From the budget to the investment

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ISBN-13:978-1484096987
ISBN-10:1484096983

INTRODUCTION

Understanding the principles of finance management is a key to the success of a company. It is important to know about the relationship between risk assessment and cash flow, and know the principles of budgeting and cash management. Financial management is a very complex area of business. That is the reason why I have organized this information into several parts.

The first part describes the basics of budgeting; this also includes an introduction to the management of budgets and performance.

The second part is about the principles of cash management and cash flow management, the handling of investments and available cash.

The third part is the most important in this book. Finance management is more than just understanding the sources of funds. It is important to know how you can affect the cash flow with debt financing and understand the meaning of the numbers of the reports and to analyze the impact.

Part four describes the term of the investment using formulas and explains how the numbers or the Net Present Value Internal Rate of Return. If you are not familiar with these numbers, it is easy to understand and you will see the influence of these values on your business. In this part, there is also an introduction to corporate restructuring and anti- takeover measures

In the fifth part of the overall risk and the nature of the risk is described. You get a view of a WBS (Work Breakdown Structure) and a description of the tools and techniques for risk assessment.

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TABLE OF CONTENTS

1 THE BASICS OF BUDGETING **8**

1.1 ESSENTIAL ELEMENTS FOR CREATING A SUCCESSFUL BUDGET 8
1.1.1 BUDGET TRAPS 8
1.1.2 THE SUCCESSFUL BUDGET FORMULA 9
1.1.3 BUILDING ON THE ASSUMPTIONS 9
1.1.4 RELEVANCE OF CONTROL 10
1.1.5 NET INCOME VS. CASH 10
1.2 STEPS AND PLANNING A BUDGET 10
1.2.1 ALLOCATION OF FUNDS 10
1.3 TYPES OF BUDGETS 11
1.3.1 SALES AND PRODUCTION BUDGET 11
1.3.2 HEAD OF DEPARTMENT BUDGETS 11
1.3.3 INVESTMENT BUDGET (LONG TERM) 11
1.4 POLICY OF THE BUDGET PLAN 11
1.4.1 SOCIALIZING, CONTACTS 12
1.4.2 UNDERSTAND AND COMPLY WITH BUDGETS 12
1.4.3 ADDRESSING REVENUE VARIANCES 12
1.4.4 COST CONTROL 13
1.4.5 EXAMPLE OF A BUDGET 13

2. MINI BUDGET **14**

2.1 PREPARATION OF A BUDGET 14
2.1.1 THE STEPS TO CREATE A PRODUCTION BUDGET 14
2.1.1.1 EXAMPLE OF A PRODUCTION BUDGET 14
2.2 MATERIALS AND PURCHASES 14
2.2.1 THE STEPS TO CREATE A MATERIAL AND PRODUCTION BUDGETS 15
2.2.1.1 EXAMPLE OF A MATERIAL PURCHASE BUDGET 15
2.3 THE WORKING BUDGET 15
2.3.1 THE STEPS FOR CALCULATING THE COST OF LABOR 16
2.3.1.1 EXAMPLE OF A WORKING BUDGET 16

3. THE ADMINISTRATIVE BUDGET **17**

3.1 COMPONENTS OF AN ADMINISTRATIVE BUDGET 17
3.1.1 EXAMPLE OF AN OPERATING BUDGET 17

4. THE BUDGET DECISION **20**

4.1 The administrative budget 20
4.2 The break-even formula 20
4.2.1Example of one break-even formula 20
4.3 The bottom-up approach 21
4.3.1 Example of a bottom- up approach with no profit 21
4.3.2 Example of a bottom-up approach with profit 22

5. CONTROL BUDGETS AND PERFORMANCE 23

5.1 The electronic spreadsheet 23
5.2 Changes to the budget 23
5.3 Steps to obtain a variance report 23
5.3.1 Example of a variance protocol 24
5.4 Impact Analysis 24
5.5 Budget performance 24

6. CAPITAL 25

6.1 Components of capital flows 25
6.1.1 Sources of cash 25
6.1.2 Decisive factors for debt financing 26
6.1.3 Factors relating to investments 26
6.1.4 Factors relating to re-investments 26
6.1.5 Capital use 26
6.1.6 Consequences of inadequate cash flow 26
6.2 The Cash Flow Management 27
6.2.1 Maximizing capital generation 27
6.2.2 Receipt of cash and cash equivalents 28
6.2.3 Withdrawals from account 28
6.3 Belated receipt 28
6.3.1 Ways to prevent delayed payments 28
6.4 Available Cash 28
6.5 Altman MDA 29
6.5.1 Example Altman MDA 30
6.6 Information for customers 30
6.7 Inventory management 30
6.8 Cash flow control 31
6.8.1 Basics of cash flow pro forma 31
6.8.2 Cash flow pro forma spreadsheet 32
6.8.2.1 Example of a cash flow pro forma spreadsheet 32
6.8.3 Total inflow 33
6.8.4 The operational capital payment 33
6.8.5 Total capital-outflow 33
6.8.6 Analysis of cash flow pro forma spreadsheet 33
6.8.7 Cost reduction program 34
6.9 The capital budgeting 34

6.9.1 CURRENT FINANCING 35
6.9.2 WORKING CAPITAL MANAGEMENT 35

7. FINANCIAL MANAGEMENT 38

7.1. SOURCES OF FUNDING 38
7,1.1 FUNDS 38
7.2 THE MAIN REASONS FOR RAISING CAPITAL THROUGH A PUBLIC STOCK OFFERING 39
7.3 SHARE ISSUES 39
7.4 BORROWING IN THE MARKET WITH THE HELP OF LOANS 39
7.4.1 SHORT-TERM BORROWINGS (BANK FINANCING) 40
7.4.2 CREDIT CRITERIA OF BANKS 40

8. CAPITAL RAISING AND FINANCING DECISIONS 41

8.1 TRANSFER OF CAPITAL 41
8.1.1 OPPORTUNITY COST OF CAPITAL 41
8.1.1.1EXAMPLE OF CALCULATING A RIR 42
8.1.2 FORWARD RATE 43
8.1.2.1 EXAMPLE OF CALCULATING A FORWARD RATE 43
8.1.3 THE FINANCIAL MARKETS 43
8.2 NOTES 44
8.2.1 BOND-TYPES AND CHARACTERISTICS 44
8.2.2 EVALUATION FACTORS OF BONDS 45
8.2.3 DETERMINING THE VALUES OF BONDS (PRESENT VALUE) 45
8.2.4 PRESENT VALUES OF AN ANNUITY 45
8.2.5 BOND YIELD TO MATURITY 46
8.2.6 ZERO COUPON BONDS 46
8.2.7 YIELD TO MATURITY ON ZERO COUPON BONDS 47
8.2.8 COMMON SHARES 47
8.2.9 PREFERENCE SHARES 48
8.2.10 RAISE CAPITAL 48
8.3 COST OF CAPITAL 49
8.3.1 CAPITAL ASSET PRICING MODEL (EQUILIBRIUM MODEL) 49
8.3.2 WACC WEIGHTED AVERAGE COST OF CAPITAL 49
8.4 DIVIDEND POLICY 50
8.4.1 CONSIDERATION IN THE DIVIDEND POLICY 50
8.5 TAX SAVINGS 51
8.5.1 CASH FLOW THROUGH DEBT 51
8.5.2 DISADVANTAGES OF DEBT 51
8.5.3 EQUITY FINANCING 52

9. FINANCIAL INSTRUMENTS 53

9.1 STOCK 53
9.1.1 BASIC CONCEPTS 53
9.1.2 INDICATORS AND SIGNALS 53

9.1.3 Stock Analysis 54
9.1.3.1 Stochastic 55
9.1.4 Complete market analysis 56
9.1.5 Order routing 57
9.1 6 Risk calculation 58
9.2 Bonds 59
9.2.1. Basic concepts 59
9.2.2 Kind of bonds 61
9.2.3. Calculations and effects 62
9.3 Fund 63
9.3.1. Basic concepts 63
9.3.2. Type of funds 65
9.3.3 Variables of funds 68
9.4 Derivative financial instruments 69
9.4.1. Basic concepts 70
9.5 The Black-Scholes model 75
9.5.1. Introduction 76
9.5.2. The variables of the option pricing models 76
9.5.3. The derivation of the formula 76
9.5.3.1 Sample Application 77
9.5.3.2. Breakdown of the formula 77

10. MANAGEMENT WORKING CAPITAL AND LIQUID RESOURCES 78

10.1 Financial planning rules 78
10.1.1 Forecasting and planning 78
10.1.2 Three elements of effective planning 79
10.1.3 Financial planning cycle 79
10.1.4 Financial planning models 79
10.1.5 Final goals 79
10.2 Current assets 81
10.2.1 The turnover rate in the camp 81
10.3 The ratio of days sales outstanding 81

11. FINANCIAL STATEMENTS AND ANALYSIS 82

11.1 Assets 82
11.2 Liabilities 82
11.3 Liquidity 82
11.4 Cash flow statement 83
11.5 Basic financial reporting, analysis and conditions 84

12. PURCHASES OF FIXED ASSETS 86

12.1 Factors that have an impact on the acquisition 86
12.2 Components of a capital budget 86
12.3 Sources of funding 86

13. THE USE OF CAPITAL BUDGET TOOLS **88**

13.1 COMPARISON 88
13.2 CURRENT VALUE 90
13.3 INTERNAL RATE OF REPAYMENT (IRR) 91
13.4 ACCOUNT MODELS 91
13.5 DIFFERENT TYPES OF PROJECTS 92
13.6 CASH FLOW MODELS 92

14. INVESTMENT ANALYSIS AND SELECTION **93**

14.1 DEREGULATION 93
14.2 ADVANCED PROJECT ANALYSIS 93
14.2.1 TOOLS FOR ADVANCED PROJECT ANALYSIS 94

15. CORPORATE RESTRUCTURING **95**

15.1 CLASSIFICATION OF MERGERS 95
15.2 FOUR MAIN VALUATION METHODS 95

16. MEASURES AGAINST TAKEOVERS **97**

16.1 THE PATH TO FINANCIAL RUIN 98

17. FINANCIAL RISK MANAGEMENT **99**

17.1 RISK IDENTIFICATION 99
17.2 RISK ASSESSMENT 99
17.2.1 FOUR KEY INPUTS 100
17.2.2 TOOLS AND TECHNIQUES FOR RISK ASSESSMENT 101
17.2.3 RESULTS OF QUANTITATIVE ANALYSIS 104
17.2.4 RISK MEASUREMENT METHODS 105
17.2.5 STRATEGIES IN RISK MANAGEMENT 106

Part 1 Budget Management

1 The basics of budgeting

Budgeting is all about the planning and management of capital flows. This gives you an overview of the financial situation of the company or for private events such as your household. The budget is a document of the actual master scheduler. The role of budgeting consists of:

- Planning to ensure an endurable profitable growth
- Allocation of resources to achieve the goals
- To achieve control of resources to the targets

The benefits are the most accurate budget. This is essential to

- Improve the financial performance
- Guarantee a sufficient cash flows (support the solvency)
- Cover the expenses by the income (compensation of revenue and expenditure)

The purposes of a balanced budget are

- Increase in sales
- Variation of income (various sources)
- Capacity building indirectly
- Capacity building directly (new machines)

1.1 Essential elements for creating a successful budget

There are five elements that are needed when creating a budget

- Budget afflictions
- Successful budget formula
- Building on the assumptions
- Relevance of control
- Net income vs. cash

1.1.1 Budget traps

Take care of the five listed traps when you wish to make a successful budget.

Budget fear

- Problem fear of numbers, where performance is measured. These figures are measurable and verifiable.

- Solution it is not the company that you are doing it is for other people

Boccia fallacy

- Problem make a solid assumption about the size of the future and the budget of this size to adapt
- Solution jump ball technology , the individual elements of the budget are as flexible elements to be considered , which can no longer appear

Edifice Complex, the bigger the better

- Problem have the conviction that a budget is a monument
- Solution from the bottom to the top of the budget work (over the proceeds ,costs)

Recipe relapse

- Problem based on overconfidence. They know what parts the budget is, but do not take the time to add all the necessary parts.
- Solution Consider the budget , part for part

Fully loaded

- Problem all costs weighing on your shoulders
- Solution look to get the effects of direct / fixed

1.1.2 The successful budget formula

A proper budget should be prepared taking into account the following factors

- Validity of the assumptions
- Accuracy of forecasts
- Answerable purpose recognition of a budget
- Ability to respond to changes
- Controllability of a budget

1.1.3 Building on the assumptions

Be careful that the forecasts are as accurate as possible within a budget. Use the following sources to create an accurate budget.

- Internal budgets of the past

- Internal existing budgets
- Internal budgets based on future assumptions
- External budgets from the past
- External current existing budgets
- External budget based on future assumptions

1.1.4 Relevance of control

The following items are part of an effective control over your budgeting

- Financial and sales planning
- Efficient and effective management
- Alignment and focusing of business

1.1.5 Net income vs. cash

Factors that may cause a difference between the net profit and loss account and the cash balance

Buying on credit	you must pay later
Sale on credit	you will get you the money later
Depreciation	you not spend any money for keeping records
Taking the inventory	may need to apply more / less material

1.2 Steps and planning a budget

To obtain an accurate budget, the following steps are necessary

- Development income / expense forecast
- Converting the forecast in planning (transformation)
- Monitoring actual performance vs. budget (tracking)

The advantages of the planning of the budget process are :

- The operational strategy = turning strategy into operation
- Coordinating sales and production
- Identifying and solving problems profit
- Establishing performance standards

1.2.1 Allocation of funds

Direct sales rose	=	advertising, sales expenses, new hardware
Directly with sales	=	change in sales, the size vary the production crew
Construction indirect power	=	more staff, no directly increase

- Capacity building
  Directly = new store (big investment) refer to the quantities sold

1.3 Types of budgets

The most common types of budgets are listed below:

- To plan sales and production sites to direct budget costs
- Departmental budgets to plan and control the expenses
- Investment budget to identify long-term needs and to fund

1.3.1 Sales and production budget

These provide information for

- Sales forecasting, distribution costs and estimated volume
- Production costs, material costs, direct labor costs

The production box are related to the direct costs

1.3.2 Head of department budgets

- Difference of sales and production departments to develop approaches
- Zero budgeting (budget from the ground)
- Overhead Budget (historical budget)

1.3.3 Investment Budget (long term)

This budget describes the nature of the expenditure. If you are planning for example, to invest in vehicles and buildings, your funds will be set for a long time.

1.4 Policy of the budget plan

In this section, the following points will be discussed, which are essential for the success of a budget

- What is important to know concerning the overview? Budget philosophy and approach to value creation, operational support and end results
- As the requirements vary in accuracy between the individual companies, the calculation is done in terms of sales, cost estimates and geographical areas on productive units, offices and product lines
- The prevention of street fights, different tactics budget, a necessary margin (bottom up), from top to bottom and the prevention of

imagination structures

- The Anticipated from a safe distance is also important (% which can be reduced without compromising the budget).

1.4.1 Socializing, contacts

Process safety review concerning important elements with other executives, including also

- Maintain contact with peers
- Discussions with your staff
- Maintaining contact with your boss
- Support the budget plans (Keep out of rumor)
- Check whether additional resources are required, before the budget is prepared

Your options

- Prepare yourself
- Presenting your proposals
- Revision of the budget interface with other budget holders

1.4.2 Understand and comply with budgets

These activities will help you to discover deviations from budgets and to take appropriate measures

- Generate revenues in steps, monitoring of expenditure
- Using variance reports for monitoring and compliance budgets
- Variance reports contain 3 columns (budget, value, difference)
- Monitor the process on a regular basis

1.4.3 Addressing revenue variances

There are several reasons for revenue variances

- Deviations are small and show no clear pattern
- Revenues are significantly higher than budgeted
- Sales caused by the competition
- Decline significantly and cannot be restored quickly

Simply observe further

- Revenue (continued) slightly up / down, no particular pattern
- A major campaign significantly boosts sales (check capacity and cash flow)
- A slump in the client industry brings revenue decline (revise any associated circuit boards)

- cheaper alternatives bring revenue decline (consider lowering the price)

1.4.4 Cost control

Effective governance helps to detect differences in the costs. This is important because expenses can vary by many influences.

- Prices change according to the budget set
- Quantities purchased differ from projected amounts
- Goods or services are faster / purchased later than planned
- Price (discounts, alternative suppliers)
- Volume (smaller amounts)
- Timing (purchase, if necessary, low inventories)

1.4.5 Example of a budget

Position	*Expenses planned*	*Expenses real*	*Difference*	*Revenues planned*	*Revenues real*	*Difference*
Work	20‘000‘000	20‘000‘000	0			
Material	15‘000‘000	12‘000‘000	-3‘000‘000			
Energy	5‘000‘000	6‘000‘000	+1‘000‘000			
Rent	3‘000‘000	2‘500‘000	-500‘000			
Marketing	5‘000‘000	4‘000‘000	-1‘000‘000			
Invest	15‘000‘000	12‘000‘000	-3‘000‘000			
Int. paid	2‘000‘000	2‘000‘000	0			
Dividende	2‘000‘000	1‘500‘000	-500‘000			
Sales				60‘000‘000	55‘000‘000	-5‘000‘000
Interest				3‘000‘000	3‘000‘000	0
Total	67‘000‘000	60‘000‘000		63‘000‘000	58‘000‘000	

This table shows , the biggest problem is not the cost but the revenue fell by 10%.

Consequences:

- Increase sales by at least 10 %
- Increase the price of the products
- Lower labor costs
- Take on a new loan from the bank , or if this is not possible , issue a bond of the company

If you issue a bond , then you need not only to calculate the cost for the issue , but also the annual interest payments on the bonds considered

2. Mini budget

Creating an effective budget is a very complex and difficult task . Therefore, it is easier to design and understand a budget for smaller and simpler accounts. These includes

- Production Budget
- Materials and purchases
- Labor Budget

2.1 Preparation of a budget

The production budge is to forecast and monitor the revenues generated by the sale activities. The factors for this kind of budget are listed below:

- products
- price
- quantity
- turnover
- total revenue

2.1.1 The steps to create a production budget

- List of all items that are sold by the business create
- The unit price for each item set
- Estimation of the amount of the single items
- Calculation of the revenue generated by each element
- Aggregate turnover

2.1.1.1 Example of a production budget

Article	***Product A***	***Product B***	***Product C***	***Total Sales***
Price	50	70	90	
Quantity	100‘000	80‘000	30‘000	
Revenue	5‘000‘000	5‘600‘000	2‘700‘000	
Total Revenue				**13‘300‘000**

2.2 Materials and purchases

This budget shows the amount of materials you need to create the production. The factors you need to consider are:

- The amount
- The standard cost (on average)
- The material costs

2.2.1 The steps to create a material and production budgets

- Identification of the substances
- Determining the amount
- Determination of the standard cost for each ingredient
- Calculating the cost of materials for each ingredient (multiply the amount by the standard cost)
- Calculation of total material costs

The required material is the material (volume) that you need to produce an item .

- Use the material and production costs for an item
- Use keep the production budget for information on the number of elements

Go for the calculation of the total cost as follows:

(Product A * standard costs for each product)

- The sum of all products is the total cost
- Check the inventory , you get to deduct the amount you need
- If you need additional material, add the required minimum amount to the total cost.

2.2.1.1 Example of a material purchase budget

Production	*Product A*	*Product B*	*Product C*	*Total Cost*
Quantity	100000	80000	30000	
Standardcost	35.00	50.00	70.00	
Materialcost	3‘500‘000	4‘000‘000	2‘100‘000	**9‘600‘000**

2.3 The working budget

This budget shows you how expensive it is to produce the item with the worker in your organization. The following factors are important:

- Time taken for each activity
- The rate per hour

2.3.1 The steps for calculating the cost of labor

- Determination of activity
- Determining the standard time for each activity
- Determination of the hourly rate for the time spent
- Calculation of labor costs (multiply standard time x hourly rate)
- Calculation of total labor costs

2.3.1.1 Example of a working budget

Production	***Product A***	***Product B***	***Product C***	***Total Cost***
Quantity	40‘000	17‘500	5‘000	
Time/minute	30	40	60	
Hourly rate	40.00	60.00	100.00	
Effective Cost	20.00	40.00	100.00	
Product/Cost	800‘000	700‘000	500‘000	
Total Cost				2‘000‘000

3. The administrative budget

This type of budget is special. The understanding of this budget is important to the success because:

- It will help in the development of a clear and sufficiently detailed budget
- It will help you to understand the flow of capital and the cost structure of the company

3.1 Components of an administrative budget

Operating statement

The profit and loss account consists of three parts

- turnover
- direct costs
- fixed costs

3.1.1 Example of an operating budget

Operation	*Product A*	*Product B*	*Product C*
Revenue	5'000'000	5'600'000	2'700'000
Direct Cost	3'500'000	4'000'000	2'100'000
Gross Revenue	1'500'000	1'600'000	600'000
Fix Cost	800'000	700'000	500'000
Nei Profit	**700'000**	**900'000**	**100'000**

From these numbers, you get the following results:

- Gross profit for the difference between the revenue and the direct costs
- The net gain is the difference between gross profit and the fixed costs
- Administration budget predicts and controls the flow of capital and is a statement for the future

3.1 2. Direct vs. fixed costs

To illustrate the difference between direct costs and fixed costs, a preliminary statement

- Direct costs change in proportion to sales (material)
- Fixed costs remain constant regardless of income (work, interest)