Format of Balance Sheet (contd...)

- The liabilities side of the balance sheet shows the sources of finance employed by the business.
- The assets side of the balance sheet shows how funds have been used in the business.

For preparing the projected balance sheet at the end of year n+1, we need information about the following:

- The balance sheet at the end of year n.

Format of Balance Sheet

Liabilities	Assets
Share Capital	Fixed Assets
Reserves & Surplus	Investments
Secured loans	Current assets,
Unsecured loans	loans & Current liabilities
advances & provisions	Miscellaneous expenditures & losses

Projected Balance Sheet

- The balance sheet, showing the balance in various asset & liability accounts, reflects the financial condition of the firm at a given point of time.

Cash Flow Statement (contd....)

- Opening balance of cash in hand & at Bank
- Net surplus/deficit (A-B)
- Closing balance of cash in hand & at bank

Cash Flow Statement (contd....)

Disposition of Funds : Total (B)

1. Capital expenditure for the project
2. Other normal capital expenditure
3. Increase in working capital
4. Decrease in secured medium & long term borrowings
5. Decrease in unsecured loans & deposits
6. Decrease in bank borrowings for working capital
7. Increase in liabilities for deferred payment to machinery suppliers
8. Increase in investments in other companies
9. Interest on term loans
10. Interest on bank borrowings for working capital
11. Taxation
12. Dividends (Equity, Preference)
13. Other Expenditure

Cash Flow Statement

Source of Funds :Total (A)

1. Share Issue
2. Profit before taxation with interest added back
3. Depreciation provision for the year
4. Development rebate reserve
5. Increase in secured medium & long term borrowings for the project
6. Other medium/long term loans
7. Increase in unsecured loans & deposits
8. Increase in bank borrowings for working capital
9. Increase in liabilities for deferred payment to machinery suppliers
10. Sale of fixed assets
11. Sale of investments
12. Other income

Financial Break even analysis: Example

Since he cash flow cost for last 10 years, its present value at a discount rate of 12% is:

PV (cash flows) =

= (.30 sales -0.25 million) × PVIF (10 years 12%)

= (.30 sales -.25 million) × 5.650

= 1.695 sales -1.4125

The project breaks even in NPV terms whose the present value of there cash flows equals the initial investment of the 20 million. Hence, the financial break even occurs when.

PV (Cash flows) = Investment

∴ 1.695 sales -1.4125 million = 20 million

Sales = 12.63 million

Financial Break even analysis: Example

1. Variable Cost: 60% of sales
2. Contribution Margin: 40% of sales
3. Fixed cost: Tk. 3 million (Dep. 2 million included)
4. Pretax profit = $(0.40 \times \text{sales})$ -Tk 3 million
5. Tax (25%) = $0.25\ \{(0.40 \times \text{sales})$ -Tk 3 mil$\}$
6. Profit after tax = $0.75\ \{(0.40 \times \text{sales})$ – Tk.3 million)
7. Cash flow= Tk 2 million + $0.75\{(0.40 \times \text{sale})$ – Tk.3 million)$\}$

   = Tk 2 million +$0.30 \times$ sales -2.25 million

   = 0.30 sales - 0.25 million.

Financial Break even analysis

- The focus of financial break even analysis is an NPV & not accounting profit. Financial break even point identifies the level of sales where the project will have a zero NPV.

Break Even Analysis

- Break-even analysis refers how much should be produced & sold at a minimum to ensure that the project does not lose money.
- The minimum quantity at which loss is avoided is called break even point. The break even point may be defined in accounting terms or financial terms.

Profitability projections (contd....)

K. Other Income

L. Preliminary expenses written off

M. Profit/loss before taxation (J+K-L)

N. Provision for taxation

O. Profit after tax (M-N less , dividend on Preferred capital & Equity capital)

P. Retained profit

Q. Net cash accrual (P+I+L)

Profitability projections (contd...)

F. Expected Sales

G. **Gross profit before interest (F-E)**

H. Total financial expenses

I. Depreciation

J. **Operating Profit (G-H-I)**

Profitability projections

- The estimates of working results may be prepared along the following lines:

A. Cost of Production

B. Total administrative expenses

C. Total sales expenses

D. Royalty & know-how payable

E. Total cost of production (A+B+C+D)

Margin Requirement

- While there is no fixed formula for determining the margin amount, the ranges within which margin requirements for various current assets lie are as follows:

Current Assets	Margin
Raw Materials	10%-25%
Work-in-process	20%-40%
Finished goods	30%-50%
Debtors	30%-50%

Working Capital requirement & its financing (contd..)

2. The principal sources of working capital finance are :

- Working capital advances provided by commercial banks
- Trade Credit
- Accruals & provisions
- Long term sources of financing

3. To obtaining working capital advances from commercial banks, there are certain limits.

They are in two forms:

- The aggregate permissible bank finance is specified as per the norms of lending.
- Against each current asset a certain amount of margin money has to be provided.

Working Capital requirement & its financing

1. The working capital requirement consists of the following:

(a) Raw Material

(b) Stocks of goods in process

(c) Stocks of finished goods

(d) Debtors

(e) Operating Expenses

Factory Overheads

- The expenses on repairs & maintenance, rent, taxes, insurance on factory assets, & so on are collectively referred to as factory overheads. Repairs & maintenance expense depends on the state of the machinery- this expense tends to be lower in the initial years & higher in the later years. Rent, taxes, insurance etc. may be calculated at the existing rates. A provision should be made for meeting miscellaneous factory expenses.

Cost of Production

- Material cost
- Utilities cost
- Labor cost
- Factory overhead cost

Estimates of Sales & Production

The starting point for profitability projections is the forecast of sales revenues. ... borne in mind:

1. It is advisable not to assume a high capacity utilization level in the first year operation, in spite of simple technology. company may face raw material shortage, limited power, marketing problem etc. A reasonable assumption is ... percent of installed capacity in the 1st Year.

50-80 percent in the 2nd year.

80-90 percent from 3rd year onwards.

Deferred Credit

Sometimes supplier of plant & machinery may propose deferred credit facility under which payment for such purchase can be made over a period of time.

Incentive sources

The government & its agencies may provide financial support as an incentive to certain types of promoters or for setting up industrial units in certain locations in the form of seed capital assistance, capital subsidy, tax exemption etc.

Means of Finance

- Share Capital
- Term Loans
- Debenture capital
- Deferred credit
- Incentive sources
- Miscellaneous sources

Initial Cash Losses

Initial losses in the project cost generally affects –

1. Liquidity position
2. Impairs the operations.