**Lecture 7 notes - Cash Budget /cash flow forecast [homework questions]**

**Question 1**

Mary decides to open a shop with initial capital of £10,000. She anticipates that sales for the first 3 months in 2023 will be:

1. January £10,000
2. February £11,000
3. March £12,000
4. She will allow 10% of her customers one month’s credit, everybody else will pay cash.
5. She anticipates that her monthly purchases will be 50% of sales value.
6. She will pay her creditors 60% in the month of purchase and 40% in the following month.
7. General expenses will be £500 per month.
8. Capital outlay will occur in February and March and will be £500 and £600 respectively.

**You are required to prepare a cash budget for Mary for January, February and March, 2023**

**Answer**

Mary

Cash budget for the 3 months to March 2023 [in £s]

|  |  |  |  |
| --- | --- | --- | --- |
| Months | January | February | March |
| Cash inflows |  |  |  |
| Capital | 10,000 |  |  |
| Cash sales [90% or 0.9 of current month sales] | 9,000 | 9,900 | 10,800 |
| Credit sales [10% or 0.1 of I month ago sales] | --- | 1000 | 1100 |
| Total cash inflows | 19,000 | 10,900 | 11,900 |
| Cash outflows |  |  |  |
| Cash purchases [50% of sales x 0.6] | 3,000 | 3300 | 3600 |
| Credit purchases [50% of I month ago sales x 0.4] | -- | 2000 | 2200 |
| General expenses | 500 | 500 | 500 |
| Capital outlay |  | 500 | 600 |
| Total cash outflows | 3500 | 6300 | 6900 |
| Net cash flows | 15500 | 4600 | 5000 |
| Opening balance | --- | 15500 | 20100 |
| Closing cash balance. surplus/[deficit] | 15500 | 20100 | 25100 |

**Q 2 HOMEWORK – please attempt before next lecture**

**SAP Ltd**

The following information relates to SAP Ltd, a small manufacturer. The company has a highly seasonal trade, with the bulk of sales being made at Christmas and Easter. Because SAP Ltd foresees a poor Christmas period the finance director has asked you to consider the cash flow position up to Easter (April) 2023

The balance at the bank at the beginning of January 2023 is expected to be £1,000. Details in respect of the months November 2022 to April 2023 are given below.

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | Nov | Dec | Jan | Feb | Mar | Apr |
|  | £ | £ | £ | £ | £ | £ |
| Sales | 28,000 | 42,000 | 30,000 | 32,000 | 45,000 | 40,000 |
| Purchases | 29,000 | 20,000 | 18,000 | 21,000 | 34,000 | 12,000 |
| Wages | 3,000 | 3,200 | 3,600 | 4,000 | 3,800 | 3,700 |
| Manufacturing overheads | 2,700 | 2,800 | 2,900 | 3,000 | 3,050 | 2,730 |
| Administration overheads | 950 | 900 | 1,100 | 1,150 | 1,200 | 1,125 |
| Selling and distribution overheads | 2,150 | 4,200 | 2,500 | 2,400 | 4,500 | 2,000 |
| Plant and machinery purchases |  |  | 8,000 |  |  |  |
| Corporation Tax |  |  | 6,000 |  |  |  |
| Dividends |  |  |  |  | 4,000 |  |
| New issue of debentures |  |  |  |  | 20,000 |  |

The following information is also available.

1. SAP Ltd takes two months credit before paying its suppliers.
2. Three-quarters of the wages are paid in the month in which they are earned, and the remaining quarter in the month following.
3. Manufacturing, administration and selling and distribution overheads are paid in full in the month following that in which overheads are incurred. Manufacturing overheads include depreciation amounting to £400 each month.
4. Plant and machinery purchases, corporation tax and dividends will be paid in the months shown. The plant and machinery are estimated to have a useful life of four years.
5. The proceeds of the new issue of debentures will be received in March 2023.
6. SAP Ltd has an agreed overdraft limit with its bank of £16,000
7. 20% of invoiced sales relate to cash transactions. 40% of credit customers pay in the month they are invoiced and the remaining 60% pay in the following month. No bad debts are expected.

**Required**

**a) Prepare for SAP Ltd a projected cash budget in columnar form for each of the months of January, February, March and April 2023 showing clearly the balance at the end of each month.**

**b) State what courses of action you think might be available to the management of SAP Ltd in respect of the company’s projected cash position.**

**Q 3 HOMEWORK – WILL BE USEFUL IF THIS CAN BE DONE BEFORE THE LECTURE.**

**a) Describe the major practical differences between a cash budget and**

**other budgets within a business’s budgetary control system.**

b) The following information relates to W Limited in 2022 and comes from its various budgets, management decisions, activities and expectations during the year:

It has agreed to buy new machinery in July for £200,000 and a finance

arrangement to pay for it in 5 equal monthly instalments, the first due on

the date of purchase.

The machinery attracts a government grant worth 15% of its purchase

price, on evidence that the machinery instalments are being made on time.

This is expected in 3 equal monthly instalments from August.

Rent payable for their premises is £24,000 per year, payable quarterly in

advance. The next payment is due in July.

Purchases of Raw Materials are budgeted to be £10,000 per month with a

variety of payment terms, but averages out as 40% is paid in the current

month and 60% in the month afterwards.

Other overheads and expenses are budgeted in each month, as follows:

* Wages of £5,000, payable in the month earned
* Depreciation of £150 in July, and £450 in each following month, applied in the relevant month
* Electricity, Water and Gas usage of £1,350 each month settled monthly
* Administration costs of 5% of each months’ receipts from sales, and paid in the following month.

Cash sales are treated as fully paid at the time of purchase and W Ltd.’s

standard credit term for its customers is full payment by the end of

the following month. The pattern of sales is expected to be:

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **£** | **May** | **June** | **July** | **August** | **September** | **October** |
| **Cash** | 12,000 | 14,000 | 16,000 | 18,000 | 20,000 | 22,000 |
| **Sales** |
|  |  |  |  |  |  |
| **Credit** | 25,000 | 26,000 | 27,000 | 28,000 | 29,000 | 30,000 |
| **Sales** |
|  |  |  |  |  |  |
| **Monthly** | 37,000 | 40,000 | 43,000 | 46,000 | 49,000 | 52,000 |
| **Sales** |  |  |  |  |  |  |

The bank balance on 30 June is budgeted to be £25,000 (in funds). An

overdraft fee of £20 is charged when any end-of-month bank balance is

overdrawn, and any end- of-month positive bank balance (that is, it is not

overdrawn) attracts 1% interest.

Bank fees and interest, where arising, are applied in the following month.

**TASK for part b)**

**Using the information given above relating to W Limited, prepare a**

**cashflow forecast / cash budget for the four months from July to October**

**2022. All calculations should be presented to the nearest whole £**

**Based upon the scenario and your cash budget in 4b) above, what conclusions can be drawn and therefore what recommendations can be given to W Ltd**

**Question aims**

**To test candidates’ ability to:**

**c)**