**FINANCIAL AND BUSINESS MANAGEMENT FOR ROAD CONTRACTORS**

**MODULE THREE SESSION FOUR PARTICIPANTS’ NOTES**

**REVENUE PROJECTIONS AND VARIANCE**

1. **Session Objectives**

By the end of the session trainees will be able to develop a forecasted revenue budget and to analyze and discuss revenue variances and how they relate to profitability and cash.

Training objectives include training participants to be able:

1. To develop a revenue variance report
2. To identify possible action on variances
3. To develop a profit budget
4. To relate revenue budgets to profits and cash.
5. **Revenue projections**

Using planning assumptions predict business volume, rates and timing. For the first year of the forecasts how projections on a monthly basis, then for the following years aggregate the amounts on an annual basis.

Long term revenue projections are useful to business managers or owners in that they help to forecast business revenues under different conditions for up to 5 or more years into the future. Accurate revenue projection helps to predict peaks and slumps in income, and enable forward planning and adjustments to staffing and equipment, cash and expenses. In making projections, analyze your current contract or contracts in progress or due. Make an estimate of how much income you expect to bill on a month-by-month basis and enter these figures on a spreadsheet. Make assumptions that are realistic and achievable. Forecast basing on past trends, future planned contracts, anticipated contracts and work in progress. Below is a suggested revenue projection format:

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| Contract particulars | Y1 | Y2 | Y3 | Y4 | Y5 | Total |
| Contract 1 |  |  |  |  |  |  |
| Contract 2 |  |  |  |  |  |  |
| Contract 3 |  |  |  |  |  |  |
| Contract 4 |  |  |  |  |  |  |
| Total Revenue |  |  |  |  |  |  |

1. **Managing variances**

Revenue variances are primarily three; total revenue variance that is further broken down into volume and price variances. The total revenue variance is the difference between budgeted revenue and actual revenue. Revenue (or sales) volume variance is the difference in budgeted quantity and actual quantity at the budgeted price per quantity. (Budgeted mileage – actual mileage) x budgeted price per kms. Stoppages due to factors such as weather, strikes and machine breakdown will lead to revenue volume variance. Variations will also do the same.

Revenue (or sales) price variance is the difference between the budgeted price and the actual price of the actual quantity done. (Budgeted price – actual price) x actual quantity billed. Sales price variances will be the responsibility of the bidding team, how competitive they are to bid and to negotiate. If price is cost plus a margin, sales prices will vary with the changes in input prices. Where costs go up, a favourable sales price variance will result while where costs fall an adverse sales price variance will result. (Note that the input cost variance will be the opposite of the sales price variance, when one is adverse the other is favourable.)

Some events may be controllable by administrators, such as the quantity of work done, stoppage time and speed of construction. This is where a greater focus should be laid. External sources of budget variance such as weather or price are usually less controllable than internal sources.

For revenue control therefore, management should focus on controllable factors to avoid adverse revenue variances.

1. **Major Constraints**
2. Delays in concluding works contracts,
3. Forecasting of potential contracts in open bidding
4. Estimation of completed works for invoicing
5. Approval of work variations
6. Timing of when payment may be done
7. Delays resulting from nature, industrial action, stock outs and machine break downs.
8. **Revenue variances and profits**

Revenue variances directly impact on budgeted profit. An adverse revenue variance reduces budgeted profit by the same amount and a favourable revenue variance increases profits by the same amount.

1. **Projection of revenues format**

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Source** | **Yr 1** | **Yr2** | **Yr3** | **Yr 4** | **Yr 5** |
|  |  |  |  |  |  |
|  |  |  |  |  |  |

1. **Annual revenue variance analysis format**

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| Source | Contract 1 | Contract 2 | Contract 3 | Contract 4 | Total |
| Budgeted Revenue | A |  |  |  |  |
| Volume Variance | B |  |  |  |  |
| Price Variance | C |  |  |  |  |
| Total variance (Impact on profit) | (B+C) |  |  |  |  |
| Actual revenue | (A+B+C) |  |  |  |  |

1. **Group activity (All)**
2. Analyze the causes of revenue variances for the provided case.
3. Identify revenue variances that are uncontrollable and controllable under the provided case and from your experience.