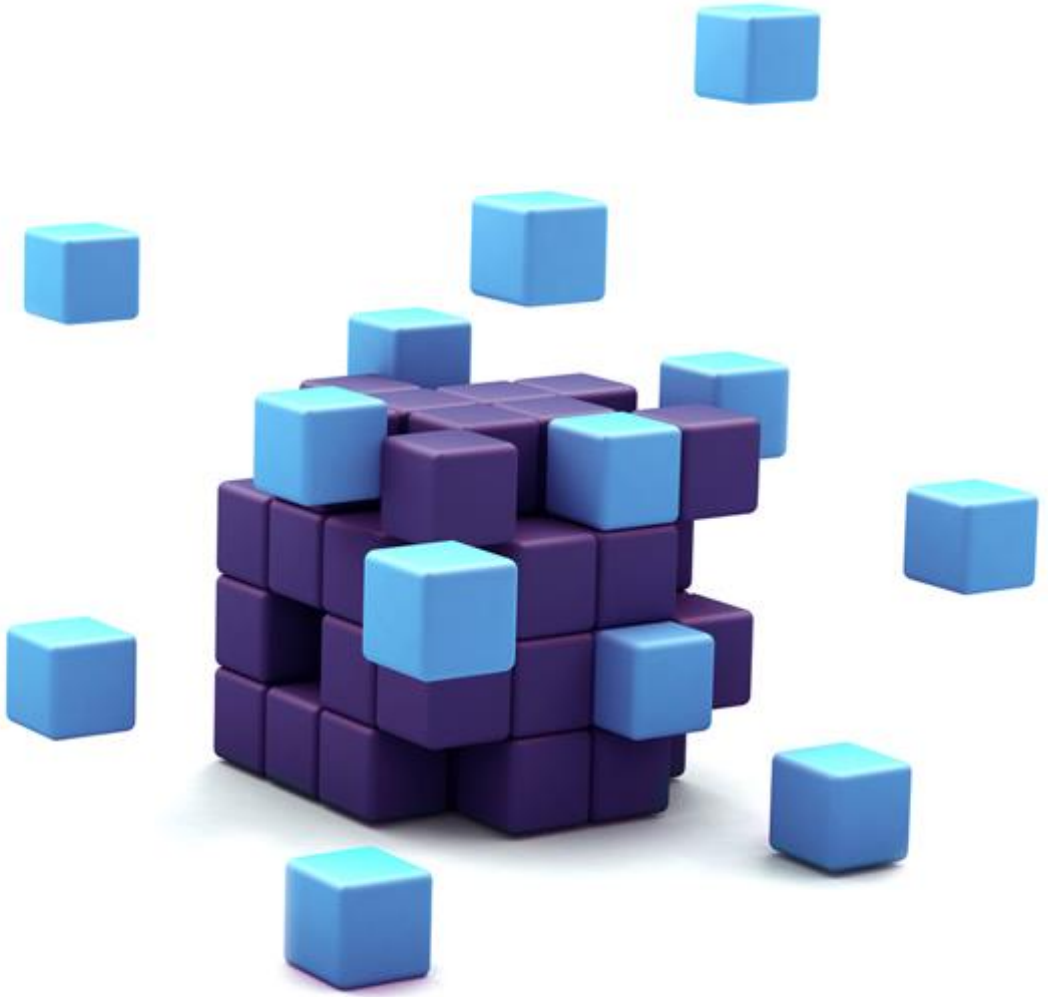
Università di Roma Tor Vergata

PLANNING, BUDGETING AND FORECASTING 101

SEPTEMBER / OCTOBER 2019 - 6 CFU

LESSON 3



ICE BREAKER

DESERT ISLAND PICKS

COURSE TARGETS AND STRUCTURE

The aim of this course, which includes a **Business Challenge**, is to **bring students closer to the real working life within the Planning and Control departments**.

Sep 20th
Introduction to the Course and to Planning, Budgeting & Forecasting

Sep 27th
The Planning & Control department role in the Organizations

Oct 3rd
The Profit & Loss and the Budgeting typical approaches.

Team Work for Business Challenge

Oct 11th
Effective presentation and storytelling

Team Work for Business Challenge

Oct 25th
Exam

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ANY QUESTIONS ?

ARE YOU READY?

THE MANAGEMENT PROFIT & LOSS – AN HIGH LEVEL OVERVIEW

WHAT IS A CONTROLLING MODEL?

… is a multidimensional “detection system” of Corporate phenomena based on industrial accounting

…translates organizational responsibilities into economic responsibilities

…ensures the correct attribution of costs and revenues, assets and liabilities to the various dimensions of control

KEY QUESTIONS ADDRESSED BY THE CONTROL MODEL : REAL LIFE EXAMPLE

Legal Entity

- *Company 1*
- *Company 2*
- *etc.*

Responsibility

- *Division 1*
- *Division 2*
- *Services*
- *Corporate*
- *…*

Activity (value chain)

- *Upstream*
- *Generation*
- *Retail*
- *etc.*

Geography

- *Italy*
- *Iberia*
- *Russia*
- *etc.*

Counterparty

- *Group LE 1*
- *Group LE 2*
- *Third Parts*
- *etc.*

Technology

- *Solar Plants*
- *Wind Plants*
- *etc.*

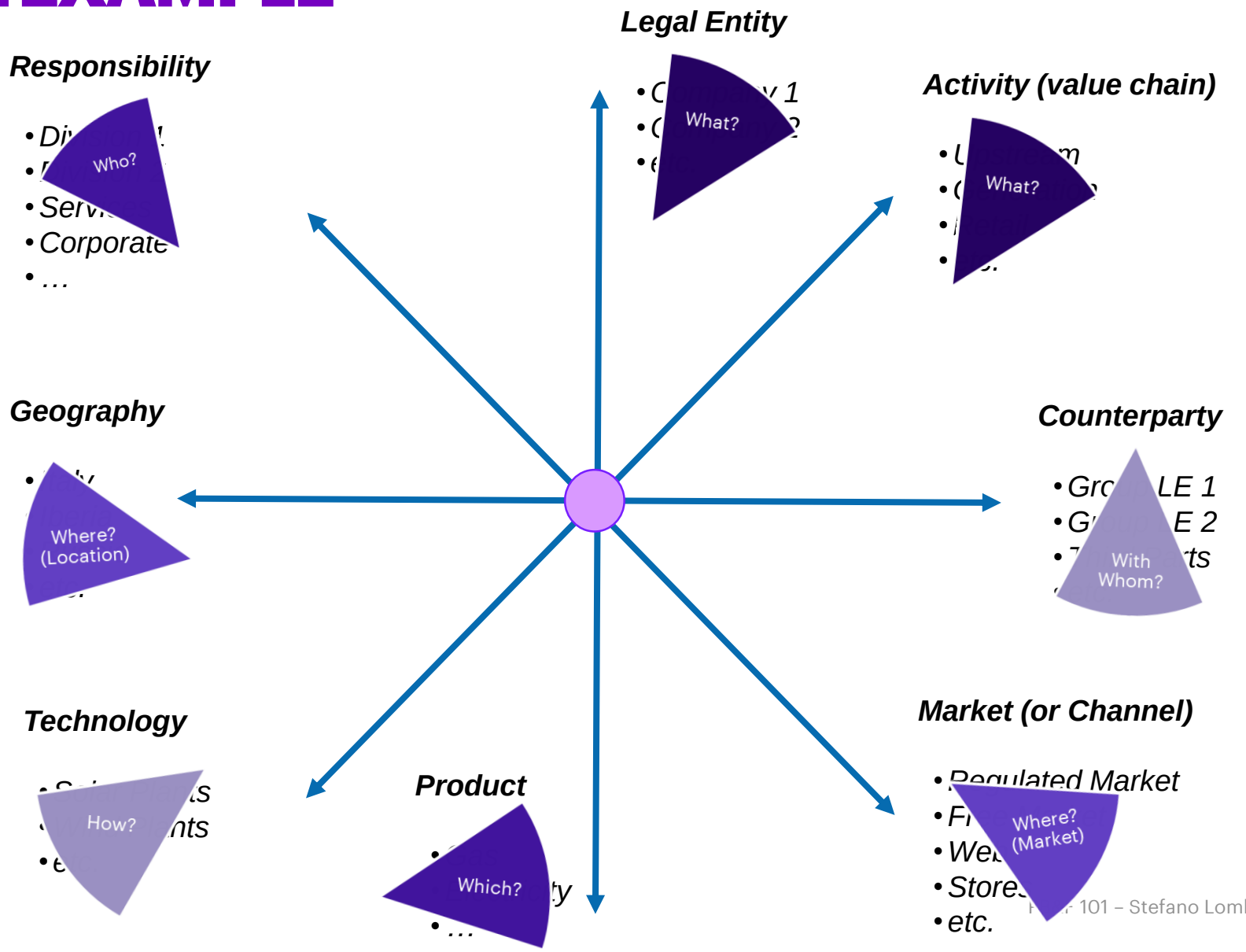
Product

- *Gas*
- *Electricity*
- *…*

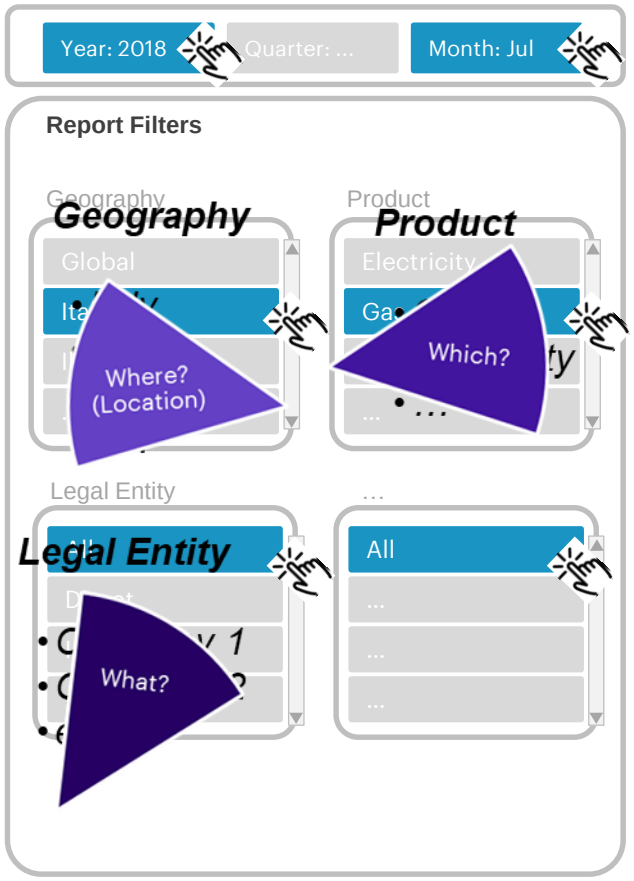
Market (or Channel)

- *Regulated Market*
- *Free Market*
- *Web*
- *Stores*
- *etc.*

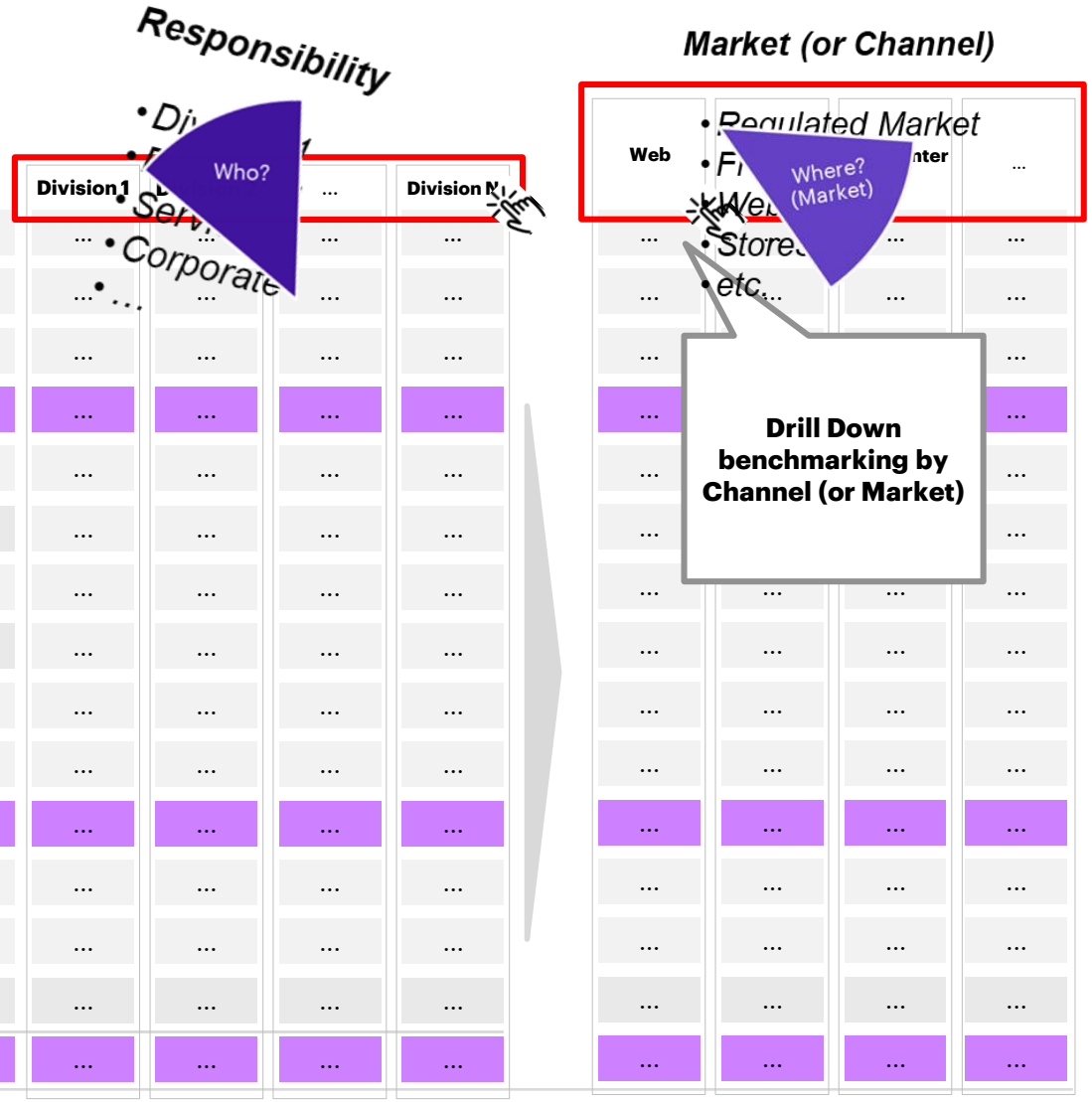
KEY QUESTIONS ADDRESSED BY THE CONTROL MODEL : REAL LIFE EXAMPLE



THE TOOL TO "READ " THE CONTROL MODEL IS THE COMPANY REPORTING



Profit & Loss



Revenues	...	...	...	...	...	...	...	...	...
Cost of goods and services sold	...	...	...	...	...	...	...	...	...
Trade Fees and Commissions	...	...	...	...	...	...	...	...	...
GROSS MARGIN	...	...	...	...	...	...	...	...	...
…	...	...	...	...	...	...	...	...	...
MARGIN FROM SALES	...	...	...	...	...	...	...	...	...
…	...	...	...	...	...	...	...	...	...
OPERATION MARGIN	...	...	...	...	...	...	...	...	...
General and Administrative	...	...	...	...	...	...	...	...	...
Other Indirect OPEX	...	...	...	...	...	...	...	...	...
EBITDA	...	...	...	...	...	...	...	...	...
…	...	...	...	...	...	...	...	...	...
Other Depreciations and Amortizations	...	...	...	...	...	...	...	...	...
EBIT	...	...	...	...	...	...	...	...	...
	...	...	...	...	...	...	...	...	...

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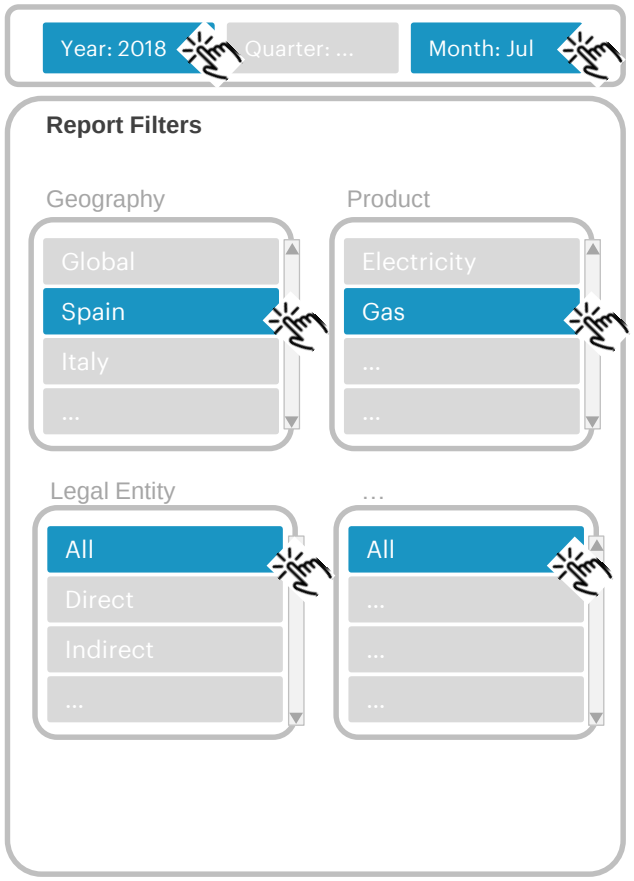

Profit & Loss

	Division 1	Division 2		Division N	Web	Stores	Call Center	...
Revenues	...	...		...	...	...	...	...
Cost of goods and services sold	...	...	...	...	...	...	...	...
Trade Fees and Commissions		...	...	...	...	...	...	...
GROSS MARGIN		...	...	...	...	...	...	...
…			...	...			...	...
MARGIN FROM SA			...					...
…			...					...
OPERATION MARG			...					...
General and Administra			...					...
Other Indirect OPEX		...	...					...
EBITDA		...	...					...
…	...	...	...					...
Other Depreciations and Amortizations	...	...	...					...
EBIT	...	...	...	...			...	...
	...	...	...	...	...	...	...	...

Mr. Doe, Mr. Rossi, Mrs. Smith, Miss Fulano, Mr. Sultano, Mrs. Mengano

Division Directors/ CEOs

Channel Directors

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Market (or Channel)

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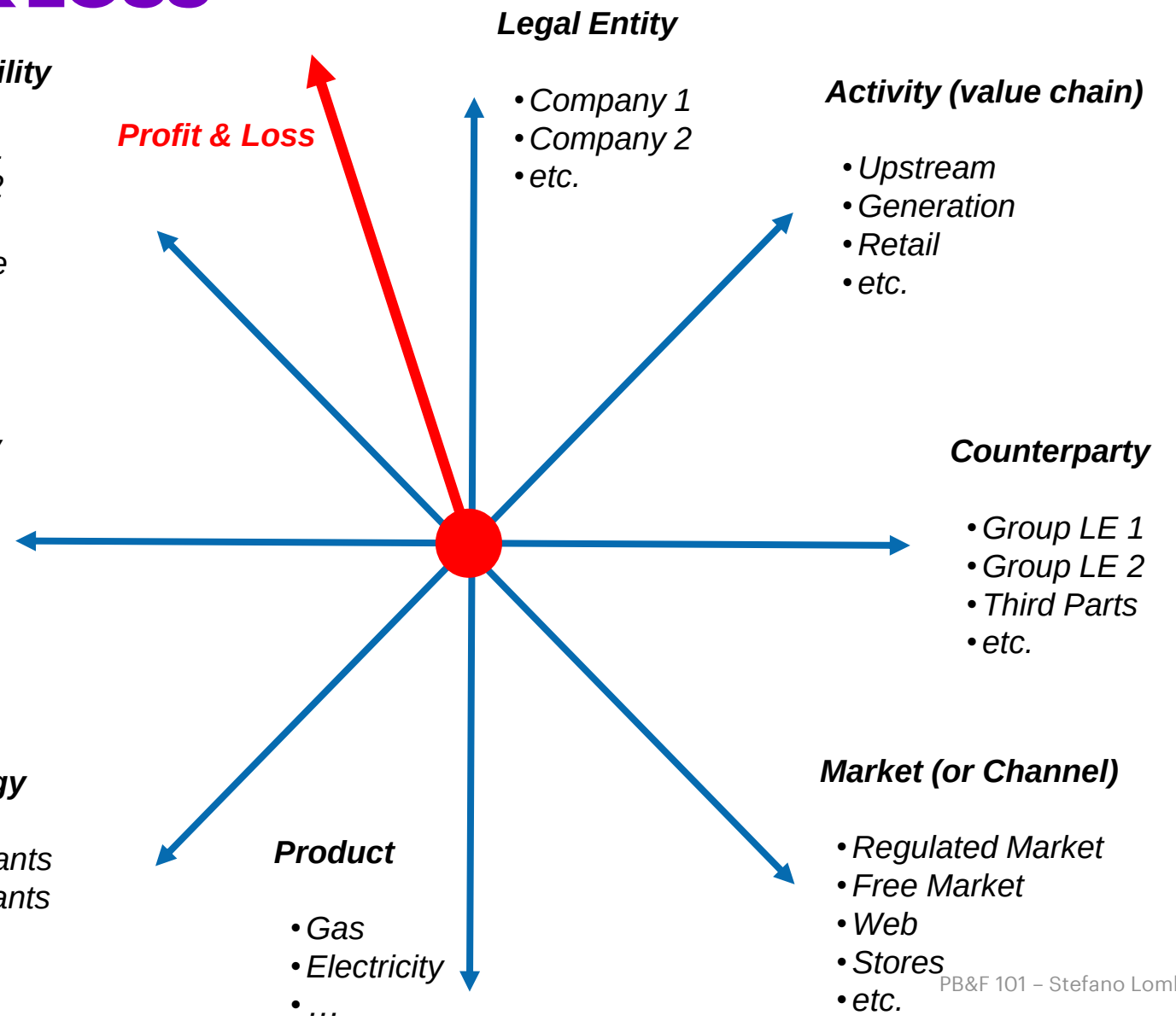
A KEY DIMENSION OF THE COMPANY CONTROL MODEL IS THE PROFIT & LOSS

The **attribution** of the Control Model **Dimension of Analysis elements** to each line of the **Profit & Loss** translates **organizational responsibilities** into **economic responsibilities**



STATUTORY AND MANAGERIAL PROFIT & LOSS REPORTING

Management
Profit & Loss

Statutory
Profit & Loss

STATUTORY AND MANAGERIAL PROFIT & LOSS REPORTING

1. **Mandatory** (law) for certain classes of Companies
2. **Break down and showcase financial actions** taken by the company in that year
3. **Prepared for a specific time** and only completed once a year
4. Used both **internally** and **externally**
5. **Specific**/Mandatory **Structure** and Formatting

Statutory
Profit & Loss

STATUTORY AND MANAGERIAL PROFIT & LOSS REPORTING

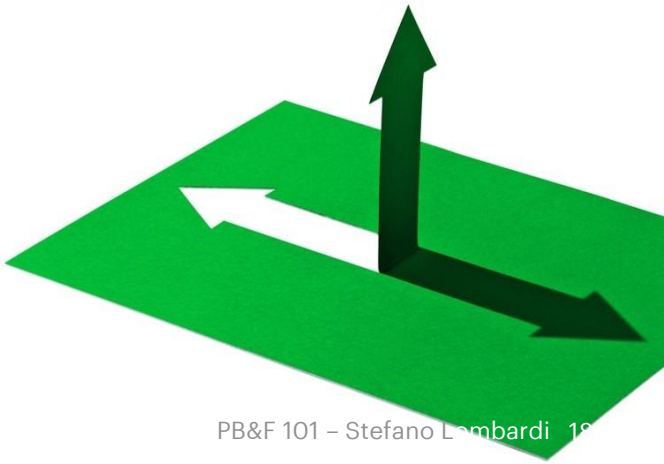
Management
Profit & Loss

1. Not Mandatory, at the **discretion of the Company**
2. Allow management team in a business to **make decisions** based on the financial position of the Firm
3. No need to be completed to official time frames (law). **Deadlines decided by the Firm**
4. Used **only internally**
5. No set format or data requirements. **Can look and include whatever the Firm you decides**.

FOCUS ON – TEAM WORK /BUSINESS CHALLENGE

Management
Profit & Loss

THE TEAMS WILL FOCUS THEIR WORK ON A MANAGEMENT PROFIT & LOSS



MANAGEMENT PROFIT & LOSS EXAMPLE – GROSS MARGIN

Revenues
Cost of goods and services sold
Trade fees and commissions
GROSS MARGIN
Cost to Acquire
MARGIN FROM SALES
Cost to Serve
MARGIN FROM OPERATIONS
General and Administrative
Other Indirect opex
EBITDA
Depreciations and amortizations of contract-specific CAPEX
Depreciations and amortizations for trade fees and commissions
Other depreciations and amortizations
EBIT

PRODUCT MARGIN

ILLUSTRATIVE

Revenues

- Revenues from product sale
- Revenues from services
- Revenues from electricity sale
- …

MANAGEMENT PROFIT & LOSS EXAMPLE – GENERAL & ADMINSTRATIVE

ILLUSTRATIVE

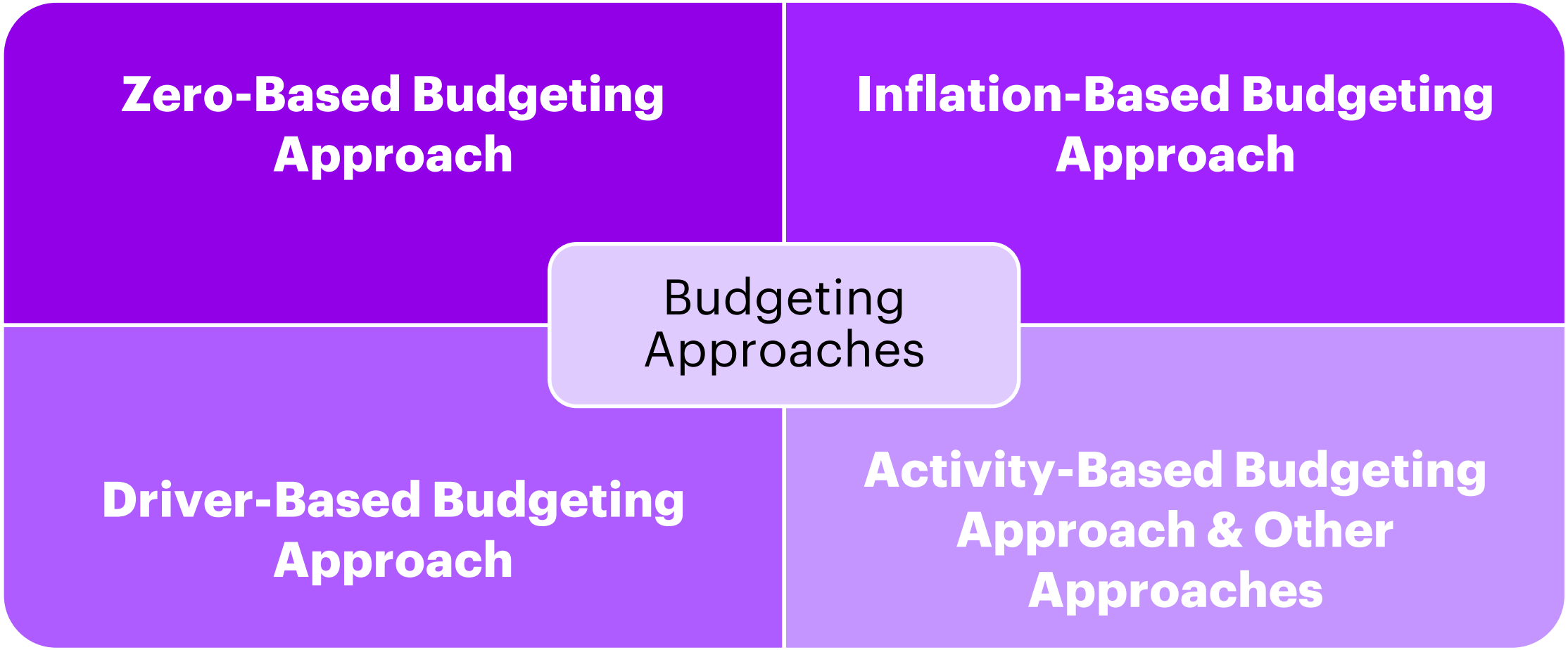
Revenues
Cost of goods and services sold
Trade fees and commissions
GROSS MARGIN
Cost to Acquire
MARGIN FROM SALES
Cost to Serve
OPERATIONS MARGIN
General and Administrative
Other Indirect OPEX
EBITDA
Depreciations and amortizations of contract-specific CAPEX
Depreciations and amortizations for trade fees and commissions
Other depreciations and amortizations
EBIT
PRODUCT MARGIN

G&A

- G&A personnel
- Security
- Facilities
- Real Estate
- …

BUDGETING APPROACHES

THE TYPICAL BUDGETING APPROACHES - OVERVIEW



THE TYPICAL BUDGETING APPROACHES - DETAILS

Zero-Based Budgeting Approach	Driver-Based Budgeting Approach	Inflation-Based Budgeting Approach	Activity-Based Budgeting Approach	Other Approaches
• Re-evaluate in detail the expenditure groups starting **from scratch each year**. • **Bottoms-up budget justification at each period**, typically annually.	• Planning models **incorporate key business drivers** (financial and non-financial) to predict resource needs.	• Prior period budget is **simply adjusted** to account for inflation or revenue growth.	• Budget **aligned to process/activities** that incur costs in every functional area of an organization. **Similar activities across functions can be grouped**, compared, and re-organized.	• ... • ...

THE TYPICAL BUDGETING APPROACHES - THE DRIVER BASED APPROACH

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THE TYPICAL BUDGETING APPROACHES - THE DRIVER BASED APPROACH

Description

Planning models incorporate **key business drivers** (**financial** and n**on-financial**) to predict resource needs. Typically coupled with "**what-if" capability** to allow for comparison of **alternative strategies** and simultaneously show probabilistic outcomes to revenue projections and cost budgets.

Benefits

1. **Financial budgeting linked to operational metrics** by using the same key drivers allowing for cause and effect linkages
2. **Drivers run across organizations**, forcing alignment on expected business outcomes over time periods
3. Flexibility to **use assumptions**
4. Monitoring of external environment leads to **event-triggered re-forecasting**, saving time and iterations

Issues/Risks

1. Continual discipline to **modify cost structures as drivers fluctuate**
2. Requires maturity to have visibility to and **alignment** on **key inter-departmental cost drivers**
3. Necessitates more robust system to support driver assumptions, scenario modeling, and approval workflow
4. **Requires access and linkage across financial and operational data** – e.g. integrated data warehouse

THE TYPICAL BUDGETING APPROACHES - THE DRIVER BASED APPROACH

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Cost of goods and services sold
Trade fees and commissions
GROSS MARGIN
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PRODUCT MARGIN

ILLUSTRATIVE

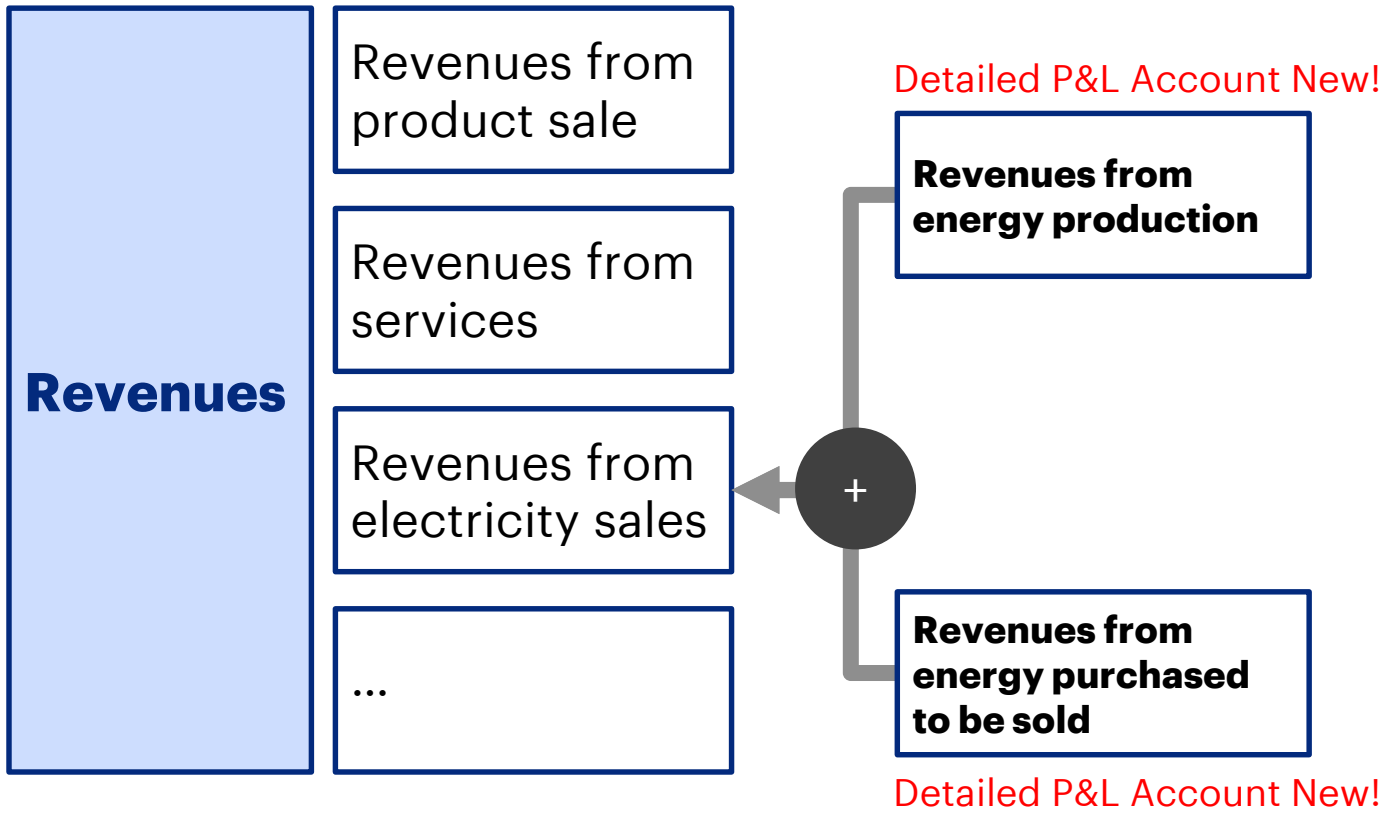
Revenues

- Revenues from product sale
- Revenues from services
- Revenues from electricity sale
- ...

THE TYPICAL BUDGETING APPROACHES - THE DRIVER BASED APPROACH

ILLUSTRATIVE

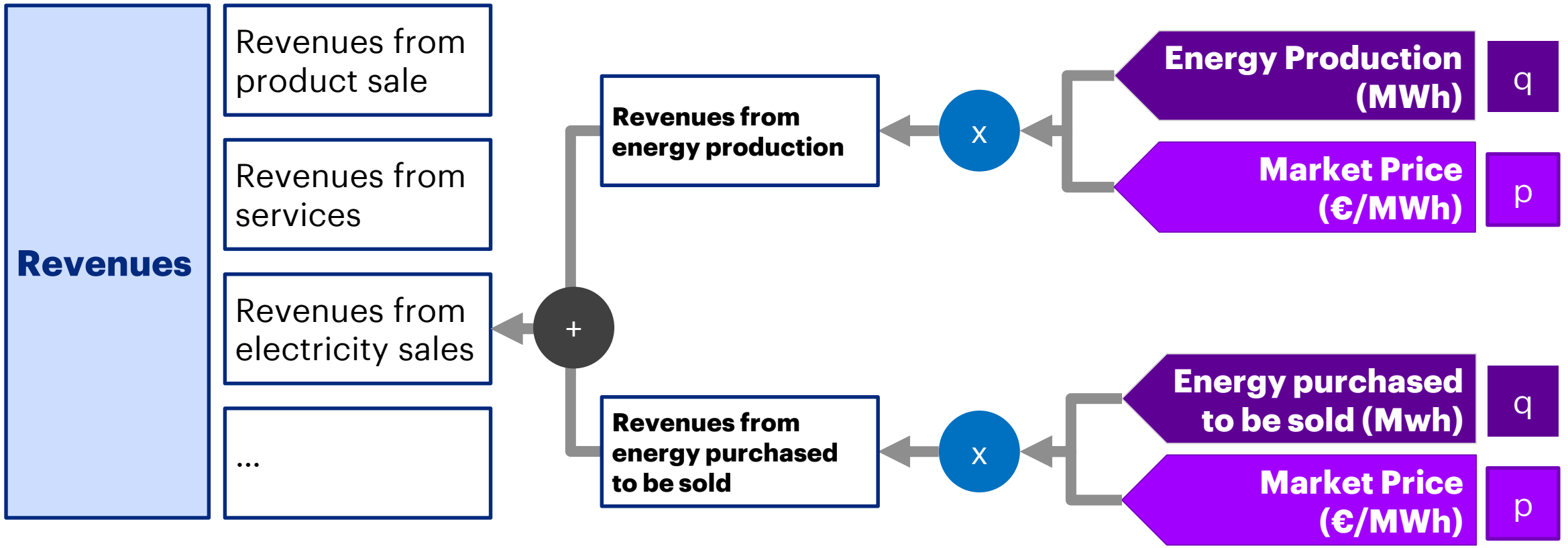
Example: Revenues from Electricity Sales



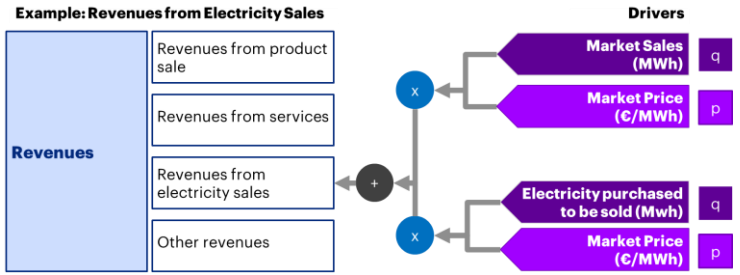
THE TYPICAL BUDGETING APPROACHES - THE DRIVER BASED APPROACH

ILLUSTRATIVE

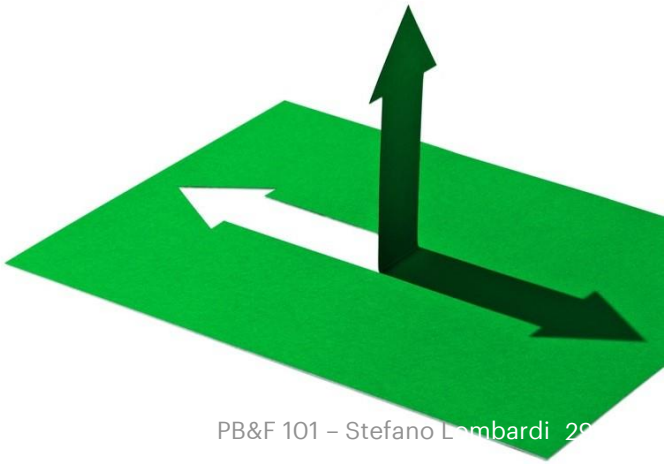
Example: Revenues from Electricity Sales



FOCUS ON – TEAM WORK /BUSINESS CHALLENGE



THE TEAMS WILL FOCUS THEIR WORK ON A DRIVER BASE BUDGETING



WRAP-UP

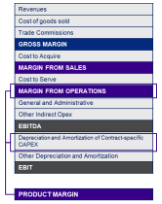
- **Management Profit & Loss reports** are produced to **allow the management team** in a business to **make decisions** based on the financial position of the company. Management P&L is exclusively used for internal decision making. Many corporations opt to create Management P&L reports quarterly, monthly, or even weekly as methods of tight financial control.

- **Driver Based Planning models** incorporate **key business drivers** (**financial** and **non-financial**) to predict resource needs. They are typically coupled with "**what-if" capability** to allow for comparison of **alternative strategies** and simultaneously show probabilistic outcomes to revenue projections and cost budgets.

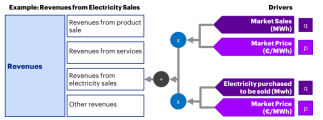
TEAM WORK /BUSINESS CHALLENGE

FOCUS ON – TEAM WORK /BUSINESS CHALLENGE WHAT YOU NEED TO DO!

Given the Management Profit & Loss



Given the Driver Based Budgeting approach



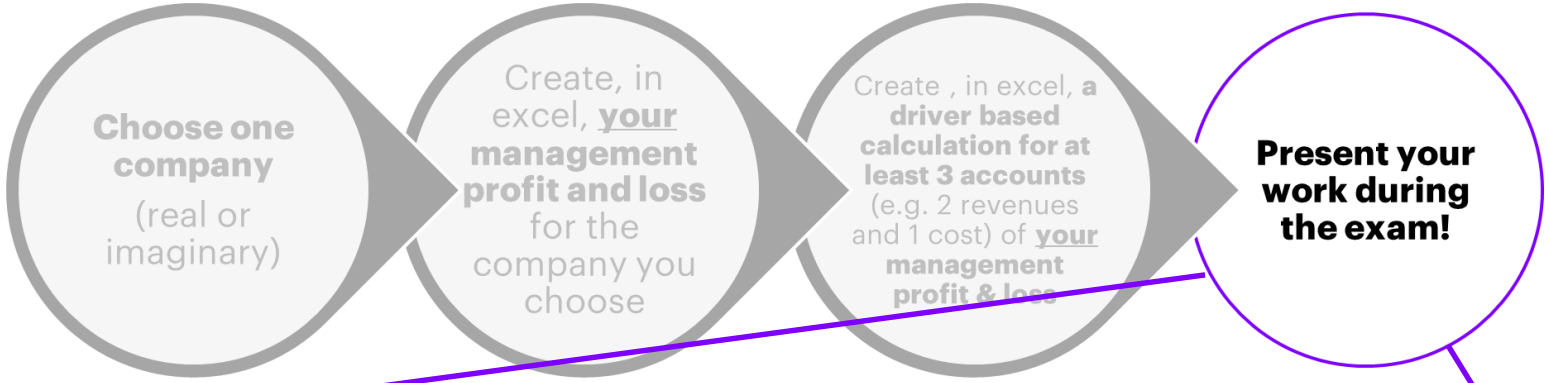
Choose one company (real or imaginary)

Create, in Excel, **<u>your</u> Management Profit and Loss** for the company you have choosen

Create, in excel, **a driver based calculation for at least 3 accounts** (e.g. 2 revenues and 1 cost) of **<u>your</u> Management Profit & Loss**

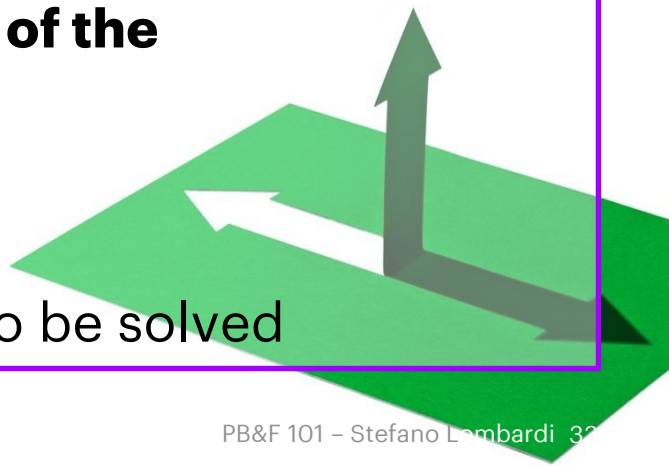
Present your work during the exam!

FOCUS ON – TEAM WORK /BUSINESS CHALLENGE WHAT YOU NEED TO DO!



Students, in team, will make **a presentation for the Exam** (e.g. Power Point, Prezi, etc.), **imagining** that they have to **present their P&L Model to the CFO of the chosen company.** The presentation **must include at least:**

- The description of the chosen Company
- The Profit & Loss driver based Planning Model
- The description of the chosen Company and the Target/Problem to be solved



YOUR FEEDBACK COUNTS!

NEXT FRIDAY, OCTOBER 11TH TIMETABLE

14.00 – 16.00:
LECTURE - EFFECTIVE PRESENTATIONS AND STORYTELLING

16.00 – 17.00 :
Q&A TIME - EACH TEAM WILL HAVE 15 MINUTES TO INTERACT WITH THE FACULTY TO SOLVE SPECIFIC DOUBTS ABOUT THE BUSINESS CHALLENGE.

IF NEEDED, TEAM REPRESENTATIVES MUST BOOK A 15 MINUTES TIME SLOT BY WRITING TO STEFANO.LOMBARDI@UNIROMA2.IT

ANY QUESTION?

HAVE A NICE WEEKEND!