Chapter 16

Fifo / Lifo
Tango is company that trades in oil. They mainly trade in West Texas Intermediate, also know as Texas Light Sweet, an internationally widely traded type of oil.
Sales – and the purchase price of the product - fluctuate over time. In the table below we see the sales and purchase transactions for June.

Date	Transaction	Units (Barrels)	Price per Barrel
June 02	Purchase	100,000	$46
June 06	Sale	70,000	$48
June 11	Sale	90,000	$50
June 15	Purchase	200,000	$49
June 20	Purchase	150,000	$50
June 25	Sale	300,000	$52

On June 01, the opening inventory consisted of 80,000 barrels with a purchase price of $45 per barrel.

Required:
A. Profit for June using First in First out (Fifo) for inventory valuation.
B. The value of the ending inventory using Fifo.
C. What can you say about June's profit if Last in First out (Lifo) were used? Would it be higher, lower or the same? And why?
D. Explain how using Fifo as opposed to Lifo influences the cash flow of the business.
E. In this example we have ignored Value added tax (VAT). Explain how VAT would influence the profit calculation.

Solutions Fifo Lifo
A. Fifo Profit

70,000*(48 – 45) = 210,000

10,000*(50 – 45) =   50,000
80,000*(50 – 46) = 320,000

20,000*(52 – 46) = 120,000
200,000*(52 – 49) = 600,000
80,000*(52 – 50) = <u>160,000</u>
1,460,000

B. Ending inventory = 70,000*50 = 3,500,000

C. Lifo profit will be lower due to rising purchase prices

70,000*(48 – 46) = 140,000

30,000*(50 – 46) = 120,000
60,000*(50 -45) = 300,000

150,000*(52 – 50) = 300,000
150,000*(52 – 49) = <u>450,000</u>
1,310,000

D. No influence on cash flow (except for effects of taxation which are ignored in this exercise).

E. VAT has no influence on profit.