6.4 Budgeting

Name: _____ Class: _____ Date: _____ **Total: 14 marks**

KEY WORDS budget • flexible budget

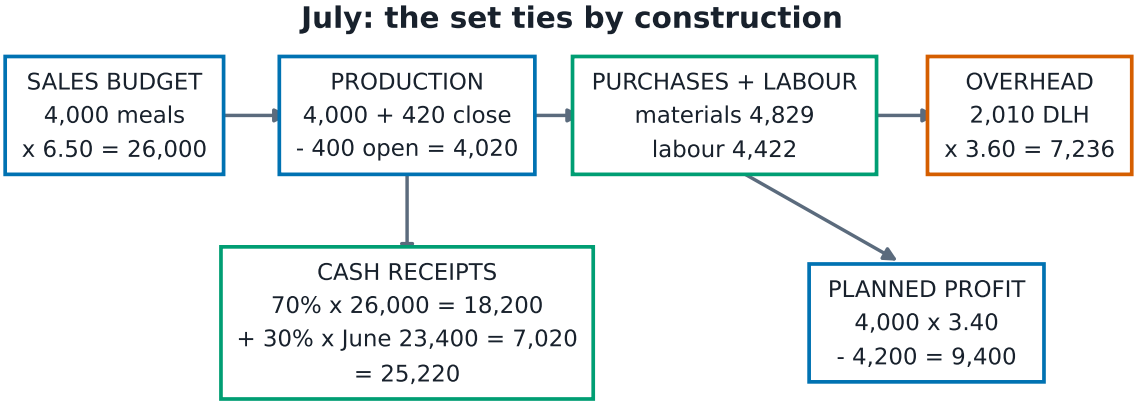
Objective

Build a tied operating budget set; convert sales to cash with the collection pattern; model inventory policy; read the behavioural effects.

1 Key knowledge and worked examples

■ The set ties

Sales → production (± inventory policy) → purchases/labour/overhead → cash (collection pattern) → profit. Cash is not lagged profit: different measure, different calendar.



June sales 3,600 meals = 23,400; August planned 4,200 meals (closing-inventory 10% rule)

Each box consumes the previous one

■ Worked example. July at Nimbus Kitchen

Production 4,000 + 420 − 400 = 4,020 ✓; purchases £4,829 ✓; cash £25,220 ✓; planned profit £9,400 ✓.

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2 Practice

Sales forecasts (units): May 900, June 1,000, July 1,200, August 1,100. Price £18. Collections: 75% in the month, 25% the following month. Closing finished inventory: 20% of next month's sales. Materials £4 a unit; the production manager is bonused on hitting the production budget.

2.1 Compute July's production budget. [3]

2.2 Compute July's cash receipts. [3]

2.3 Compute July's materials purchases in pounds (ignore materials inventory). [2]

2.4 August demand collapses to 700 units. Compute the honest production budget, then explain in two lines the parking that the manager's bonus invites. [4]

2.5 In two lines: why does the cash budget differ from the profit budget even in a steady month? [2]

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Solutions

2.1

- Closing = 20% × 1,100 = 220; opening = 20% × 1,200 = 240.
- Production = 1,200 + 220 − 240.
- = 1,180 units.

2.2

- July sales £= 1,200 × 18 = £21,600; June = £18,000.
- 0.75 × 21,600 + 0.25 × 18,000.
- = £20,700.

2.3

- 1,180 × 4.
- = £4,720.

2.4

- Closing = 20% × 700 = 140; opening 220.
- Honest production = 700 + 140 − 220 = 620 units.
- The bonus invites producing toward 1,180 anyway: ~560 extra units park fixed cost in inventory.
- Reported profit rises while cash falls – the absorption trap meets the target (unit 6.3).

2.5

- Different measure: receipts/payments vs revenue/expense.
- Different timing: the 25% in transit and payment lags.