

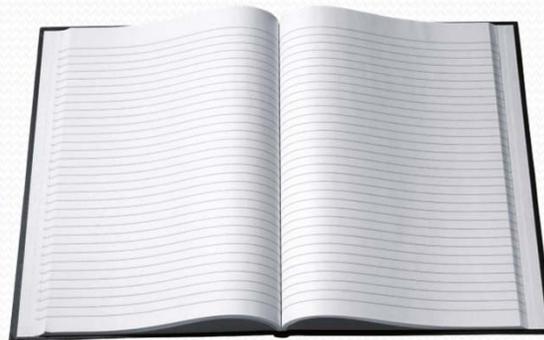
Week 2 – Chapter 3

SALES and REVENUE BUDGETS



FNSACC503A
Manage Budgets and Forecasts

By the end of this lesson, you will be able to...



1. Discuss qualitative and quantitative methods of forecasting revenue.
2. Discuss the factors affecting revenue forecasting.
3. Prepare a sales budget for a merchandising firm and a revenue (or fees) budget for a professional services firm.

Master budgets

- a combination of all the budgets of an organisation.
- all the budgets in a master budget link back to the **assumptions** made about the **quantity and value of sales** incorporated in the sales budget.
- therefore, it's very important to get these assumptions right.

MASTER BUDGETS (chapter 1 : budgeting fundamentals)

Budget income statement

MERCHANDISING	PROFESSIONAL SERVICES*	MANUFACTURING
Budget income statement		
Sales	Fees income	Sales
Purchases >> COGS	Professional and support labour costs e.g. dentist + dental assistant	Production + Ending Inventories * direct materials (usage + purchases) * direct labour * factory overhead >> COGS
Marketing expenses	Marketing expenses	Marketing expenses
Admin. expenses	Admin. expenses	Admin. expenses
Financial expenses	Financial expenses	Financial expenses



Cash budget



Capital expenditure budget



Budgeted balance sheet

* sells expertise and knowledge

What is forecasting?

MIXTURE OF

ART + SCIENCE



Forecasting methods

Qualitative → based on opinion, therefore **subjective**

1. Jury of executive opinion
2. Delphi technique
3. Sales force composite
4. Market research

Quantitative → make use of mathematical modelling, therefore **objective**

1. Time series models
2. Causal models

FACTORS AFFECTING REVENUE FORECASTING **STUDENT ACTIVITY**

Instructions:

Read through each of the following case studies. See if you can guess which of the sixteen factors the case study is referring to. The correct answer will be revealed on slide following the case study.

CASE STUDY

Jennifer Taylor is the Finance Manager at Holiday Heaven, a boutique travel agency which specialises in arranging five-star holidays in some of the world's most exotic locations. Holiday Heaven is renowned in the travel industry for providing its services exclusively to the rich and famous living in both New York and Los Angeles. However, over the next 12 months, Holiday Heaven's CEO has made the decision to expand the company's **target customer base** to include famous people living in other parts of the world. Rumour has it that The Royal Family will be one of Holiday Heaven's new customers. In preparing the travel agency's revenue budget for the coming year, Jennifer will increase last year's sales figure by 50% to reflect this change in the company's strategy.

FACTOR

16. CHOICE OF CUSTOMERS or MARKET SEGMENTS

CASE STUDY

Olivia Tan works as the Financial Analyst of Step Up which manufactures and sells a range of practical yet stylish shoes for both men and women. Olivia is in the process of preparing the company's sales budget for the coming year and after her meeting with the Operations Manager, she found out that the company recently finished building another production plant located in Somersby which has effectively doubled the company's production capacity. Based on the fact that last financial year the company had trouble keeping up with the demand for most of its popular styles, Olivia has, in preparing the new sale's budget, made the assumption that stock manufactured in the Somersby plant will be sold, resulting in a huge increase in the company's sales revenue.

FACTOR

15. PRODUCTION CAPACITY

CASE STUDY

Recent social trends indicate that more often than not, both parents in every household work either on a part-time or full-time basis. With this comes an increase in the demand for convenience foods because on the days where both parents work, there is just not enough time in the evening for a wholesome family meal to be prepared. Jackie Chan works as the Management Accountant of a company which specialises in making and selling convenience food options aimed at the consumer with a family to feed. They are marketed as nutritious and complete family-sized meals which require minimal preparation. In line with this trend, Jackie is going to forecast an increase in the company's sales revenue for next financial year.

FACTOR

4.

SOCIAL / CULTURAL TRENDS

CASE STUDY

A company called Procter & Gamble owns a dog & cat food brand called Eukanuba. It is sold in 1kg, 3kg and 7.5kg bag sizes. For the month of July, a promotion is planned whereby consumers will receive the 1kg bag for free if they purchase the 7.5kg bag. This will encourage consumers who normally purchase the small bag to trade up to the larger bag. This will translate into an increase in sales revenue of 10% if the promotion is run in all the major pet stores across NSW.

FACTOR

14.

PLANNED ADVERTISING and PRODUCT PROMOTIONS

CASE STUDY

Jack Daniels owns a building company which specialises in the construction of aged care facilities. Following the recent census, the Australian Bureau of Statistics released a report saying that Australia has an ageing **population**. Over the next 10 years, Jack expects his sales revenue to increase as the demand for retirement homes goes up.

FACTOR

1. DEMOGRAPHIC TRENDS

CASE STUDY

Sam Turner owns and operates several petrol stations across Sydney. In an article in The Daily Times yesterday, Sam read that by the year 2020, it is predicted that one in ten cars globally will run on battery power. The electric car is expected to have a major impact on the car industry especially given that it is a more environmentally friendly alternative to the types of cars that we see on the road today and given that petrol prices are expected to keep on going up. The increasing popularity of this **new product** will mean a decrease in the demand for petrol given that these cars run on battery power. As a result, Sam has predicted a year-on-year decrease in sales revenue of about 2.5%.

FACTOR

10.

NEW PRODUCTS

(launched by the firm)

11.

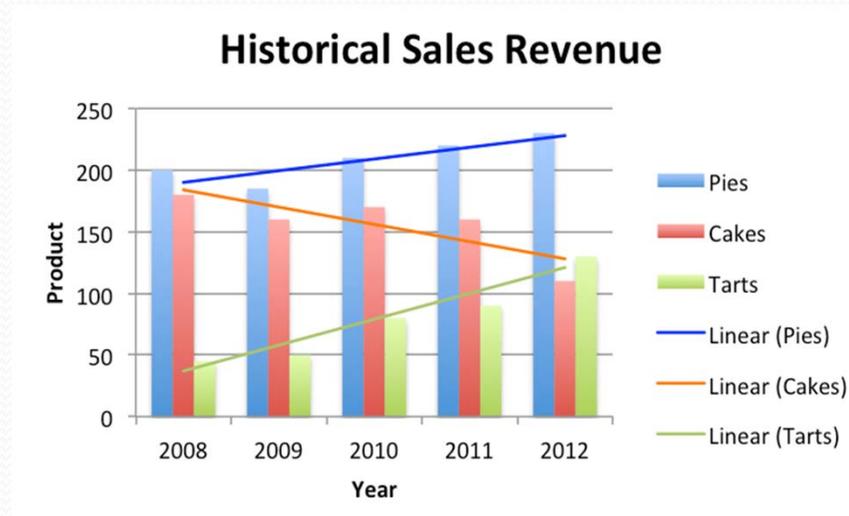
NEW PRODUCTS

(launched by the firm's competitors)

* may also include new product releases in general

CASE STUDY

Sarah Lee is preparing her sales budget for next financial year by period and by product. She downloads some of her past sales data and puts together the following graph which she uses as an indicator of future sales levels:



FACTOR

12.

PAST SALES LEVELS AND TRENDS

CASE STUDY

Ted Jones is the Management Accountant of Fisher Price which is a company that makes toys for infants and children. Ted has been asked to prepare the sales revenue budget for a 6-month period to 30 June 2014 for a new product it hopes to launch on 1 January 2014.

VeggieTales is an American TV series. The animated feature involves stories for young children told by a group of vegetable characters who live on a kitchen countertop. Fisher Price is in the planning phase of creating each of the characters from the series which will be molded of plastic. It will sell each of the characters separately together with one of the five play sets in the series. To get some idea of the market potential for this new product, Ted has asked a **market research** company to conduct some research. Once he has an idea of the market potential, he will be in a better position to estimate the company's sales potential, the sales potential for the product being a certain percentage of its market potential and equivalent to the company's estimated maximum market share for the 6-month period.

FACTOR

9.

MARKET RESEARCH

CASE STUDY

Deborah Andrews works as the Management Accountant of Revlon which manufactures and sells cosmetic & skin care products to retailers & department stores in more than 100 countries around the world. Every year, the company's policy is to increase the price of all products in the development and growth phases of their life cycle. Generally, a product passes through four (4) phases of its life cycle. It is conceived and eventually born (phase 1). It then grows as it gradually gains in buyer acceptance (phase 2). Eventually it matures as it attains full buyer acceptance (phase 3) and then it dies as it is discarded for something better (phase 4). In preparing the revenue forecast for these products, Deborah has taken into account the planned price increase which is expected to boost sales revenue for the company by 10%.

FACTOR

13. THE FIRM'S PRICING POLICY

CASE STUDY

A major issue facing all of us at the moment is the Australian Government's decision to introduce the carbon tax which came into effect on 1 July 2012. According to the Federal Government, Australia needed to address **climate** changes immediately or face greater risks of enduring even more extreme weather conditions such as bigger bushfires, harsher storms and devastating floods. The Government responded by putting a price on carbon **pollution** in a bid to reduce greenhouse gas emissions. While this tax will be paid only by the top 300 or so businesses in the country and not by householders or small businesses, much of the tax will be passed on to the individual consumer in the form of increased prices, particularly for electricity. Jane Harrison is the Financial Accountant of Energy Australia. In preparing the company's sales revenue budget for the financial year ended 30 June 2013, she has taken into account the affect that the carbon tax will have on the company's sales revenue by adding an extra 9% onto the figures for next financial year. She has based this increase on the assumption made by the Commonwealth Treasury that households will be charged, on average, an extra \$9 for every \$100 of electricity consumed.

FACTOR

6. SUSTAINABILITY TRENDS

CASE STUDY

The Smith's Snackfood Company produces and sells a range of salty snack foods, its biggest seller in Australia being its potato chip range. Competitive intelligence revealed that their strongest **rival** in the industry, Kettle Foods, is planning on releasing a baked potato chip range next financial year. This new product has already received some positive attention from the Health Food industry due to having a lower fat content than standard chip varieties which are fried. With consumers being more health conscious these days continuing to switch to healthier snackfood alternatives, Sally Tims, the Financial Analyst at Smith's, knows that this move by Kettle Foods will more than likely lead to a downturn in the revenue expected by Smith's from the sale of its potato chip range. Smith's are busy working on a healthier wholegrain chip variety called 'Grain Waves', but it won't hit the market until the year after next. In preparing the revenue budget for next year for each of the company's brands, Sally will decrease the sales revenue for the potato chip range by 5%.

FACTOR

8.

COMPETITOR'S PLANS

CASE STUDY

Peter Jackson works for a company which specialises in the manufacture of LCD screens. LCDs (Liquid Crystal Displays) contain polarised glass which is then coated with crystals through which an electric current is passed to form an image. This year the company invested a large amount of money in a new type of **technology** that will revolutionise the way these screens are made. Not only will it cut production time down by 45%, it has the ability to convert a cheaper type of glass into this high quality polarised glass that will perform the same function compared with its more expensive counterpart.

Next year, this new technology will be completely up and running and as such, Peter has forecasted an increase in the company's sales revenue for next year. The resultant cost savings from the use of this new technology are expected to boost the company's bottom line and some of it will also be passed on to the consumer in the form of lower prices. This is expected to lead to a significant increase in the demand for this product by companies who purchase this product to make televisions & computers.

FACTOR

5.

TECHNOLOGICAL TRENDS

CASE STUDY

Ben Smith is the Financial Accountant of a car dealership in Sydney. He is in the process of preparing the company's sales budget for next financial year. **Interest rates** are currently at an all-time low and economists have predicted them to remain fairly flat over the coming year.

Based on this assumption, Ben has forecasted an increase in the dealership's sales revenue from the sale of new cars. Generally, lower interest rates mean that consumers have more disposable income to spend on things like new cars which are considered more of a luxury item during times of economic downturn.

FACTOR

2.

GENERAL ECONOMIC TRENDS

(i.e. those affecting all industries)

CASE STUDY

Lana Evans owns a child care centre in Picton. She is in the process of preparing her fees income budget for next financial year and remembered hearing something about the Federal **Government** wanting to introduce a child care rebate. After speaking to someone from DEEWR (The Department of Education, Employment and Workplace Relations), Lana found out that effective 1 July next year, parents with children in a registered child care facility will be entitled to receive 50% of any out-of-pocket expenses back from the Government. Lana knows from being involved with various parenting committees in the area that getting half of the child care fee back from the government would make it worthwhile for many stay-at-home parents to return to work. As a result, Lana has decided to employ three (3) extra carers in the 0-2s room and will bump up her sales revenue forecast by 10% to take into account the expected increase in the number of enrolments at her centre.

FACTOR

7. POLITICAL or LEGAL EVENTS

CASE STUDY

Adrian West owns and operates a Sydney bus company.

Yesterday, Adrian read an article in The Sydney Times newspaper which predicts the recent fall in the value of the Australian dollar versus the U.S. dollar to drive **domestic fuel prices** up in the short- to medium-term. The article went on to say that to counteract this predicted increase in the price of petrol, more and more people will probably opt to take public transport to work instead of driving their car. In preparing the company's revenue forecast for the coming year, Adrian has taken these changes in personal travel into account because they are predicted to lead to a slight increase in the demand for his bus service to and from the City which will lead to an overall increase in his service fee income.

FACTOR

3.

INDUSTRY-SPECIFIC ECONOMIC TRENDS

(i.e. those affecting the industry within which the firm operates)

Disclaimer

Please note:

All of the case studies used to illustrate each of these factors are fictitious. Although they may be based on real companies, the people in these case studies as well as any information provided about these companies and any related past or future events have been made up. They are and will continue to be used for educational purposes only.

Activity Findings

Did you notice how in each case study...

1. Either the **price** or the **quantity** of the product was influenced by one or more of our relevant factors, hence why the sales forecast had to be revised (either up or down).
2. A budget was being prepared by different types of **companies** operating in all different types of **industries**.
3. The budgeting **role** belonged to a different person (e.g. small business owner & Financial Analyst).
4. Different **sources of data / information** were used to prepare the sales revenue forecast.

Sales budget preparation

P PRICE \times **Q** QUANTITY

a. SALES BY PRODUCT

Est. sales volume (units) x Est. sales price (\$) = Est. total sales (\$)
(PRODUCT 1 volume) x (PRODUCT 1 price)

b. SALES BY PERIOD

Est. sales volume (units) x Est. sales price (\$) = Est. total sales (\$)
(PERIOD 1 volume) x (PERIOD 1 price)

c. SALES BY PRODUCT and PERIOD

Est. sales volume (units) x Est. sales price (\$) = Est. total sales (\$)
(PRODUCT 1; PERIOD 1 volume) x (PRODUCT 1; PERIOD 1 price)

d. SALES BY AREA

Est. sales volume (units) x Est. sales price (\$) = Est. total sales (\$)
(AREA 1; PERIOD 1 volume) x (AREA 1; PERIOD 1 price)

Fees income budget preparation

$$P_{\text{PRICE}} \times Q_{\text{QUANTITY}}$$

- Est. sales volume (units) = Hours of work
- Est. sales price (\$) = Hourly rate
- Est. total sales (\$) = Total fees income

This week's homework

- Read chapter 3 → Revenue and Sales Budgets
- Complete homework questions (chapter 3)
(ref. STUDENT ONLINE STUDY GUIDE)



**You are now ready to start the
next lesson on:**

Chapter 4

Operating Budgets

(non-manufacturing)

