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Spoilage with a Production Function

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Abstract

The traditional accounting for spoilage has been somewhat ad hoc since there has been no general theory of how spoilage occurs or can be controlled. This paper uses an economic analysis to model the determinants of spoilage in the production process and to show how normal spoilage can be chosen in a cost minimisation program. The model also generates an expanded variance analysis of spoilage which provides guidance in the investigation and interpretation of abnormal spoilage. It is argued that this approach results in both optimal and flexible product decisions.