

Budget Preparation

Editorial

Last month I commenced a theme of managerial finance with an article on Planning for Profit.

This month sees the first of a series of case studies to aid your continuing professional development. These will be based on an SME with a turnover of approximately £3.2m per year and profits of £350,000. It has an investment of £1.8m.

Once again enjoy your reading.

Dr Philip Dunn

Editor

Budget Preparation

Castout Ltd manufactures sea fishing rods. It has three main products, H1, H2 and H3. The information below relates to their plans for three months ended 31 March 2006.

		Product		
		H1	H2	H3
Sales Units	Jan	1,200	950	1,300
	Feb	1,350	1,150	1,230
	Mar	1,350	1,150	1,300
Opening Stock	1 Jan	1,300	1,150	1,250
	31 Mar	1,500	1,300	1,350
Selling Prices		£80	£68	£70

Standard Labour Specification (standard hours per unit)

Product		Cost Centre			Total
		C100	C110	C120	
H1	H1	2.5	2.0	0.5	5.0
	H2	2.8	1.2	0.5	4.5
	H3	2.2	2.0	0.3	4.5

Standard rate per hour £7

Standard Material Specification (material common to all three products)

		Product		
		H1	H2	H3
Units of material per unit of output		1.5	1.25	1.3
Cost per unit of material: £12				
Projected stock of material	1st January			5,000 units
	31st March			5,100 units

Overheads

	Cost Centre		
	C100	C110	C120
Variable Production Overhead	£37,500	£25,600	£15,200
Fixed Production Overhead (allocated/apportioned)	£25,800	£16,700	£9,900

Other Costs

Admin selling and distribution			£52,000
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You are required to prepare the following Budget Report for Castout Ltd for the quarter ended 31 March 2006.

- Sales and budget - showing volume and value
- Production budget (units)
- Material usage budget (units)
- Material purchases budget (value)
- Labour budget

- (f) Overhead budget to determine fixed and variable overhead recovery rates for the period
 (g) Finished stock budget (units and valuation)
 (h) Budget operating statement for period

Castout

Budget Report for the Quarter Ended 31 March 2006

(a) **Sales budget (by volume and value)**

	Product			Total
	H1	H2	H3	
Jan	1,200	950	1,300	
Feb	1,350	1,150	1,230	
Mar	<u>1,350</u>	<u>1,150</u>	<u>1,300</u>	
Units	<u>3,900</u>	<u>3,250</u>	<u>3,830</u>	
Selling price by unit	£80	£68	£70	
Turnover	<u>£312,000</u>	<u>£221,000</u>	<u>£268,100</u>	<u>£801,100</u>

(b) **Production budget**

	Product		
	H1	H2	H3
Sales (a)	3,900	3,250	3,830
Closing stock projection	<u>1,500</u>	<u>1,300</u>	<u>1,350</u>
	5,400	4,550	5,180
Less: Opening stock projection	<u>1,300</u>	<u>1,150</u>	<u>1,250</u>
Production (units)	<u>4,100</u>	<u>3,400</u>	<u>3,930</u>

(c) **Material usage budget (units)**

Material common to all products

	Product			Total
	H1	H2	H3	
Production (b)	4,100	3,400	3,930	
Material usage per unit of output	<u>1.5</u>	<u>1.25</u>	<u>1.3</u>	
Material usage	<u>6,150</u>	<u>4,250</u>	<u>5,109</u>	<u>15,509</u>

(d) **Material purchases budget (units and value)**

Material usage (c)	15,509
Closing stock projection	<u>5,100</u>
	20,609
Opening stock projection	<u>5,000</u>
Purchases (units)	<u>15,609</u>
Standard purchase price per unit of material	£12
Purchases	<u>£187,308</u>

(e) **Direct labour budget**

Standard hours required per cost centre

Product	Production (b)	Cost Centre			Total
		C100	C110	C120	
H1	4,100	10,250	8,200	2,050	20,500
H2	3,400	9,520	4,080	1,700	15,300
H3	3,930	<u>8,646</u>	<u>7,860</u>	<u>1,179</u>	<u>17,685</u>
Hours		<u>28,416</u>	<u>20,140</u>	<u>4,929</u>	<u>53,485</u>
Direct Labour Cost (@ £7 / hr)		<u>£198,912</u>	<u>£140,980</u>	<u>£34,583</u>	<u>£374,395</u>

(f) **Production Overhead Budget**

	Cost Centre			Total
	C100	C110	C120	
Standard hours (e)	28,416	20,140	4,929	
	£	£	£	
Variable overhead	37,500	25,600	15,200	78,300
Variable overhead recovery rate	1.32	1.27	3.08	
Fixed overhead	25,800	16,700	9,900	52,400
Fixed overhead recovery rate	0.91	0.83	2.01	

(g) **Finished stock budget**

Here we need to determine the standard cost for unit for each product. The stock will be valued at production cost.

	Product		
	H1	H2	H3
	£	£	£
Direct labour (note 1)	35.00	31.50	31.50
Direct material (note 2)	18.00	15.00	15.60
Variable overhead (note 3)	7.38	6.76	6.37
Fixed overhead (note 4)	<u>4.94</u>	<u>4.55</u>	<u>4.26</u>
	<u>65.32</u>	<u>57.81</u>	<u>57.73</u>

Notes:

1 Example calculation:

H1 Total standard labour hours per unit = 5.0 (given) @ £7/hr = £35.00

2 Example calculation:

H1 Units of material per unit = 1.5 (given) @ £12/unit = £18.00

3 Example calculation:

	C100	Cost Centre C110	C120	Total
Standard hours per unit	2.5		2.0	0.5
Variable overhead recovery rate (f)	£1.32		£1.27	£308
Variable overheads recovered	£3.30		£2.54	£1.54
				£7.38

4 as for variable overheads (note 3) using fixed overhead recovery rates from (f)

Finished stock valuation	H1 £	H2 £	H3 £	Total £
Opening stock	84,916	66,482	72,163	223,561
Closing stock	97,980	75,153	77,936	251,069

(h) Budgeted Operating Statement for Quarter Ended 31 March 2006

	£	£
Sales (a)		<u>801,100</u>
Opening stock raw materials (@ £12)	60,000	
Add purchases (d)	<u>187,308</u>	
	247,308	
Less: closing stock raw materials (@ £12)	<u>61,200</u>	
Cost of raw materials used		186,108
Direct labour (e)		374,395
Variable overhead (f)		78,300
Fixed overhead (f)		<u>52,400</u>
Cost of production		691,203
Opening stock of finished goods (g)	223,561	
Closing stock of finished goods (g)	<u>251,069</u>	
Finished goods stock adjustment		<u>(27,508)</u>
Cost of goods sold		<u>663,695</u>
Gross profit		137,405
Admin, selling and distribution costs		<u>52,000</u>
Net profit for period		<u>£85,405</u>