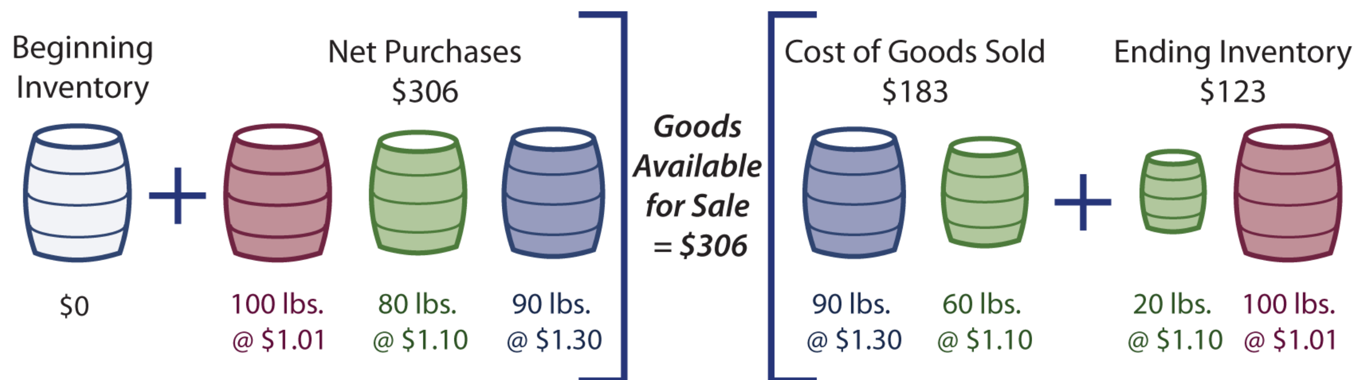
Here is a good website that explains key ratios well!

http://www.investopedia.com/terms/i/inventoryturnover.asp

In this lesson, we start with some key principles that you will want to know. The materiality concept tells us that we want to be certain an item is material or not. This means that if it is large/significant we will take extra care in accounting for it accurately. Of course, we are always accurate. But, the larger the item – the more risky an error can be.

Next we see that there are three main inventory costing methods. This means that we will have one of these in place at our company. These are:

- FIFO
- LIFO
- Average Cost



The FIFO method means that we will assume, (and deduct), that the items sold now were the first ones (or oldest ones) that we purchased. LIFO is "last in, first out" so you can guess what that will mean! Average cost uses just an averaging of how much the unit cost us to know how much to reduce our inventory by.

Important Reminders/Tips

Check out all Assignments for week 3 in the Student Guide. See you in the Discussion Boards!

Enjoy your week!

Debra Touhey, MSA, CFE

Reference

Horngren, C.T., Harrison, W.T. Jr. & Oliver, S. M. (2012). Accounting (9th edition). New Jersey: Prentice Hall.