

**A PROFITABILITY ANALYSIS IN RELATION TO SALES,  
COSTS AND PROFIT OF NEPAL TELECOM**

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## LIST OF TABLES

<b>Table No.</b>		<b>Page no.</b>
4.1	Budgeted and Actual Sales	67
4.2	Presentation of Mean and Standard Deviation of Sales	68
4.3	Fitting Straight Line Trend by Least Square	69
4.4	Mean and Standard Deviation Actual Sales and actual Profit	71
4.5	Growth of Profit	72
4.6	Actual Overhead Budget	74
4.7	Relationship between Actual Sales and Overhead	76
4.8	Variable Cost Analysis	80
4.9	Fixed Cost Analysis	81
4.10	Income Statement	82
4.11	Competition of Various Ratio	84
4.12	Analysis of BEP Considering Other Income and other Expenses	85

## **LIST OF FIGURE**

<b>Figure No.</b>		<b>Page no.</b>
4.1	Budgeted and Actual sales Revenue	68
4.2	Profit and Loss	73
4.3	Actual Overhead	75
4.4	Actual Sales and Overhead	77
4.5	Graphical Presentation of BEP	86

## **TABLE OF CONTENTS**

	Page No.
Recommendation	I
Viva-voice Sheet	II
Declaration	III
Acknowledgement	IV
Table of Contents	V
List of Table	VI
List of Figures	VII
Abbreviations	VIII

### **CHAPTER - I**

#### **INTRODUCTION**

General Background	1
Public Enterprise	1
Concept of Revenue Planning	4
Concept of Profit Plan	5
A Brief Introduction of Nepal Telecom Limited	6
Statement of the Problem	8
Objective of the Study	8
Significance of the Study	8
Limitation of the Study	9
Organization of the Study	10

## CHAPTER - II

### REVIEW OF LITERATURE

2.1	Introduction	11
2.1.1	Conceptual Framework	11
2.1.2	Budget or Plan	11
2.1.3	Planning Vs. Sales Forecasting	12
2.1.4	Strategic or Long –range Sales Plan	13
2.1.5	Expenses Budget and Plan	18
2.1.6	Selling and Distribution Expenses Budget	19
2.1.7	Administrative Expenses Budget or Plan	19
2.1.8	Capital Expenditure Budget or Plan	20
2.1.9	Cash Budget or Plan	21
2.2	Profit Planning as a Concept	21
2.2.1	Profit :Meaning and Concept	23
2.2.2	Planning	24
2.2.3	Types of Planning	27
2.2.4	The Role of Forecasting in Planning	29
2.2.5	Forecasting Vs. Planning	30
2.3	Purpose of Profit Planning	30
2.3.1	Long Range and Short Range Profit Plan	31
2.4	Budgetary Control	32
2.4.1	Meaning of Budgeting and Budget	32
2.4.2	Essential of an effective Budgeting	34
2.5	Fundamental Concept of Profit Planning	36

2.5.1	Profit Planning and Control Process	42
2.5.1.1	Identification and Evaluation of External Variables	43
2.5.1.2	Development of Broad Objectives of the Enterprises	43
2.5.1.3	Development of Specific Goals for the Enterprises	44
2.5.1.4	Development and evaluation of Company Strategy	44
2.5.1.5	Executive Management Planning Instruction	45
2.5.1.6	Preparation and Evaluation of Project Plans	45
2.5.1.7	Development of Strategic and Tactical Profit Plan	45
2.5.1.8	Implementation of Profit Plan	46
2.5.1.9	Use of Periodical Performance Report	46
2.5.1.10	Follow Up	47
2.6	Advantage and Disadvantage of PPC	47
2.7	Basic Assumption and Limitation Profit Plan	49
2.8	Implementation of Profit Plan	50
2.8.1	Completion of the Annual Profit Plan	50
2.8.2	Implementing the Profit Plan	51
2.8.3	Performance Report	52
2.8.4	Review of Previous Research Work	53
2.9	Research Gap	61

### **CHAPTER – III**

#### **RESEARCH METHODOLOGY**

3.1	Introduction	62
3.2	Research Design	62
3.3	Data Collection Procedures and Sources of Data	63

3.4	Population and Sample	63
3.5	Tools and Techniques Employed	63

## **CHAPTER – IV**

### **DATA PRESENTATION AND ANALYSIS**

4.1	Introduction	65
4.2	Sales Revenue Budget or Plan	65
4.3	Sales Budget	66
4.3.1	Sales Budget and Profitability	70
4.4	Growth Analysis	72
4.4.1	Profit and loss Analysis	72
4.5	Actual Overhead Budget	73
4.5.1	Relationship Between Sales and Overhead	75
4.6	Cost Plan Analysis	77
4.7	Variable Cost	79
4.8	Fixed Cost	80
4.9	Semi Variable Cost Analysis	81
4.10	Cost Volume Profit Analysis	82
4.11	Analysis of CM Ratio, BEP, Margin of Safety	83
4.12	Major Findings	87

## **CHAPTER – V**

### **SUMMARY, CONCLUSIONS AND RECOMMENDATION**

5.1	Summary	89
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5.2	Conclusions	91
5.3	Recommendation	93

## **BIBLIOGRAPH**

## **APPENDIX**



## **ABBREVIATION**

A.D. - Anno Domini  
A/C - Account  
B.S. - Bikram Sambat  
BEP - Break Even Point  
C.V. - Co-efficient of Variation  
CDMA - Code Division Multiple Access  
C-Phone - Cellular Phone  
CVP - Cost Volume Profit  
e.g. - That is  
F/Y - Fiscal year  
FC - Fixed Cost  
GDP - Gross Domestic Product  
GSM - Global System of Mobile  
ISTD - International Subscriber Trunk Dialing  
Ltd - Limited  
No - Number  
NT - Nepal Telecom  
NTC - Nepal Telecommunication Corporation Ltd.  
P.E. - Probable Error  
PE - Public Enterprises  
PPC - Profit Planning and Control  
PSTN - Public Switched Telephone Network  
S.D. - Standard Deviation  
SMS - Short Message Service  
STD - Subscriber Trunk Dialing  
T.U. - Tribhuvan University  
VC - Variable Cost

# **CHAPTER - I**

## **INTRODUCTION**

### **1.1 General Background:**

Nepal is one of the least developed countries with poorest economic condition of the world. Situated in northern hemisphere, known as land of Mt. Everest and the birthplace of lord Buddha, Nepal is a tiny landlocked country. Nepal remains as one of the 48 least developed countries in the world. It lies between India and China. It covers an area of 147181 square kilometers and runs all along 885 kilometers from the **east** to the west and 145 kilometer to 241 kilometers from the north to south. It has more than 30.85% people living below poverty line and its per capita income is only about \$ 320 or NRs. 22540 (World Bank Report 2009). It is placed among the countries having the lowest per capita income. The economic development of the country, which reflected by the annual GDP growth rate, is around 1.9% and it has in fluctuating trend (Economic survey 2007/08).

In the contest of Nepalese industrialization is in its infancy. Industrial sectors have contributed in the economy not more than 20% and more than 80 % people still depend on agriculture for the live hood (Population census 2058).

### **1.2 Public Enterprise:**

Public enterprise are those which are managed, controlled and owned by government to provide goods or service to the people at fair price. In such enterprise, government owns half or more than half of total shares. In Nepal, public enterprise is established with fund of HMG or with the help of financial assistance of international agencies or foreign countries. Public enterprises are established not only for commercial purpose but also for public welfare and thus are strong means of socio-economic development of nation. Standing on that fundament, public enterprise has to maintain proper balance between profit and service.

Mainly the exploitation of consumers and workers, necessity of development of infrastructure, defenses structure, utilization of natural resource and unemployment condition of nation compels government to establish public enterprises.

When we see the history of PEs, we find that most of them well created by government themselves to manage certain key sectors of the economy (Joshi, 1989:1).

Different scholars, agencies and government have defined the term 'public enterprise' differently to suit their own respective situations. Public enterprise means ownership and operation of industrial, agricultural, financial and commercial undertakings. In the words of World development report 1998, State owned enterprises are financial autonomous and legally distinct entities wholly or partially owned by government.

State owned enterprise are financial autonomous and legally distinct entities. They are generally owned and controlled by government. The ownerships with the government should be 51% or more to make entity PE. Public enterpriser usually autonomously organized with the government providing the initial capital and being responsible for contribution overview of their activities finance and development. They are government creations with certain mission and objectives. However, controls by government at every aspect of public enterprise are undesirable. They should have certain degree of freedom as well (Baral, 2001: 2).

UN has defined public enterprise as those organizations, namely governmental enterprise and public corporation which are entirely or mainly owned and /or controlled by public authorities consisting of establishment which by virtue or their kind of activities, technology and mode of operation are classified as industries.

Public enterprises were established in developed countries in 18<sup>th</sup> century and in the developing countries after Second World War. In context of Nepal, Nepal Bank Ltd. was established in 1904 BS in private sector, but after 2010 BS, government purchased 51% of its shares and it became first public enterprise in Nepal. During the Second World

War, some other PEs was established. However, they could not make any substantial progress. Nepal started its planned economic development from 2013 BS. Then the number of public enterprise has increased substantially in the various field of national economy. There were 64 PEs in Nepal before privatization program of HMG lunched. They are manufacturing as well as service enterprise. Both of them are interested to earn profit by bearing social responsibility as well. Among them, Nepal Electricity Authority is the one.

### **1.2.1 Role of Public Enterprises in Nepal:**

Nepal a land locked country is one of the least developed countries of the world with poor economic condition. It has an area 147181 sq. Km, length of 885 Km from east to west and average breadth about 193 Km form north to south. More than 32% of the people are living below poverty line. Per capita income of Nepal is about \$236, GDP growth rate is around 3.7% and it has fluctuation trend. More than 80% of people still depend on agriculture and not more than 10% on industrial sector for their livelihood.

Nepal is exercising mixed economic policy for its economic prosperity. It creates the co-existence of private and public sector. Despite many private enterprises, they are only oriented to generate profit and ignore social welfare, compel the government to reserve some enterprises by full or partial ownership.

The co-existence of both private and public sector is necessary and useful for achieving the twins' objectives of social and economic development, envisaged in national level policy. Mainly, the role of PEs has been in basic infrastructure, defense sector, industrial estate public utilities, and commercial sector, trading and sectors. PEs are important to create industrial bases in the country, to provide better goods/service to the people at reasonable price, to generate employment opportunities, to collect government revenue, to mobilize the national resource into productive uses and to fulfill the government plans and objectives. PEs has helped to boost the standard of living, to balance regional development, to utilize resource optimally, to contribute import substitution and export promotion. Therefore, the role of PEs in developing countries like Nepal is the most

important for socio-economic development of people, enterprise and the nation. No nation in the world is without public enterprises.

However, almost Nepalese PEs have been suffering from regular operation loss according to the past annual budgets and economic survey of various projects. They are unable to generate substantial return from their investment and at last to contribution to the nation through dividend as well as tax. They are creating a huge amount of liabilities and being the financial burden to the government and thus after the restoration of democracy, the government has adopted the policy of privatization. During the eight five-year plan, the industrial act 2049 was enforced and equally, privatization took place.

### **1.3 Concept of Revenue Planning:**

The starting point in preparing profit plan is the sales plan, which displays the projected sales in units and Rupees. The sales planning process is an essential part of profit plan and control because, it provides for the basic management decisions, about marketing and based on these decisions it is an organized approach for developing a comprehensive sales plan. If sales plan is not realistic and relevant, most if not all of the other parts of overall profit plan are also not realistic. Therefore, if the management believes that a realistic sales plan cannot be developed, there is little justification for PPC, Similarly, if it were impossible to assess the future revenue potential of a business, there would be little or no incentive to investors and prospective investors, Hence, the sales plan is both ends and means of revenue planning.

The preparation of a sales plan requires forecasting of sales, the sales forecasting is one of the inputs in sales plan. A critical step in the budgeting process sales forecast as distinguished from a sales plan is a technical projection of the potential customer's demand for specified time horizon with specified underlying assumption. It is converted to a sales plan when management has brought to bear on its judgment-planned strategies, commitment of resources and the managerial commitment to aggressive action to attain sales goal. Sales plan provides standard for comparison with the result actually achieved

thus it is an implement control device of management, where forecasting represents merely a probable events over which no control can be exercised.

#### **1.4 Concepts of profit plan:**

A profit plan has an immense value in management; it helps in planning and coordinating, if used appropriately, but not a replacement for management. Profit planning is a comprehensive and coordinated plan expressed in financial terms for the operations and resources of an enterprise for some specific period in the future. Profit planning is a comprehensive statement of intentions expressed in financial terms for the operation of both short and long period. It is a plan of the firm's expectation and is used as a bass for measuring actual performance of managers and their units.

Profit planning is predetermined detailed plan of action developed and distributed as a guide to current operations and as partial basis for the subsequent evaluation of performance. Thus it can say that profit planning is a tool which may be used by the management in planning the future course of actions and controlling the actual performance (Gupta, 1997: 141).

Every company or institution is established based on the definite goals and objectives. According to the objectives, the company performance is tasks. Mainly two types of institutions such as profit oriented and service oriented instructions are established, but most of them are profit oriented because profit is the lifeblood of the business which not only keeps it alive but also assures the future and makes it sound. Profit planning is an important tool of the firm to achieve the objectives. Profit do not just happened profits are managed. The management should follow various processes for profit planning because the management process and profit planning and control are related each other (Lynch & William, 1989: 30).

A profit plan is an advance decision of expected achievement based on the most efficient operating standards in effect or prospect of time it is established against which actual accomplishment is regularly compared.

Profit maximization is the basis objectives of a firm and to make profit render reliable service to its customers. Profit is a device to measure efficiency of a firm.

The term comprehensive profit planning and control is defined as a systematic and formalized approach for performing significant phase of the management planning and control function. Especially it involves:

- The development and application of broad and long-range objectives for the enterprises.
- The specification of enterprises goals.
- The development of strategic long range profit plan in broad terms.
- The specification of tactical short-range profit plan detailed by assigned responsibility (division, products, projects).
- The establishment of a system of periodic performance reports detailed by assigned responsibility and follow up procedures

In many of the better-managed companies, comprehensive PPC has been identified as a way of managing. It focuses directly up on a rational and systematic approach to management by objectives and realistic flexibility in performing the management process.

## **1.5 A brief introduction of Nepal telecom limited:**

Telecommunication is an inevitable infrastructure of development to all countries. It is considered as prerequisite for the other dimension of development. In Nepal the need of telecommunication, Nepal Telecom primarily fulfills services. History of telecommunication service in Nepal is not so long. First telecommunication service in the country is introduced in 1974 BS. This was called Magneto Telephone. Since then and up to the launching of first five-year plan of 2012 BS, the development of telecommunication was in slow pace. After Nepal started systemic economic development by launching its first five-year plan in 2012 BS, various national and international trunk line were added and cross bar telephone lines to and public offices were distributed. With the formal inception of Nepal Telecommunications Corporation in 2032 BS, a systematic

development of telecommunication services has been started. It was established under the telecommunication Corporation Act 2028 BS. In fact, the advent of telecommunication Corporation Act is the major step taken by the Nepal Government to provide systematic and scientific telecommunication facility.

Introduction of liberalized economic policy in Nepal gradually facilitated the private sector investment as a result multinational companies also showed their presences. Further enterprises that are more public started to be privatized. Such trend could not also remain intact without influencing Nepal telecommunication Corporation. Hence, Nepal telecommunications Corporation has been changed to Nepal Doorsanchar Company limited in 2061 BS under the company act. Its popularly known commercial name is Nepal Telecom.

The prime objective incorporated by Nepal Telecom is to provide reliable and affordable telecommunication services all over the country. This objective is in turn coupled with economic development of country. At present Nepal Telecom has provided national and international trunk services in all 75 district of nation. Service provided by Nepal Telecom:

- Basic telephone service
- National and international trunk call service
- Rural telecom service
- Pay phone service
- Mobile telephone
- Voice data and telegraph Leased Circuit services
- Email and Internet service
- Intersect Mini-M services
- Home country direct dialing services
- International telegraph services
- Telex services
- V-sat services



## **1.6 Statement of the problem:**

Most of the public enterprises, especially those who are involved in service sector are not preferring well. The reason for, which can be attributed to no or ineffective performing planning of revenue sector, which is basis for all other planning. Hence, in this purposed research following problems will be studied.

1. Are there any shortcoming with planning practice and its implementation?
2. What kinds of practice and effectiveness of sales, cost and profit?
3. What are problem faced by NTC in planning program?

## **1.7 Objectives of the study:**

The basic objectives of this study is to appraise existing revenue planning practice of NTC. Appropriately for the application of comprehensive revenue planning system. Besides this, following are the objectives, which will be, considered for research purpose.

1. To analysis the existing planning practices of NTC.
2. To make analysis of revenue, cost & profit of NTC.
3. To provide appropriate suggestions and recommendation for improvement of NTC.

## **1.8 Significance of the study:**

Every organization should systematically plan is activities. Planning has become important for growth and development for an enterprise. It also in making managerial decisions. A proper planning process helps to achieve organizational objectives easily. The present 4study deals with revenue planning. AS revenue, planning is the corner stone for every planning proper planning for revenue is necessary for the organization. This study is more significant to public enterprises as it will try to analyze and examine the relation of sales planning other functional planning like production, inventors etc. The study will be useful and beneficial to all interested parties concerned with planning it will

provide valuable suggestions and ideas to people related in revenue planning any firm and NTC. Proper applicability of Revenue planning system in the public enterprises

## **1.9 Limitations of the Study:**

In this dynamic world, nothing existing is free from information. This study also is not an exception. The researcher has however tried to eliminate the limitation to the best possible extent, yet it suffers from the following limitations.

1. The study is made for partial fulfillment of the requirements of master in business study, in short of time. Therefore, Nepal telecom Limited has been taken for this study.
2. Only the Revenue planning aspect of the Nepal Telecom Limited has been analyzed, leaving other area uncovered.
3. The study covers the related data of Nepal Telecom Limited from 2000/2001 to 2005/2006.
4. All the data have been used from secondary: there may be the question of accuracy of the data
4. The accuracy of this study is based on the data available from the managements of Nepal Telecom Limited.
5. The various published documents of the NTC and the response made by the respondent during the informal discussion.

## **1.10 Organization of the Study:**

The study divides into following chapters.

**Chapter I:** First chapter deals with the background of the study, statement of problem, objective of the study, significance of the study, research hypothesis, limitation of the study, and scheme of the study.

**Chapter II:** Second chapter deals with available literature review. It include conceptual framework, review of the published and unpublished books, journals, articles, previous unpublished masters' degree thesis etc.

**Chapter III:** Third chapter explains the research methodology used in the study, which includes research design, sources of data, population and samples, data analysis tools etc.

**Chapter IV:** Fourth chapter is the heart of the study. This chapter includes presentation and analysis of data using different financial and statistical tools.

**Chapter V:** Last chapter revolves with suggestion, which includes the summary of the main findings conclusion of the study and recommendations. Bibliography & appendixes have been included at the end of the study.

## CHAPTER – II

### REVIEW OF LITERATURE

#### **2.1 Introduction:**

Review of the literature is supported to revise the eminent literature relating to the study various books, articles, journals, bulletins, reports, news, paper and theses etc. which are the bases for preparing it .some philosophers, writers or researchers have given the contribution on it since many years. There are two parts in the review of literature. They are-

- Conceptual frame work
- Review of related study

#### **2.1.1 Conceptual Framework:**

In this chapter, the researcher aims to shed light on the relevant theoretical background of the study being under taken. It comprises the conceptual framework about the Telecom, its activities, profit-planning concepts, and review of books, previous study. So far, this study is concerned with reviewing the Revenue planning of Nepal Telecom. In this connection, the researcher has reviewed various literatures in the form of books, newspapers, journals, browsing materials from the concerned websites, previous dissertations in the relevant subject matters etc.

#### **2.1.2 Budget or plan:**

The sales Plan is the foundation for periodic planning in the firms because practically all other enterprises planning is built on it. All the other plans and budget are depending upon the sales budget. The budget is usually presented in both units and dollar of the sales revenue or sales volume. The preparation of sales plan is based upon the sales forecasts. It is also known as corner stone for all the other budgets. That is because the production level and the inventory level and hence manufacturing costs as well as non-manufacturing costs generally depend on the forecasted level of unit's sales or revenue.

The sales planning process is a necessary part of PPC because

- a) It provides further basic management decisions about marketing.
- b) Based on those decisions, it is an organized approach for developing a comprehensive sales plan. If the plan is not realistic, most if not all the other parts of the overall profit plan also are not realistic. Therefore, if management believes that, a realistic sales plan cannot be developed; there is little justification of PPC.

**Primary objective of sales budgets are as follows:**

1. To reduce uncertainty about future revenue.
2. To incorporate management judgment and decision into the planning process.
3. To provide necessary information for developing other elements of a comprehensive profit plan.
4. To facilitate management in controlling sales activities.

### **2.1.3 Panning vs. Sales Forecasting:**

Sales plan for any period starts from the analysis of the past trend, economy & expectation of future phenomenon and future forecasting. Sales forecasting known as prediction, estimation and expectation for future related to sales.

Sales planning and forecasting often are confused. Although related, they have distinctly different purpose. A forecast is not a plan rather it is a statement and or a quantified assessment of future conditions about particular subjects i.e. sales revenue based on one or more explicit assumption. A forecast should always state the assumption upon which it is based. Forecast should be viewed as only one input into the development of sales plan. The management of a company may accept common modify or reject the forecast. In contrast, a sales plan incorporates management decisions that are based on the forecast, other inputs and management judgment about such related terms as sales volume, price sales efforts production and financing

### **2.1.4 Strategic or long-range sales plan:**

A comprehensive sales plan includes both strategic and technical sales plan. Strategic sales plan is known as long-range sales plan. Usually it is 5 to 10 years. As a practical approach, a company may schedule completion of strategic long-term sales plan as one of the first steps in overall planning process. Long-term sales plan are usually developed as annual amounts.

The long term sales plan uses broad grouping of products (product lines) with separate consideration of major and new product and services. Usually it required depth analysis of future market potential, which may build up from a foundation such as population changes, state of economy, industry projections and finally company objectives. Long-term management strategies would affect such areas as long term pricing policy, development of new product and innovation of present products, new directions in marketing efforts, expansion or changes in distribution channels and cost patterns. The influence of managerial strategy decision is explicitly brought to bear on the long term sales plan primarily on a judgmental basis.

### **Tactical or short-range sales plan**

In planning short range or tactical sales plan, one should consider its long-range sales plan. A common approach used for short time horizons in a company is to plan sales for twelve months into the future, detailing the plan initially by quarter and months for the first quarter. At the end of each month or quarter throughout the year, the sales plan is restudied and revised by adding a period in the future and by dropping the period just ended. Thus tactical sales plan are usually subject to review and revision on a quarterly basis. The short-term sales plan includes a detailed plan for each major products and or grouping of minor products. Short-term sales plans are usually developed in terms of physical units (or jobs) and in sales and or service dollars.

A short-range sales plan should include considerable detail, whereas a long-range plan should be in board terms.

## **Developing comprehensive sales plan**

A comprehensive sales plan should satisfy the requirements of, and be consistent with, the overall comprehensive PPC program. A comprehensive sales plan should be based on foundation established by management. The foundation components of comprehensive sales plan are:

1. External variables identified and evaluated.
2. Broad enterprise objectives and goals formulation.
3. Strategic for the company development.
4. Planning premises specified.

## **General steps in developing of comprehensive sales plan**

1. Develop management guidelines specific to sales planning including the sales planning process and planning responsibility.
2. Prepare one (or more) sales (market) forecast consistent with specified forecasting guidelines including assumptions.
3. Assemble all the other data that will be relevant in developing a comprehensive sales plan.
4. Based on steps 1, 2 and 3 above apply management evaluation and judgment to develop a comprehensive sales plan.
5. Secure managerial commitment to attain the goals specified in the comprehensive sales plan.

These steps must be revised and implemented in various ways depending upon the characteristics of the organization and the expertise of the management.

## **Methods of Projecting Sales**

Methods of projecting sales may vary with nature of organization, organizational structure of the business etc. In general, these methods can be used for forecasting of sales in an organization:

### **1. Judgement Method:**

Judgment method is also known as personal judgment method a rule of thumb method, non-mathematical method, or directorship method. In this method, sales projection is made based on personal judgment of executive person responsible for sales forecasting. Under this method, these techniques are used:

#### ***a. Sales force composite***

In this method, sales forecast is made by personal judgment of sales person involved in the field of marketing.

#### ***b. Sales division managers composite***

Under this method, sales forecast is made by sales department executive based on collecting relevant information regarding product market.

#### ***c. chief executive decision***

From the available proposed sales forecast by sales person and sales department executive, chief executive decision about the future projected level of sales.

### **2. Mathematical and Statistical Approaches:**

Under this approach statistical and mathematical tools for projection of sales, there are some usually followed statistical methods for projection of sales:

#### ***A. Economic rhythm method***

Under this method, future sales projection is made based on rhythmic change in economic i.e. Cyclical variance, seasonal variance, price variance etc.



### ***B. Special historical analogy***

Under this method past history is taken for forecasting future sales based on same future expected phenomena of the economy.

### ***C. cross cut method.***

Under this method, future sales are projected based on drawing a best-fit line of the past sales and by a diagonal cut between diagrams. Time series can be under this taken as one of the example of cross cut method.

### ***D. Correlation method.***

This is the most used statistical tools for forecasting future on the basis of establishment of the interrelationship between dependent variable i.e. sales and independent variable i.e. demand, price change, product life cycle, market share, substitute product in the market etc.

## **3. Special purpose method:**

Under this method, managerial purpose of sales forecast is taken in high focus for projecting future sales. These three methods are taken under this approach.

### ***A. Industry analysis***

Generally multinational companies use this method of forecasting future sales, which operates in high competition and highly affected by international economy and technology change,

### ***B. Product line analysis***

Business, which has more than one product and each product, has separate identity in the market usages product line forecasting for forecasting sales of any specific product group.

### ***C. End use analysis:***

Under this method of a projection of own sales is made after analysis or projection of customers consumption. Based on future demand sales is forecasted under end use method.

### **Combined Method:**

As per the need and nature of business and available resource, company may use combination of more than one method mentioned above for projection of its future sales.

### **Factors Affecting Sales Forecast and Sales Plan or Sales Budget:**

A sales plan is prepared for the sales forecast. A sales forecast is broader than a sales budget; generally encompassing potential sales for the entire industry, as well as potential sales for the firm is forecast of sales. Forecast that are to be considered in making a sales forecast include:

1. Past experience in terms of sales volume.
2. Prospective pricing policy
3. Unfilled order backing
4. Market research studies.
5. General economic conditions.
6. Industry economic condition.
7. Movement of economic indicator such as gross national product, employment, prices, and personal income.
8. Advertising and product promotion.
9. Industry competition
10. Market share.

While preparing sales plan following points are to be considered.

1. Price cost volume consideration:

In a competitive market, the price and sales volume are mutually interdependent. Because sales volume and price are so closely tied together, a complicated problem is posed for

the management of almost all company. Thus, two basic relationships involving the sales plan must be considered (i) estimation of the demand curve that is the extent to which sales volume varies at different offering prices and (ii) the unit cost curve, which varies with the level of productive output.

## 2. Product line consideration:

Determination of the number and variety of product that a company will plan to sell is crucial in the development of sales plan. Sales plan must include tentative decision about new product lines to be introduced old product lines to be dropped, innovations and product mix.

### **2.1.5 Expenses budget and plan:**

In the comprehensive profit planning or budgeting, expenses budget also play important role. There are different categories of expenses based on objectives of use. However, there are three main categories of expenses

1. Factory or manufacturing overhead
2. General administrative expenses
3. Selling and distribution expenses.

Nevertheless, for the efficient planning and controlling of expenses it is necessary to further classify expenses on the following basis:

1. Based on controllability.
  - a. Controllable expenses.
  - b. Uncontrollable expenses.
  
2. Based on behavior
  - a. Variable expenses.
  - b. Fixed expenses.
  - c. Semi variable or mixed expenses.
  
3. Based on traceability
  - a. Direct expenses.
  - b. Indirect expenses.

In manufacturing organizations there are mainly, two-responsibility center exists. First, one is production department and another is service department.

### **2.1.6 Selling and distribution expenses budget:**

All the expense incurred in course of delivery of goods to the consumer is selling and distribution expenses. This budget is association with the sales budget. The two primary aspect of planning and distribution expenses budget are as follows:

#### **A. Planning and coordination:**

In the development of the tactical plan, it is essential that a favorable economic balance be achieved between sales efforts (expense) and sales result (revenue).

#### **B. Control of distribution expenses**

A side from planning consideration, it is important that serious efforts be given to controlling distribution expenses budget. Control is especially important, since

- a. Distribution expenses are frequently a significance expenses of total expenses and
- b. Both sales management and sales personals tend to view such expenses lightly, in some cases extravagant, such as entertainment expenses. Distribution expense control involves the same principle of control as manufacturing overhead. Control must be build around the concept of.
  - c. responsibility centre and
  - d. Expense objective.

### **2.1.7 Administrative Expense Budget or Plan:**

Administrative expenses budget includes all the expenses other that manufacturing and selling distribution expenses budget. Administrative expenses are incurred in the responsibility centers that provides supervision of and service to all functions of the enterprise rather than in the performance of any one function. Because a large portion of

administrative expenses is fixed rather than variable, the notion persists that they cannot be controlled. Aside from certain top management salaries, most administrative expense is determined by management decision.

General administrative expense is close to top management; therefore, there is strong tendency to overlook their magnitude and effect on profit. Each administrative expense should be directly identified with a responsibility centre, and the centre manager should be responsible for planning and controlling expense.

### **2.1.8 Capital Expenditure Budget or Plan:**

The investment in fixed assets is known as capital expenditure decision. A fixed asset means assets that have more than one year service life. Planning regarding capital expenditure is known as capital budgeting.

Capital budgeting consists in planning the deployment of available capital for the purpose of maximizing the long-term profitability (return on investment) of the firm.

The term capital investment refers broadly to large expenditure made to purchase plant assets, develop new product lines, or acquire subsidiary companies. Such decision commits financial resource for large period and is difficult, it is not impossible, to reverse once the funds are invested. Thus, companies stand to benefit from good capital investments (or suffer from poor ones). From many years.

The process of evaluating and prioritizing capital investment opportunities is called capital expenditure. Capital budgeting relies heavily on estimates of future operating results. These estimates often involve a considerable degree of uncertainty and should be evaluated accordingly (Williams, Haka and Bettner, 2004:1022).

The capital expenditure budget (or plan) is an important part of a comprehensive profit plan. It is directly related to a company's operating assets, especially land, equipment and other operating assets and cash.

### **2.1.9 Cash Budget or Plan:**

Cash is one of the important assets of any enterprise. It is also considered as lifeblood of any enterprise. Therefore, cash management is very important for any management. Cash budget is the one of the important way for effective cash management. Cash budget helps for effecting plan of cash i.e. maximum utilization of cash and arrangement of needed cash efficiently. The cash budget is based on other functional budget where cash involved is essential. Cash budget has three main parts consisting of (i) cash receipts (ii) cash disbursement and (iii) cash balance. There are two different approach of cash management. First, one is cash budget approach and another one is financial accounting approach.

### **2.2 Profit Planning as a concept:**

Profit planning involves selection of defined periods for the strategic and tactical profit plans (often five years and one year, respectively) in other words profit planning is a comprehensive statement of intentions expressed in financial terms for the operation of both short and long period. It is a plan of the firm's expectation and is used as a basis for measuring the actual performance of managers and their units. A profit plan has an immense value in management; it helps in planning and co-coordinating if used appropriate, but not a replacement for management. Profit planning is a comprehensive and co-coordinated plan expressed in financial terms, for the operations and resource of an enterprise for some specific period in the future. A profit plan or budget is the formal expression of the enterprises plans and objectives stated in financial terms for a specified future period of time (Fremgen, 1973:144).

Profit planning is a predetermined detailed plan of action developed and distributed as a guide to current operations and as a partial basis for the subsequent is a tool which may be used by the management in planning the future course of actions and controlling the actual performance (Gupta, 1992:521).

Profit plan is estimation, predetermination of revenues and expenses that estimates how much income will be generated, and how it should be spent in order to meet investment and profit requirements. In the case of institutional operations, it presents a plan for spending income in a manner that does not result in a loss.

The term comprehensive profit planning and control is defined as a systematic and formalized approach for performing significant phase of the management planning and control functions specially it involves:

- The development and application of broad and long-range objectives of the enterprise.
- The development of strategic long range profit plan in broad terms.
- The specification of enterprises goals.
- The specification of tactical short-range profit plan detailed by assigned responsibility (Division, Products, projects).
- The establishment of a system of periodic performance reports detailed by assigned responsibility and follow up procedures.

In many of the better-managed companies, comprehensive PPC has been identified as a way of managing it focuses directly up on a rational and systematic approach to management by objectives and realistic flexibility in performing the management process.

A profit planning and control program can be one of the more effective communications network is in an enterprise. Communication for effective planning and control requires that both the executive and the subordinate have the same understanding of responsibilities, ensures a degree of understanding not otherwise possible. Full and open reporting in performance reports that, focus on assigned responsibilities likewise enhance the degree of communication essential to sound management.

Profit planning is an example of short range planning. This planning focuses on improving the profit especially from a particular product over a relatively

short period. Therefore as used here, it is not the same as corporate planning of a cost rendition program (Terry, 1968:2).

Profit planning involves streamlining activities in order to get employees profit minded and to secure maximum benefit from minimum effort and expenditure. Best results seem to be obtained by assigning a profit planner to investigate all the factors affecting the profit obtained from a single production the planner is given the right to probe the economics, the organization. The mode of operations, the pricing, the marketing or any fact of making and selling the product that in his judgment affects profit accruing from that product. The concentration of profit efforts upon one product and the fight of the planner to cross-traditional functional boundaries of the enterprise to translate needs from one group to another and to obtain concurred profit building efforts among those who can affect profits are the fundamental factors that contribute to the success of profit planning.

A profit plan is an advance decision of expected achievement based on the most efficient operating standards in effect or and prospect of time it is established against which actual accomplishment is regularly compared.

Profit Planning through volume of cost analysis, however, is a modern concept of management planning tools designated primarily for industrial enterprises. It involves a study of what a business cost and expenses should be and will be at different level of operations and it include a study of the resultant effect up to due to this hanging relationships between volume and cost.

### **2.2.1 Profit**

#### **Meaning and Concept of profit:**

Profit is as important to a firm as water to the fish. Profits are the excess of income over cost of production and services. Profit is the amount available for ownership or equity after payments are made to all other factors used by the firm. Profit is the basic elements of profit plan so that the concept of profit planning may not be complete idea of profit.



According to oxford dictionary, profit means a) financial gain b) amount of money gained in business especially spent. Advantage or benefits gained from something (Hornby; 1992: 5.67).

Profit is the reward for risk taking in business. If the entrepreneur does not receive the reward, he will not be prepared to undertake the risks involved in the business. This profit of the entrepreneur exceeds the ordinary return on capital. Entrepreneur would not be ready to undertake the risks (F. B. Hawley).

According to Schumpeter, profit is the reward for innovations. The objective of innovation is to reduce cost of production and cause gap between existing price of the commodity and its new cost. The innovation may come in many forms, such as introduction of new production technique, or a new machine, or plan, a change in internal organizational structure of the firm.

Profits around which all enterprises activities directly or indirectly revolve play the significant role for judging the managerial efficiency. In absence of profit, nobody can think about the long-term survivability of the enterprises.

### **2.2.2 Planning:**

Planning is the process of developing enterprises objectives and selecting a future course of action to accomplish them. It includes developing premises about the environment in which they are to be accomplished. Planning is the foundation of PPC. We should be clear in the concept of planning. According to oxford Dictionary, Planning means:

- (To do something) arrangement for doing or using something, considered or worked out in advance.
- Why of arrangement something especially when shown on a drawing scheme.
- Go according to plan (Hornby; 1992: 5.45).

Planning is deciding in advance what is to be done in future (Bhusan, 1976: 362).

A planning process includes setting goals, evaluating resources forecasting by different methods and formulating a master plan. Planning depends upon the organized objectives. For the planning purpose a firm's objectives can distinguish mainly three, the first is

prime, the second is instrumental objectives are aims for accomplishment of more basic aim. For this purpose, the company has established divisional departmental and individual job objectives. Specific objectives are those objectives that have been specified as to time and magnitude, which is known as goals. Because of specifying a period and a target amount, this goal is capable of giving specific guidance to various senses of management planning. Objective setting of a firm is very difficult. Unfortunately, most top management fails to develop a clear and operational statement of company objectives. More carefulness is necessary for this tedious job. Carefully stated firm's objectives would yield at least the following benefits.

- Company objectives provide the ultimate criteria for resolving difficult company decisions and
- Company objectives are the basis for long-range profit planning.
- Planning is the process of developing enterprises objectives and selecting future course of action to accomplish them. It includes.
- Establishing enterprises objectives,
- Developing premises about the environment in which they are to be accomplished,
- Decision-making.
- Identifying activities necessary to translate plans into action, and
- Current re-planning to current deficiencies.

The planning processes both short and long term is the most crucial component of the whole system. It is both foundation and the bond for the other elements because it is through the planning process that we determine what we are going to do. How we are going to do it and who is going to do it and who is going to do it. It operates as the brain centre of an organization and like the brain it both reasons and communicates.

Planning is the conscious recognition of the futurity of present decision. Planning is the feed forward process to reduce uncertainty about the future. The planning process is based on the conviction that management can plan its activities and conditions that state of the enterprise that determines its destiny (Pandey, 1991: 554).

Planning could be taken as the tools of achieving organizational goals efficiently and effectively from the selection of various alternatives within an acceptable period. Planning consists in setting goal for the firm both immediate and long-range considering the various means by which such goals may be achieved and deciding which of any variables alternatives means would be best suited to the condition expressed prevail.

**The essence of planning is:**

1. To accomplish goals
2. To reduce uncertainty
3. To provide direction by determining the course of action in advance.

Planning is determined course of action for achieving organizational goals or objectives effectively and efficiently at a fluid environment with a certain period through the selection of various alternatives. On the other hand, it holds accountability and responsibility about result to individual. A full appreciation of the firm task requires distinguishing among three types of company's activities, which we call strategic planning, management control and operational control. The strategic planning is an important function of top management. Planning requires the management to setting a future state toward which effort will be directed i.e. objective, assessing the organization's resources, i.e. what the organization is going to work with, assessing the current and lately' determine how and when to allocate resource accomplish the objective. Planning on the other hand is selecting objective and determining a course of action including allocation resources in order to achieve those objectives in a specific time. Planning states what, when, and how things will be accomplished. An adequate planning is necessary for control of operations.

## **2.2.3 Types of planning:**

### **I . Corporate planning**

Corporate planning means the systematic process of setting corporate objectives and making strategic decisions and developing the plans necessary to achieve these objectives.

Corporate planning is one part of profit plan. It was first started in the USA in 1950, and it is however being used in one form or another in many companies there.

Corporate planning is to determine the long-term goals of a company as a whole and then to generate plan designated to achieve these goals bearing in mind probable change in its environment. He pointed out the premises of the corporate planning are:

- Before drawing up a plan, which is designed to do something, decide what you want it to do.
- In these days of rapid change, it is necessary to look ahead as far a possible to anticipate these changes.
- Instead of treating a company as a collection of department, treat it as a corporate whole.
- Take full account of the company's environment before doing up any up any plan (Robertson,1968; 535).
- Long term planning is included in corporate planning. Corporate planning often is considered synonymous with long-tern planning. The main objectives of corporate planning are as follows.
- Achieving objectives.
- Embodiment of goals and objectives in the Enterprises.
- Formulating realistic and attainable objectives.
- Clarity and adequacy of goals and objectives.
- Communication of goals and objectives.
- Involvement of personnel in developing the goals of the enterprises.

## **II. Strategic long range planning**

Strategic plan is a road map for the future of the organization. It is a long range plan for five years and more. Top management prepares it. It is the means for implementing corporate strategy. It provides broad direction to take the organization where it wants to be in the long run. Its thrust is to search sustainable competitive advantage for the organization.

Strategic plan establishes overall mission, objectives and strategy for an organization. It makes strategic choice about future courses of action from among the relevant strategies. Policies for acquisition and deployment of resources are also specified.

- Mission is the reason for the existence of an organization. It identifies product, customer and competitive advantage.
- Objectives are desired outcomes in terms of results to be achieved strategies are broad plans to achieve objectives.

Strategic planning is the careful, deliberate, systematic taking of decisions which affect or are intended to affect the organization as a whole over long period of time (Steiner & Miner: 1972: 5.15). Strategic planning is the formalized long range planning process used to define and achieve organizational goals

Basically, the long range planning is more important for broad and long living enterprises. A long-range planning is closely concerned with the concept of the corporation as a long living institution the planner must include the following factors in his plan from the analysis of available information.

- a. Probable future opportunity.
- b. Uncertainty and
- c. Challengers.

Strategic planning is a decision making process such decision should be related about

- Determination of goals, objectives and strategies.
- The level and direction of capital expenditure.
- The accession of new sources of funds
- Organization design and structure etc.

### **III. Tactical (short term) planning**

Tactical plan is a short-range plan. It is developed for a short period of time usually a year, initially by quarters and by months for the first quarter. A tactical planning is done at all level and involves directing the organizations activities to achieve overall it strategic objectives consistent with the organization's mission and policies. Standing plans provides consistency by and efficiency for non-going operations, and single use plans are developed for unique situation. Projects are short-term plans designed to achieve objective within large-scale programs. Short-term plans cover about a year, and are less formal and detailed than long-range plans, which usually cover more than three months. The short range planning is selected to conform to fiscal quarter for years. Because of the practical needed for conforming plans to accounting periods and the some. What arbitrary limitation of the long range to three to five years is usually based as has been indicated on the prevailing belief that the degree of uncertainty over along period makes planning of questionable value.

#### **2.2.4 The Role of Forecasting in Planning:**

The forecasting is to take future decision at present from the analysis of relevant factors of past and present situation. It is an integral part of decision-making activities of management.

An organization established goals and objectives seeks to predict the environmental factors that selects action all that is hopes will result in attainment of goals and objectives. The need for forecasting is increasing as management attempts to decrease its dependence on change and become more scientific in dealing with its environment. Since each area of organization is related to all others. A good or bad forecast can effect the entire organization.

It should be realized that building is not merely forecasting although forecasting is form of he basis of budgeting. Forecasting is estimate of the future environment with in which the company will operate. Budgeting or planning on the other hand involves the

determination of what should be done, how the goals may be reached and what individual units are to be assumed responsible and be held accountable. Budget provides orderly way to attain goals and provides a time schedule for future action to produce (Pandey; 1991: 576).

Forecasting is indispensable in planning. Forecasts are statement of expected future conditions definite statements of what will actually happen are partially impossible. Expectations depend upon the assumptions made. If the assumptions are possible, the forecast has a better chance of being useful forecasting assumptions and techniques vary with the kind of planning needed.

The short-term forecasting is needed in budget making. A budget set for the following year will be much useful. It is regarded to sales levels, which will eventuate rather than near to current sales level. As budget distributed according to current sales may establish policy as to lines of emphasis, but will obviously, required successive adjustment if sales levels changes.

### **2.2.5 Forecasting Vs planning:**

Planning and forecasting often are confusing of being the same. Nevertheless, forecast is not a plan, rather is it a statement and for a quantified assessment of future conditions about a particular subject based on one or more explicit assumptions, planning on the other hand, involves the use of forecast to help to make good decisions about most attractive alternatives for the organization. Thus, a forecast seeks to describe what will happen, where as a plan is based on the notion that by taking certain action how the decision maker can affect subsequent events in a given situation and thus influence the final results, in the direction desired. Generally speaking, forecasting and forecasts are inputs to the planning purpose.

### **2.3 Purpose of Profit Planning:**

A comprehensive profit planning is a systematic and formularized approach for stating and communicating the firm's expectation and accomplishing management in such a way to maximize the use of a profit plan and to achieve the maximum benefit from the resources available to an organization over a particular span of time. The maximum

objective of profit planning is to assist in systematic planning and controlling the operations of the enterprise. The purposes for the application of profit planning are:

- To state the firm's expectation (goal) in formal terms clearly to avoid confusion and facilitate their attainment.
- To communicate expectation to all concerned with the management to the firm so that they understand, support and implement.
- To provide a detailed plan of action for reducing uncertainty and for its proper direction of individual and group efforts to achieve goals.
- To coordinate the activities and efforts in such a way that the use of resources is maximized.
- To provide a means of measuring and controlling the performance of individuals and units and to supply information based on which the corrective action can be taken.

### **2.3.1 Long range and short range profit plan**

Two types of plans are developed; one strategic (long-range) and another tactical short range. The former profit plan takes a time horizon of 5 to 20 years and the latter for short period. The long range planning is a picture of more summary data. A part of this plan is more or less informal as presented by tentative commitments made by the executive committee in the organizational planning season. The formal portion of long-range profit plan includes the following component detailed by each year.

- Income statement
- Balance sheet
- Capital Expenditure plan
- Personal Requirements
- Research plan and
- Long Range Market Penetration plan

Thus, the long range profit plan covers all the area of anticipated activity; sales expenses, research and development, capital expenditure, cash, profit and return on investment.



The short-range tactical profit plan shows the primarily annual results, the detail by months, responsibility and products; in an organization, these annual summaries should be prepared.

To provide a general understanding of the profit plan and to provide an overall view of the comprehensive short-range profit plan.

According to Galenn and other, it is possible for the firms to develop these two profit plans for all aspects of the operations. Assuming participatory planning and receipt of the executive instruments, the manager of each responsibility center will immediately initiate activities within his or her responsibility center to develop strategic profit plan and tactical profit plan. Certain format and normally the financial function should establish the, general format, amount of detail, and other relevant procedural and format requirements essentially for aggregation of the plan. All these activities must be coordinating among the centers in conformity with the organization structure.

The preparation of long-rang profit planning in addition to short range profit planning is also viewed as a total planning concept of business. Long range planning is essential to maintain the annual profit at improving level. The ultimate measure of the success of a business in generally based on growth in the volume of sales, increasing return on capital investment, efficient organization and these are all long-term consideration.

## **2.4 Budgetary Control:**

### **2.4.1 Meaning of Budgeting and Budget:**

A budget is a detailed plan outlining the acquisition and use of financial and other resources over a given period. It represents the plan for the future expressed informal quantities terms. The act of preparing a budget is called budgeting. The uses of a budget to control a firm's activities are known as budgetary control.

A budget is a detailed plan expressed in quantitative terms that specifies how resources will be acquired and used during a specified period of time. The procedures used to develop a budget constitute a budgeting system (Hilton, 2001:404).

According to fremgen, a budget is the quantitative expression of a proposed plan of action by management for a future time and is an aid to the coordination and implementation of the plan. Budget is defined as a comprehensive and coordinated plan, expressed in financial terms for the operations and resources of enterprises for some specified period in the future.

According to his definition the essential elements of a budget are:

- Plan
- Operation and resources
- Financial terms
- Specified future period
- Cooperation

Therefore, we can say that budget is a quantitative expression of a plan of action and an aid coordination and control. Basically, budgets are forecasted financial statement formal expressions of managerial plans.

### **Budgeting: As a Device of Profit Plan**

Budgeting, as a tool of planning, is closely related to the broader system of planning in an organization. It serves basically as a device for management, control; it is rather pivot of any effective scheme of control. Budgeting is the principle tool of planning and control offered to management by accounting function (Welsch, et al; 2004: 632). The prime objective of budgeting is to assist in systematic planning and in controlling the operations of the enterprises. In fact budgeting is best sources of communication and an important tool in the hands of management. Since, budgeting deals with fundamental polices and objectives, it is prepared by top management. A formal budget by itself will not ensure that a firm's operations will be automatically geared to the achievement of the goals set in the budget. For this to happen, the top-level managers and lower level employees have to understand the goals and support them and coordinate their efforts to attain them.

A budget is comprehensive in that all the activities and operations of an organization are included in it. It covers the organization as a whole and not only some segments. The budgets are prepared for each segment of an organization. These are integrated into an overall budget for the entire organization. The overall budget is referred to as the master

budget. Budgeting is a device of a planning and control that serves as a guide to conduct operation and a basis for evaluating actual results.

The main objectives of budgeting are:

Explicit statement of expectations

- I. Communication
- II. Coordination
- III. Expectations as a framework for judging performance

#### **2.4.2 Essentials of an Effective Budgeting:**

An effective budgeting system should have some essential to ensure best results. The following are the chief characteristics of an effective budgeting.

- A. Sound forecasting
- B. An Adequate and planned Accounting System
- C. Efficient Organization with Definite lines of Responsibility
- D. Formation of budget committee
- E. Clearly defined business policies
- F. Availability of statistical information
- G. Support of top management
- H. Good reporting systems
- I. Motivational approach

#### **A. Sound forecasting**

Forecasts are the foundation of budgets, these forecasts are discussed by the executives and when most profitable combinations of forecasts are selected they become budgets. The sounder are the forecasts better results would out of the budgeting system.

#### **B. An Adequate and Planned Accounting System**

There should be proper flow of accurate and timely information in the enterprise, which is, must for the preparation of budgets. Only having an adequate and planned accounting system in the firm can ensure this.

### **C. Efficient Organization with Definite Lines of Responsibility**

An efficient adequate and best organization is imperative for budget preparation and its operation. Thus a budgeting system should always be supported by a sound organization structure demarcating clearly the lines of Authority and responsibility Not only this, there should be a true delegation of authority from top to low levels of management. This will provide adequate opportunity to all executives to make decisions and to participate in the function of budget preparation. Thus, an efficient organization helps not only in budget co-ordination but also plays important role in budget co-ordination and operation.

### **D. Formation of Budget Committee**

As mentioned earlier, Budget committee receives the forecasts and targets of each department as well as periodic reports and finalizes. In addition, approves the departmental budget. Thus in order to make a budgeting system more and more effective, a budget committee should always be set up.

### **E. Clearly Defined Business Policies**

Every budget reflects the business policies formulated by the top management. In other words, budgets should always prepare taking in to account the policies set for particular department or functions. Nevertheless, for this purpose, policies should be precise and clearly defined as well s free from any ambiguity.

### **F. Availability of Statistical Information**

Since budgets are always prepared and expressed in quantitative terms. It is necessary that sufficient and accurate relevant that should be made available to each department. Such date may not be available from accounting system alone and therefore they may be processed through statistical techniques. These data should be as far as possible, reliable accurate and adequate.

### **G. Support of Top Management**

If a budget program is to be made successful, the sympathy of each member of the management team towards it should starts preferably from top i.e. chairperson. The

enthusiasm for budget operation as well as direction for it should initiate and come from top.

## **H. Good Reporting Systems**

An effective budgeting system also requires the presence of a proper feedback system. As work proceeds in the budget period, actual performance should not only be recorded but it should also be compared with budgeted performance. The variations should be reported promptly and clearly to the appropriate levels of management.

## **I. Motivational Approach**

All the employees or staff other than executives should be strongly a properly motivated towards budgeting system. In an organization, it is needed to make each staff member feel too much involved in the budgeting system. To meet this end, motivational approach towards budgeting should be followed.

## **2.5 Fundamental Concepts of Profit Planning:**

The fundamental concepts of PPC include the underlying activities or tasks must generally be carried out to attain maximum usefulness from PPC. These fundamentals have never been fully codified. An outline of the fundamental concepts of profit planning and control are:

1. Managerial involvement and commitment
2. Organizational adaptation
3. Responsibility accounting
4. Full communication
5. Realistic expectation
6. Flexible application
7. Timeless
8. Individual and group recognition
9. Zero base budgeting
10. Activity costing
11. Behavioral view point

12. Management control using PPC

13. Follow up

( Goet, et al; 2062:1.3)

Each of these fundamentals is discussed briefly in the following paragraphs. Moreover, it has tried to proof to what extent they are playing the role to make PPC a meaning full and a comprehensive approach.

### **Managerial involvement and commitment:**

Managerial involvement entails managerial support, confidence, and participation and performance orientation. All levels of management especially top-level management should consider following points in order to make PPC program successful. Managerial support, confidence, participations and performance orientations include managerial involvement. All level of management especially top-level management should consider following points in order to make PPC program successful.

- Understand the nature and characteristics of profit planning and control.
- Be convinced that this particular approach to manage is preferable for their situation.
- Be willing to devote the effort required to make it operative.
- Support the program in all its ramifications.
- View the results of the planning process as performance commitments.

For the comprehensive profit planning and control (PPC) program to be successful it must have the full support of each a members of management, starting with the president the impetus and direction most come from the very top (Goet, et al; 2062: 1.4).

### **Organizational adaptation**

A profit planning and control programmed depend upon sound organizational structure for the enterprise and a clear-cut designation of lines of authorities and responsibilities. The purpose of organizational structure and the assignment of authority are to establish a framework with in which enterprise objectives may be attained in a co-ordinate and

effective way on a continuing basis. The responsibility for the obligation of each departmental manager should be well clarified. Whatever may be the nature and sense of organizational structure, one should always bear in mind the fact that no organizational structure can be taken as ends itself but it should always be treated as means or tools to attain the goal. In conclusion the organizational involvement includes.

- Delegation of authority and responsibility to each functional sub. Units.
- Sub-divide the whole organization into different functional subunits
- Each subunits should prepare its own annual or periodic plan
- Based upon plan prepared by subunits a master plan is to be prepared by higher management (Goet, et al; 2062: 1.4).

### **Responsibility Accounting**

In order to set up profit planning and control on a sound basis, there must be a responsibility accounting system that is one tailored primarily to the organizational responsibilities. A responsibility accounting system can be designed and implemented on a relevant basis regardless of the accounting system standard cost system, direct costing systems, and so on. Therefore, PPC requires responsibility accounting system.

### **Full Communication**

Communication can be defined as an interchange of thought or information to bring about a mutual understanding between two or more parties.

Communication can be either of dialogue messages or understanding from working together. Although most of the management gives least importance on communication but it is the most important thing for any organization observation and control. Most of the organization faces lot of problem due to bad communication system.

For profit planning and control; effective communication means development of well-defined objectives specification of goals, development of profit plans and reporting and follow up activities related to performance evaluation for each responsibility center. Communication for effective planning and control requires same understanding of responsibilities and goals in both the executives and subordinates.

## **Realistic Expectation**

Perfection on setting goal or objectives of the future sales, production levels, costs, capital expenditures, cash flow and so on determines the success of profit planning and control programmed. So, for profit planning and control purpose, a realistic approach with time dimension and external and internal environment that will prevail during the time span should be considered. This is called realistic expectation.

## **Timeliness**

Time and Tide wait for none'. Whether an individual or an entity remains idle or busy, time passes at the same rate. The problem of the manager in one hand is to accomplish the planned activities in a given time and on the other hand is to prepare the plan itself phasing of the planning is of two types:

- Timing of planning horizons and
- Timing of planning activities.

Planning horizons refers to the period of time into the future for which management should plan. Decision made to the organizations obviously can affect only the future. No present decisions can effects or change the past, since all managerial decisions are futuristic, each management is faced with the basic question of time dimension. The effective implementation of PPC concepts requires that the management of ES establish a definite time dimension for certain types of decision. And timing of planning activities suggests that there should be a definite management time schedule established for initiating and completing certain phases if the planning process (Goet, et al; 2062: 1.5).

## **Flexible Application**

The stress that a PPC programmed must not dominate the business and that flexibility in applying the plan must be forthright management policy. Therefore, those strait jackets are not imposed and all favorable opportunities are seized even through they are not covered by the budget. Rigidity in practicability will be the harmful boundary in an association in an occasion for the enterprises. So, such boundary should be avoided



which mean there should be flexibility in PPC so that the unseen golden opportunity should be grasped in future for the betterment of that organization (Goet, et al; 2062: 1.5).

### **Zero Base Budgeting**

Zero Base Budgeting is a method of budgeting in which managers are required to start from zero level every year and to justify all costs as if the programs involved were being initiated for the first time. Under zero-base budgeting, every budget is constructed on the premise that every activity in the budget must be justified. It starts with the basic premise that the budget for next year is zero and that every expenditure, old and new, must be justified based on its cost and benefit.

### **Activity Costing**

Responsibility accounting system generally accumulates costs by department and product costing systems associate costs with units of product or service organization also frequently finds it useful to associate costs with activities. By decomposing an organizations production process into discrete set of activities, and then associating costs with each of those activities. Moreover, by systematically identifying the activities through out the organizations managers can identify redundant activities (Welsch, et al; 2004: 42).

### **Individual and Group Recognition**

Behavioral aspects of human being are of the field of study of the psychologist, educators and businessperson, and finding was that there could be so many unknown misconception and speculations, which has to be considered for an efficient management. A good and dynamic leadership can resolve this problem by integrating all the group efforts for betterment of the organization.

### **Management control Using PPC**

The primary purpose of control is to ensure attainment of the objective, goals and standards of the enterprises. Control has many facets such as direct observation, oral

express, policies and procedures, reports of actual results and performance reports. PPC focuses on performance reporting and evaluation of performance to determine the causes of both high and low performance. The essential characteristics of a PPC performance reports are as follows (Welsch, et al; 2004: 40).

- Performance is classified by assigned responsibilities
- Controllable and non controllable items are designated
- Timely reports are issued.

Emphasis is given to a comparison of actual results and planned results should be designated the responsible manager and show actual results.

### **Behavioral viewpoint**

An ounce of behavior is better than a quintal of the theorem so ever be the theory and theorem, the organization only when it improves its behavior, is best or in another way Welsch has suggested that the motivation of human resources through dynamic leadership central to effective management. It is found by many psychologist and educators and businessmen that, there are many known and unknown, misconception and speculations concerning the responses of the individual and the group in the varying situation so the PPC programs bring many of these behavior problems in the sharp and focus and trying to resolve (Welsch, et al; 2004: 53).

### **Management by Exception**

A comprehensive profit planning and control program facilities in many ways, underlying these is the measurement of actual performance against planned objectives goals, and standards and the reporting if that measurement in performance reports. This measurement and reporting extends to all areas of operations and to all responsibility centers in the enterprises. It involves reporting

- a. Actual result
- b. Budgeted or planned results and
- c. The differences between the two

This type of reporting represents an effective application of the well-recognized management exception principle. The exception principle holds that the manager should concentrate primarily on the exceptional or unusual items that appear in daily, weekly and monthly reports, thereby leaving sufficient managerial time for overall policy and planning considerations. It is the 'out of line' items that need immediate managerial attention to determine causes and to take corrective action. The items that are not out of line need not utilize extensive management time, however; they should trigger "rewards" in appropriate ways. To implement the exception principle, techniques, Procedures must be adopted to call the manager attention to the 'out of control' items. Performance reports because they include a comparison of actual results with plans by areas of responsibility, emphasize in a relevant ways performance variation. The out of line items stand out. It is with respect to these items that the busy executive should investigate, determine the causes and take corrective action (Welsch, et al; 2004: 45).

## **Follow Up**

This fundamental holds that both good and substandard performance should be carefully investigated the purpose being three fold.

- In the case of substandard performance, to lead in a constructive manner to immediate corrective action.
- In the case of outstanding performance, to recognize it and perhaps provide for a transfer of knowledge to similar operation and
- To provide a basis for better planning and control in the future.

### **2.5.1 Profit Planning and Control Process:**

Profit planning and control process necessarily integrates the planning, leading and control function of management. A PPC program includes more than the traditional idea of a periodic or master budget. Rather, it encompasses the application of a number of related management concepts through a variety of approaches, techniques and sequential steps. These steps are outlined in this study in the following manner.

### **2.5.1.1 Identification and Evaluation of External Variables:**

It is discussed the distinction between external and internal variables for an enterprises. These variables exert major influences on an enterprise. The variable identification phase of the PPC process focuses on a) identifying and b) evaluating the effects of the external variables. Management planning must focus on how to manipulate the controllable variables. Variables, which have a direct and significant impact on the enterprises, are called relevant variables. Variables may have their different relevancy according to the market nature. For the enterprises purpose the external relevant variables are population, G.N.P. competitive activities product line, and industry sales. And so far internal variables are concerned employees, capital, research productivity, pricing operating costs, advertisements etc. a particularly significant phase of this analysis includes an evaluation of the present strength and weakness of the enterprises the comprehensive PPC approach is based on the expectation that these significant aspects of operations will be critically analyzed and evaluated periodically and in an orderly manner (Welsch, et al; 2004:74).

### **2.5.1.2 Development of the Broad Objectives of the Enterprises**

Development of the broad objectives of the enterprises is a responsibility of executive management. Based on a realistic evaluation of the relevant variables and an assessment of the strength and weakness of the organization, executive management, can specify or restate this phase of the PPC process.

The statement of broad objectives should express the mission, vision and ethical character of the enterprise. Its purpose is to provide enterprise identify continuity of purpose is to provide and definition. One research study listed the purpose of the statement essentially as follows.

1. To define of the purpose of the co.
2. To clarify the philosophy character of the Co.
3. To create particular climate with in the business.
4. To set down a guide for managers so that the decisions they make will reflect the best interest of the business with fairness and justice to those concerned (Welsch, et al; 2004: 75).

### **2.5.1.3 Development of Specific Goals for the Enterprises:**

This component of a comprehensive PPC process is to bring the statement of broad objectives into sharper focus and to move from the realm of general information to more specific planning information. It provides both narrative and quantitative goals that are definite and measurable. These specific goals relate to the enterprises as a whole and to the major responsibility centers.

Executive management as the second component of the substantive plan for the upcoming budget year should develop these goals. Executive management should exercise leadership in this planning phase so that there will be a realistic and clearly articulated framework within which operations will be conducted toward common goals (Welsch, et al; 2004: 77).

### **2.5.1.4 Development and Evaluation of Company Strategy:**

Company strategies are the basic thrusts, ways and tactics that will be used to attain planned objectives and goals. A particular strategy may be short-term or long-term. Here are some actual examples of basic strategies:

- Increase long-term market penetration by using technology to develop new products and innovation the product.
- Emphasize product quality and price for the top market.
- Expand market the company will not enter foreign markets in the near future.
- Market with low price to expand value.
- Use both institutional and local advertisement program to build market share.
- Improve employee morale and productivity by initiating behavior management program.

Among probable alternatives, the best should be chosen which would tackle to the objectives and goals of the organization. Strategies focus on 'how' so that they outline a plan of action for the enterprises (Welsch, et al; 2004: 78).

### **2.5.1.5 Executive Management Planning Instruction**

This phase involves communication of the substantive, plan to middle and lower management levels. It explains the broad objective, enterprise goals enterprise strategies, and any other executive management instruction, needed to develop the strategic and tactical profit plans. It also is called the statement of planning premises or the statement planning guidelines. Executive management explicitly establishes a planning foundation that is a condition precedent to the movement in the planning process. On the basis of this planning foundation the statement of planning guidelines is set as executive management instructions and is disseminated in order to initiate a sophisticated and potent move from broad corporate planning to the development of profit plans by each major responsibility center in the enterprises. It is simply a communication steps from executive management to the lower levels of management and it should adopt the fundamentals of full communication (Welsch, et al; 2004: 79).

### **2.5.1.6 Preparation and Evaluation of Project Plans:**

Project plans encompass variable time horizons because each project has a unique tie dimension. Project plan encompass such items as plans for improvement of present products, new and expanded physical facilities, entrance into new industries, exit from products and industries, new technology, and other major activities that can be separately identified for planning purpose. The nature of projects is such that they must be planned as separate units.

Consistent with this approach during the formal planning cycle, Management must evaluated decide up on the plan status of each project in process and select any new projects to be initiated during time dimension covered by the up coming strategies and tactical profit plans (Welsch, et al; 2004: 79).

### **2.5.1.7 Development of strategies and tactical profit plan:**

When the managers of the various responsibility centers in the enterprises receive the executive management planning instruction and the projects plans, they can begin intensive activities to develop their respective strategic or tactical profit plans. The strategic and tactical profit plans are usually developed concurrently. Certain format and

procedural instructions should be provided by a centralized source, normally the financial functions, to establish the general format, amount of detail and other relevant procedural and format requirements essential for aggregation of the plans of the responsibility centers, into the overall profit plans. All of this activity must be coordinated among the centers in conformity with the organization structure.

When the two plans for the overall enterprises are completed, executive management should subject the entire planning package to a careful analysis and evaluation to determine whether overall plans are the most realistic set that can be developed under the circumstances. When this point reaches the two profit plans should be formally approved by the top executive and distributed to the appropriate managers (Welsch, et al; 2004: 80).

#### **2.5.1.8 Implementation of profit plan:**

Implementation of management plans that have been developed and approved in the planning process involves the management function of leading subordinates in attaining enterprises objectives and goals. Thus effective management at all levels requires that enterprises objectives, goals, strategies, and policy to be communicated and understood by subordinates. “There are many facets involved in management leadership. However, the comprehensive PPC program may aid substantially in performing this function, plan, strategies and policies foundation for effective communication. The plan should have been developed with the managerial conviction that they are going to be met or exceeded in all major respects. If these principles are effective in the development process, the various executives and supervisor will have a clearer understanding of their responsibilities and the expected level of performance (Welsch, et al; 2004: 80).

#### **2.5.1.9 Use of periodical Performance reports:**

The accounting department on a monthly basis prepares performance reports. In addition, some special performance reports are prepared more often on an “as needed” basis. The performance reports a) compare actual performance with planned performance and b) show each difference as a favorable or unfavorable performance variation (Welsch, et al; 2004: 85).

### **2.5.1.1. Follow up:**

Follow up is an important part of effective control because performance reports are based on assigned responsibilities; they are the basis for effective follow up actions. It is important to distinguish between cause and effect. The performance variations are effects, the management must determine the underlying causes. The identification of causes is primarily as responsibility of line management (Welsch, et al; 2004: 88).

Finally, there should be a special follow up of the prior follow up actions. This step should be designed to

- Determine the effectiveness of prior corrective actions and
- Provide a basis for improving future planning and control procedures.

## **2.6 Advantages and disadvantages of PPC:**

The usefulness of comprehensive PPC may offer more benefits, which may be summarized as below.

1. It forces early consideration of basic policies.
2. It requires adequate and sound organization structure; that is there must be a definite assignment of responsibility for each function of the enterprise.
3. It compels all members of management, from the top down, to participate in the establishment of goals and plans.
4. It compels departmental managers to make plans in harmony with the plan of other departments and of the entire enterprise.
5. It requires that management put down in figures what is necessary for satisfactory performance.
6. It requires adequate and appropriate historical accounting data.
7. It compels management to plan for the most economical use of labor material and capital.



8. It instills at all levels of management the habit of timely, careful and adequate consideration of the relevant factors before reaching important decision.
9. It reduces cost by increasing the span of control because fewer supervisors are needed.
10. It frees executives from many day-to-day internal problems through predetermined policies and clear-cut authority relationships. It thereby provides more executive time for planning and creative thinking.
11. It tends to remove the cloud of uncertainty that exists in many organizations, especially among, lower levels of management, relative to basic policies and enterprise objectives.
12. It pinpoints efficiency and inefficiency.
13. It promotes understanding among members of management of their co-workers problems.
14. It forces management to give adequate attention to the effect of general business condition.
15. It forces a periodic self-analysis of a company.
16. It checks progress or lack of progress towards the objectives of enterprises.
17. It forces reorganization and corrective action (including rewards)

PPC model should not be assumed that the concept is full proof or that it is free of problem. The following main arguments are usually given against PPC

1. It is difficult, if not impossible, to estimate revenues and expenses on our company realistically.
2. Our management has no interest in all the estimates and schedules. Our strictly informal system is better and works well.
3. It is not realistic to outline and distribute our goals, policies and guidelines to all the supervisors
4. Budgeting places too great a demand
5. It takes away management flexibility.
6. It creates all kinds of behavioral problems.
7. It places the management in a straitjacket.

8. It adds a level of complexity that is not needed.
9. It is too costly asides from management time.
10. The managers, supervisors and other employees hate budgets.
11. What ever exists in the world has both advantages and disadvantages; and it is clear that we use or apply it only in that case if it has many advantages. A PPC model also has more advantages than disadvantages. Thus, now a days PPC system (model) is especially familiar to organizations and widely used in this world of management.

## 2.7 **Basic Assumption and Limitations Profit Plan:**

Profit planning system is more common in large companies, to serve the management. Still, the usefulness of budgeting to very small business could have been circumvented by an early attempt to qualify the dreams of headstrong. However, there are so many assumptions of using profit-planning program.

The basic assumptions prior to the start of the profit planning system are:

- Profit plans are based on estimates and reality hardly coincides to the estimate. Therefore, a profit planning and control program must be continually adapted to fit changing circumstances.
- Profit plans are just plans and the execution of a profit plan will not occur automatically. It requires smart and sincere human effort.
- Profit planning should not limit the manager's thinking
- However, each tool suffers some limitation and its use is fruitful within these limits. Profit planning and control is also not a limitless tool; so it is essential that the user of profit planning and control must be having a full knowledge of its limitations. The limitations of profit planning are as under:
- Based on estimates: profit planning is not an exact science. Its sources depend upon precision of estimates.
- Danger of Rigidity: profit planning is not an estimation and quantitative expression of all relevant data. So, there can be the tendency to attach some sort of rigidity or finality to them:
- Application for long period

- Execution is not automatic
- Not a substitute for management
- Costly affairs
- Proper evaluation
- Lower morale and productivity

The profit plan should be regarded not as a master but as a servant. It is one of the best tools yet devised for advancing the affairs of a company and the individuals in their various spheres of managerial activity. It is not assumed that any profit plan is perfect. The most important consideration is to make sure, by intelligent use of profit plans that all possible attainable benefits are derived from the plans as rendered and to re-plan when there are compelling business reasons (Goet, et al; 2062: 1.6).

## **2.8. Implementation of the profit plan**

### **2.8.1 Completion of the Annual Profit Plan:**

The development of an annual profit plan ends with the planned income statement, the planned balance sheet, and the planned statement of cash flows. These three statements summarize and integrate the detailed plans developed by management for the planning period. They also report the primary impact of detailed plans on the financial characteristics of the firm. In profit planning, the budget director has an important responsibility for designing and improving the overall system. "Other essential sub budgets are the following.

- Planned statement of cost of goods manufactured.
- Planned statement of cost of goods sold.
- Planned income statement.
- Planned statement of cash flows.
- Planned balance sheet.

The profit plan completion date is important. Issuances of a profit plan after the beginning of the budget period are one sure way of destroying much of the budget potential (Welsch, et al; 2004: 466).

### **2.8.2 Implementing the profit plan:**

Profit plan should represent potentially attainable goals, yet the goals should present a challenge to the enterprise. The plan should be developed with the conviction that the enterprise is going to meet or exceed all major objectives. Participation enhances communication (both down ward and upward). If this principle is to be effective, the various executives should have a clear understanding of their implementation responsibilities.

The final test of whether the efforts and cost in developing a profit plan are worthwhile is its usefulness to management. The plan should be developed with the conviction that the enterprises are going to meet or exceed al major objectives; participation enhances communication. If this principle is to be effective, the various executives and supervisors should have a clear understanding of their responsibilities. The copies of the complete profit plan be prepared and distributed to the member of executive management. The guiding principle in establishing the distributed policy might be to provide one copy to each member of the management team according to his/her overall responsibilities, while taking in to account the problem of security. After distribution of the profit plan, a series of profit plan conferences should be held. The top executives discuss comprehensively the plans expectations and steps in implementation. At this top level, meeting the importance of action, flexibility and continuous control may well be emphasized. In essence, each manager has to realize that the budget is a tool for his or her use. Conferences should be held to convey the profit plan to each level of management.

The manager of each responsibility center obtains an approved profit plan for his center and it becomes the basis for current operations and excerpts considerable coordinating and controlling effects.

Performance must be measured and reported to management. Execution of the plan is assured through control procedure must be established so that accomplishment, or failure is immediately known. On this basis action can be taken to correct or minimize and undesirable effects. Short term performance reporting is essential.

A budget programs viewed and administrated in a sophisticated way does hamper or restrict management, instead, it provide definite goals around which day today and mouth

to mouth decisions are made. Flexibility in the use and application of both the profit plan and variable budgets also should be considered in detail. Flexibility in budget application is essential and it increases the probabilities of achieving or bettering the objectives (Welsch, et al; 2004: 472).

### **2.8.3 Performance Reports:**

Performance reporting is an important part of a comprehensive PPC system. Its phase of a comprehensive PPC program significantly influences the extent to which the organization has planned goals and objectives are attained. Performance reports deal with control aspect of PPC. The control function of management defined as the action necessary to assure the objectives, plans, policies and standards are being attended. Performance reports are one of the vital tools of management to exercise its controls function effectively.

Special external reports, reports to owner & internal reports are specially presented in the organization. Performance reports include in internal reports groups. It is usually prepared on a monthly basis and follows a standardized format. Such reports are designed to facilitate internal control by management. Fundamentally, actual result of reports is compared with goals & budget plans. Frequently they identify problems that require special attention since these reports are prepared to pinpoint both efficient & inefficient performance.

- **Features of performance reports**

In comprehensive PPC, performance report is very important. The main objective of performance reports is the communication of performance measurement, actual results and the related variances. Performance reports offer management essential insights in to all the facts of operational efficiencies. Performance reports should be:

1. Tailored to the organizational structure and focus of controllability (that is by responsibility centers).
2. Designed to implement the management by exception principle.
3. Repetitive to implement the management by exception principle.
4. Adapted to the requirement of the primary users.

5. Simple understandable & reports only essential information.
6. Accurate and designed to pinpoint significant distinctions.
7. Prepared and presented promptly.
8. Constructive in tone.

- **Aspects of Performance Reports**

To the extent to which the various managers use their performance reports depends on many factors, some behavioral and some technical. One important factor is the extent to which the performance reports serve the management and decision-making needs of the users. Top management needs reports that give a complete and readily comprehensible summary of the overall aspects of operations and identification of major events. Middle management needs summary data as well as detailed data on day-to-day operation. Similarly, lower level management needs reports that must be detailed, simple, understandable & limited to items having a direct bearing on the supervisor's operational responsibilities.

In the design and preparation of performance reports, careful attention must be given that titles and headings should be descriptive; column heading & side caption should clearly identify the data, & the technical jargon should be avoided. Reports should not be too long & complex; tabulations should be avoided. Performance reports should be standardized to a reasonable degree and if they should be relevant.

Performance reports should be available on a timely basis. To attain a realistic balance between immediate reporting & the costs of detailed reporting, monthly performance reports are widely used in the organization.

#### **2.8.4 Review of Previous Research Work:**

Review of literature is essential to explore what other research in the area has uncovered. A literature review is the process of reading, locating and obtaining the relevant subject matters in the area of students' interest. The purpose is to develop some expertise in the area, to see what new contributions can be made, and to review some idea for developing a research design.

A critical review of the literature helps the researcher to develop a thorough understanding and insight into previous research work that relates to the present study. It is also a way to avoid investigating problems that have already been definitely answered (Woolf , et al; 2004:39).

There are some research works conducted by the students of T U in the field of profit planning practices as well as in the field of revenue planning in the service sector enterprises. Most of them have focused on the budgeting aspect. Budgeting is only one aspect of comprehensive profit planning; therefore, some research work could not incorporate overall aspects of Revenue Planning

**Sitaula;** (2006) submitted the Theses on the topic “*Sales plan and Its impact on Profitability*” (A case study of Unilever Limited.)

**His main objective:** The fundamental objectives of present study is to analyze the current practices of sales budgeting and its effectiveness in manufacturing enterprises established under foreign investment .

- To analyze the sales budget prepared by Unilever Nepal Limited.
- To evaluate the deviations between budgeted and actual sales.
- To make comparison of sales budget with profit of the Unilever Nepal limited.
- To provide the appropriate suggestions and recommendation for improvement of planning system of Unilever Nepal Limited.

**His major Finding:**

- The company does not have practice of preparing sales budget although there is tentative sales budget.
- Actual sales are below than the budgeted sales.
- The correlation between budgeted and actual sales shows a positive correlation. It means that the company can meet its sales goals as specified in annual program.
- There is no cost classification system in the company. The costs are not segregated into fixed and variable in systematic manner.

- The company has no practice of systematic sales forecasting. Sales forecasting is not based on realistic ground. It has no practice of using statistical techniques in sales forecasting.
- Sales territories of UNL can be divided as domestic and export sales. In the FY 2061/062 the domestic is 100% of total sales and export sales is nil.
- Mainly 8 different types of consumer product lines are produced by UNL.

**His major recommendation:**

- The company should practice of preparing detail sales budget.
- The cost segregated in systematic manner.
- The company should try to increase the actual sales than the budgeted sales.

**MR. Paudel:** (2006); Has made a study entitled, “*Role of sales budgeting in the Profitability of Public Enterprises in Nepal: A case study of Dairy Development Corporation (DDC)*”.

The fundamental objectives of the study are to highlight and appraise the current practice of the sales planning and its effectiveness in manufacturing concern particularly in Dairy development.

**His major objectives :**

- To analyze the sales budget prepared by DDC'
- To Evaluate the variance between budgeted and actual achievement of DDC
- To compare the sales with profit of DDC
- To provide the suitable suggestion and recommendations for the improvements of the planning system of DDC.

**His major Finding:**

- DDC does not have comprehensive profit plan based on the realistic expectation.
- DDC does not have long term strategic sales plan.
- Lack of coordination between performance department and measurement department.
- Participation of only top levels in planning and decision-making.
- Lack of communication between high level and low-level staffs.



- Sales forecasting based on the personal judgments of top-level staffs.
- Actual sales are lower than budgeted sales.
- Lack of adequate supply of milk and collection centers for the milk from farmers.
- Rate of increases in cost is higher than the rate of change in sales.
- Non-evaluation of internal and external variables.

**His major recommendation:**

- DDC should make the long term sales plan
- There should be coordination between performance department and measurement department.
- There should be participation top level and lower level in decision making process.

**Shrestha:** (2006) Has made a "*study on role of sales plan in profit planning in Nepalese public enterprises*", ( A case study of NEA)

The general objectives of this study is to examine and evaluate the practice of profit planning and control with special reference of sales planning and its impact on profit of Nepal Electricity Authority.

**His main objectives :-**

- To analyze the variance of annual budgeted sales and actual sales.
- To analyze the relationship between sales and profit
- To analyze the interrelationship between sales and profit.
- To study the trend of sales and problems of NEA.
- To interpreter the sales related ratio.

**His Major Finding:-**

The major findings because of various analysis, observation and discussion wit authentic and published documents are enumerated below:

- With special reference to sales planning, it can be said that NEA has practice of preparing various functional budgets in the process of preparing comprehensive profit plan.

- The budgeted and actual sale has CV 94.5% and 116.1% respectively. Therefore, actual sales are more variable than budgeted sales.
- The trend value of sales is in increasing trend. The time series analysis indicates that it will go on increasing in the following years too.
- There is positive and a perfect correlation between budgeted sales & actual achievement of sales. The value of correlation between budgeted and actual sales is 0.9915.
- An actual sale is less than actual production. It indicates remarkable loss of power in NEA

**His major recommendation:-**

- NEA should practice of preparing various functional budget in the process of preparing comprehensive profit plan.
- There should actual sales which are more variable than budgeted sales.
- There should be positive and perfect correlation between budgeted sales and actual achievement sales.

**MR. Karki:** (2007) has made a study entitled, “*Revenue Planning in Service oriented Company*” A case study of Nepal Nepal Telecom limited.

His main objectives of the study are to search and highlight the role of revenue planning in the performance of N.T.C.

**His major objectives:-**

- To sketch out the use of revenue planning tools and techniques.
- To examine the use of planning in managerial short run and long run decision making.
- To point out short Cumming in sales budgeting and planning.

**His major Finding:-**

- No plans and programmed has been made about possible consumption of telephone industries.
- NTC has not adopted of practice of preparing monthly revenue earning reports

- The revenue plan prepared by the branches and sub branches were not taken as reference for preparing of central revenue plan.
- There are consistency between planned sales and actual sales, their correlation was high.
- Planned sales revenue was highly and positively correlated. The correlation of actual sales revenue is also positive and high.
- The analysis of category wise revenue plan shows that achievement in domestic, noncommercial and industrial categories are highly consistent. But the achievements in remaining categories are fluctuating.
- NTC has been making efforts to bring operating loss down to 10% since 1990/00 but actual loss crossed about 2% in the analysis period.

**His major recommendation:**

- Plans and programs should be made about possible consumption of telephone industry.
- Consistency should be between planned sales and actual sales.
- Actual sales should be high and positively correlated with planned sales.

**MR Niraula** (2008) has made a study entitled, *“Impact of budgeting in profitability of Nepalese Public Enterprises”* A case study of Nepal Electricity Authorities.

**His main objectives :**

- To analyze the various functional budget of NEA.
- To analyze the true picture of managerial budgeting adopted by NEA.
- To analyze the variance between budgeted and actual achievement of the authority.
- To point out the major short Cumming and recommendation for improvement.

**Major Finding:-**

The major points that I found by the detailed study as well as analysis of the entire budgeting practice of NEA in relation to its profitability are presented below:

- Actual and budgeted sales are found to be significant but the difference between budgeted and actual production is found to be vague. In spite of the fact, there is

perfect correlation between budgeted and actual sales and production respectably.

- NEA has adopted the practice of preparing strategic as well as managerial budgeting, but even the strategic plan can not play a vital role for its development.
- It is bearing a high fixed cost due to the technology that it is using till now, overstaffing and many more.
- Actual sales are always less than actual production due to power loss which is a main problem of NEA, which effects its profit directly.
- It has not classified its overhead systematically, which creates difficulties in analyzing the expenses properly.
- The information system of NEA was not effective. The lower level staffs normally do not get information properly and clearly. In stead of the fact, there is no any plan to develop an effective information system till now.
- EA has no sufficient cash surplus to pay for expenditure; it was to borrow loan to meet minimum cash balance and we can say that it is the result of poor cash plan. And for that it is paying huge amount of interest in every year and the trend is of adding on it rather than of paying back.
- Account receivable and average collection period are found to be increasing within the study period. It is also upgrading the condition of cash shortage.

**His major recommendation:-**

- NEA should adopt the practice of preparing strategic plan as well as managerial budgeting
- NEA should control the power loss.
- The information system of NEA should be effective.

**MR. Karn:** (2008) Has made a study entitled, “*Profit Planning Mechanism of Nepal Nepal Telecome limited*”

The major points that I found by the detailed study as well as analysis of the entire budgeting practice of NTC in relation to its profitability are presented below:

**His major objectives:**

- To analyze the Financial position of Nepal Telecom
- To analyze the target and actual budget of Nepal Telecom
- To assess the strength and weakness of Nepal Telecom.

**His major Finding:-**

The study showed that the actual sales achievement of NTC is highly consistent with budgeted sales in the fiscal year 2002/03 to FY 2007/08. The actual sales achievement is below than target sales. Target are sets high expectations, but actual sales achievement are on average 92.57 percentage of budgeted sales. It can be said that the targets were not sets on a realistic basis. The analysis of above table also shown that there is no systematic sales plan, it clear that the performance of planning section of NTC is not satisfactory and its prepare the sales plan on adhoc basis. Budgets are set only the assumption of management.

Budget is prepared because of historical data. Nevertheless, NTC actual achievement of sales or revenue is less than budgeted sales or revenue during the study period. It shows that the efficiency of the management for prepared the planning. Besides this due to the unavoidable situation or external environmental condition, NTC cannot meet the targeted sales. Mobile phones are distributed due to the political situation of the country in the FY 2004.

Average inventory turnover ratio of NTC for the past five years is 20.3618 times. It ranged between a highest of 32.565 times in FY 2004/05 AD and a lowest of 10.812 times in the FY 2003/04 A.D. The overall Ratio Trends shows an upward direction particularly in the most recent years. Average age of inventory of NTC for the study period is 21 Days.

Average Debtors Turnover Ratio of NTC for the past five years is 2.8282 times. It ranged between a highest of 3.119 times in the FY 2003/04 AD and a lowest of 2.3796 times in the FY 2003/04 AD. Average Collection Period of NTC over the five years of the study period is 128 days. Average of the total Assets Turnover Ratio of NTC for past five years is 0.26404 times. The ratio seems to be a little volatile as it ranged from 0.2580 in the FY 2003/04 to 0.2747 in the FY 2003/04 AD. Fixes Assets Turnover of NTC is in increasing

trend. It ranges from a minimum of 0.823 Times in the FY 2003/04 AD to a maximum of 1.026 times in the FY 2004/05 AD.

**His major recommendation:-**

- NTC should make realistic forecast
- NTC should start to practice of preparing monthly budget
- In the case of preparing the central budget NTC should take suggestion by branches and sub branches.

## **2.9 Research Gap:**

A brief review of above-mentioned dissertations, it is seen that most of the enterprise are not operating effectively. The previous researches have also not applied the full concept of Budgeting and Revenue also but the previous studies can't be ignored because they provide the foundation to present study. In other words, there has to be continuity in research. This continuity in research is ensured by linking the present study with the past research studies. Here, it is clear that the new research cannot be found on the exact topic.

The purpose of this research is to develop some expertise in one's area, to see what new contribution can be made and to receive some ideas, knowledge and suggestions in relation to "Revenue planning and its impact on Profitability of Nepal Telecom Limited". Therefore, to fulfill this gap, this research is selected. To complete this research work: many books, journals, articles and various published and unpublished dissertations are followed as guideline to make the research easier and smooth.

Previous researchers could not cover all the aspects of Revenue planning in Nepalese public enterprises. Therefore, this study is useful to the Public enterprises as well as different persons: such as shareholders, investors, policy makers, state of government and other researchers etc. Thus, present study may be valuable piece of research work.

## **CHAPTER THREE**

### **RESEARCH METHODOLOGY**

#### **3.1 Introduction:**

The term 'research' is believed to be derived from the French word 'Researcher' meaning to search again. The research work is undertaken following a systematic way, which is called Research Methodology. As per Kother, it is the way to solve systematically about the research problem.

This chapter refers to the overall research method comprising the theoretical aspect to the collection and analysis of data. This study covers quantitative methodology in a greater extent and cases the descriptive part based on both technical aspect and logical aspect. The major objective of this research are to analyze the revenue planning practice in Nepal Telecom Limited, its effectiveness, use of short term and long term revenue planning tools, to evaluate the variance in budgeted and actual result and find out financial strength and weakness. The Research Methodology includes research design, data collection procedures and research variable and tools used.

#### **3.2 Research design:**

A research design is purely and simple the framework or plan for a study that guides the collection and analysis of data, as per Kerlinger. Research design is the plan, structure and strategy of investigation conceived to obtain answers to research questions and control variance. This study is an examination and evaluation of process in Revenue planning and its impact on profitability of NTC. Various functional budgets and other related accounting information's and statement of the enterprises are the materials to analyze and evaluate the revenue planning system of the Enterprises. Descriptive as well as analytical research designs have been adopted in this research.

### **Data Collection Procedures and Sources of Data:**

This study is mostly based on secondary data. However, primary data and information have been obtained through informal discussions with the executives and other staff of the company. Secondary data have been collected from the annual published accounting and financial statement of NTC. Similarly, other necessary data have collected from publication of the Nepal Telecom Authority (NTA), Central Bureau of statistic and related publications.

As per effective Research work, data play very important role to the last extent all the research data for this research work as taken from its origin. For this research work all, the quantitative data are collected directly from NTC. For the data regarding functional budget, data are collected from secondary source only.

Some qualitative data are collected from the persons directly or indirectly related with NTC. Some descriptive data are collected from office staff of the NTC and some data are collected from previous researcher.

### **3.4 Population and Sample:**

As this research aims at studying the revenue planning aspect of the NTA, taking the reference of NTC and data have been analyze for several years of its operation. Here, all the NTA are population of the study and NTC has been selected as sample for the present study.

### **3.5 Tools and Technique Employed:**

This study is confined to examine the Revenue planning of NTC. Therefore, the data have been collected accordingly and managed, analyzed and presented in suitable tables, formats, diagrams, graphs and charts. Such presentation have been interpreted and explained wherever necessary. Financial, Accounting, Mathematical and Statistical tools



are used to analyze. The presented data, which includes Ratio analysis, Percentage, Regression analysis Correlation coefficient, Mean, Standard deviation, Coefficient of Variance, and time series etc.

### **Financial and Accounting Tools**

Following financial tools have been used to analyze the data in this study.

1. Ratio analysis: By ratio analysis, we study the arithmetical relationship of two data.
2. CVP analysis.

### **Statistical and Mathematical Tools**

We have analyzed the data presented in this study by applying following statistical and mathematical tools.

1. Percentage increment
2. Mean.
3. Standard deviation
4. Coefficient of variance.
5. Regression analysis.
6. Correlation of coefficient.
7. Probable error.
8. Time series.

The research methodology adopted for this study is shown above. The following chapter includes the data presentation and analysis

## **CHAPTER - IV**

### **Data Presentation and Analysis**

#### **4.1 Introduction:**

In Nepalese context, public enterprise is playing important role in economic development and social development because its main objective is social service than the profit from operation. Nepal is developing country, so public enterprises are strong means of development in order to prepare infrastructure, production of services and goods for controlling the price situation, to increase the government revenue and to contribute significantly in the national development as well as to assist in the country's economic development.

In Nepal only public enterprises have higher access to the national resources and it is important to survive public enterprise for utilization of all the national resource at maximum. But at present context the country is facing a big problem with the performance of public enterprise. They are suffering from heavy and continuous losses due to poor managerial efficiency and competitiveness. It has become a financial and administrative burden to Nepalese government for this Nepalese government has started to phase out poor performing public enterprise either by privatizing or liquidating them.

#### **4.2 Sales Revenue Budget or Plan:**

The sales Plan is the foundation for periodic planning in the firms because practically all other enterprises planning is built on it. All the other plans and budget are depending upon the sales budget. The budget is usually presented in both units and dollar of the sales revenue or sales volume. The preparation of sales plan is based upon the sales forecasts. It is also known as corner stone for all the other budgets. That is because the production level and the inventory level and hence manufacturing costs as well as non-manufacturing costs generally depend on the forecasted level of unit's sales or revenue.

The sales planning process is a necessary part of PPC because

- a) It provides further basic management decisions about marketing.
- b) Based on those decisions, it is an organized approach for developing a comprehensive sales plan. If the plan is not realistic, most if not all the other parts of the overall profit plan also are not realistic. Therefore, if management believes that, a realistic sales plan cannot be developed; there is little justification of PPC.

**Primary objective of sales budgets are as follows:**

- a) To reduce uncertainty on future revenue.
- b) To incorporate management judgment and decision into the planning process.
- c) To provide necessary information for developing other elements of a comprehensive profit plan.
- d) To facilitate management in controlling sales activities.

### **4.3 Sales budget:**

N.T.C. has a long experience of preparing sales budget, which is known as long term load forecast. Sales budget is prepared by N.T.C. according to the nature of consumers. Consumer are categorized into domestic, commercial non-commercial, communication center like local, STD, ISD telephone user and mobile users.

The previous sales performance and their respective budget are presented to know about sales trend of past and to forecast the future sales trend of N.T.C.

The table 4.1 present the sales budget and actual sales achievement in unit ion Rs from the fiscal year 2002/03 to 2007/08.

**Table 4.1**  
**Budgeted and actual sales**

Rs. in Million

FY	Budget	Actual	Achievement %
2002/03	5821.21	5487.79	94.2
2003/04	6558.50	6159.20	93.9
2002/03	7032.23	7208.87	102.5
2003/04	8221.50	6070.42	73.8
2004/05	8122.25	10725.96	132.0
2007/08	9532.24	10413.36	109.2

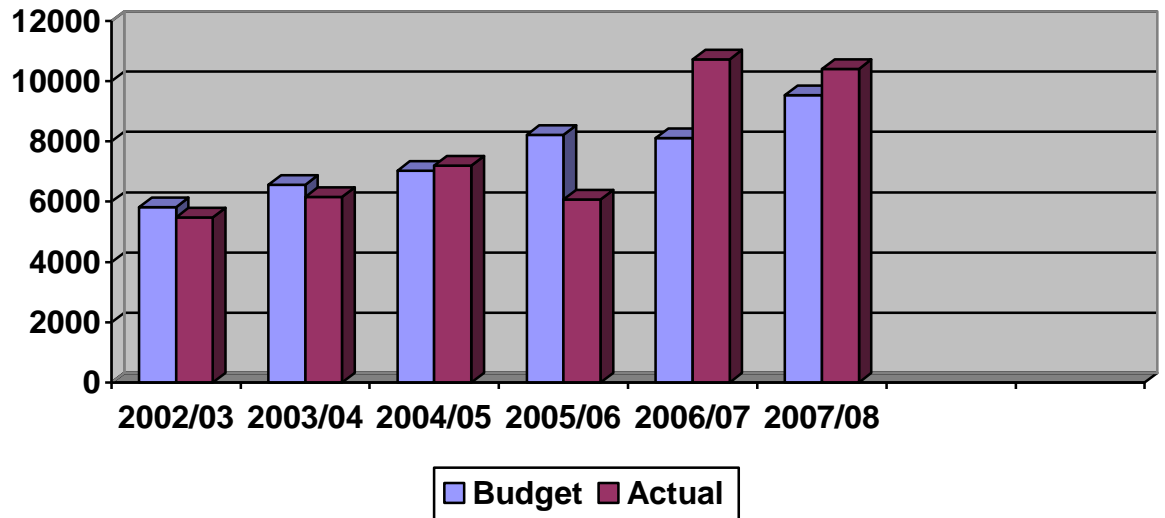
Source : Annual report of N.T.C.

From the above table of budgeted sales and achievement of NTC, it is clear that budget achievement rate is satisfactory where it achieved more than 100% and there is a minimum achievement of 93.9% in fiscal year 2003/04. Since the fiscal year 2007/08 the latest year of research data, it seems that NTC is achieving 109.2% of its budgeted sales. In financial year 2002/03 actual sales figure of NTC was Rs 5487.79 millions and slightly increased to Rs 6159.20 millions in financial year 2003/04. Similarly actual sales figure of NTC was Rs 7208.87 millions in 2002/03 and slightly decreased and reached to Rs 6070.42 millions in financial year 2003/04. But in remaining period and as a whole actual sales of NTC is in increasing trend besides actual sales figure in financial year 2003/04.

- **Sales Trend of N.T.C**

The graphical trend line shows the movement of value of a variable from one period to another for clear pasteurization. Sales budget and gross achievement from the fiscal years 2002/03 to 2007/08 have been presented below in a graphical trend line

**Figure 4.1**  
**Budgeted and actual sales revenue**



The graphical presentation shows the fluctuating trend between the budgeted and actual sales during the study period. The gap is remarkable in 2004/05.

**Table 4.2**  
**Presentation of mean and SD**

Description	Budget 'X' in '000	Actual 'Y' in '000
Mean (x)	75.524	76.776
S.D.	11.865	21.087
C.V.	0.1571	0.2746

From the above statistical analysis, the budgeted mean Rs. 75524 and its actual mean is Rs. 76474. The budgeted standard deviation is Rs. 11865 but actual standard deviation is 21087. And budgeted C.V. is 0.1571 and actual C.V. is 0.2746.

## Time series analysis:

Time element is also an important factor for the study of trend of actual sales least square method and time series study can also be used to analyze the trend of actual sales and to estimate possible future sales for the given period of time. A straight-line trend shows the relationship between actual sales year. To fit the straight line trend, the time factor are consider as independent variables and actual sales is considered as dependent variables.

Here, the straight line trend by the least square trend methods for actual sales up on time is expressed by

$$y = a + b x$$

where,

y = actual sales

x = Time (years)

**Table 4.3**  
**Fitting straight line trend by least square**

<b>FY</b>	<b>Actual sales (y)</b>	<b>x year</b>	<b>x<sup>2</sup></b>	<b>xy</b>
2002/03	5487.79	-2	4	10975.58
2003/04	6159.20	-1	1	-6159.20
2004/05	7208.87	0	0	0
2005/06	6070.42	1	1	6070.42
2006/07	10725.96	2	4	21451.92
2007/08	10413.36	3	9	31240.08
Total	460656	3	19	41627.64

Source : Annual report of N.T.C.

FY 2002/03 is assumed as base years therefore the value of x or mid time is zero, Negative before the base year and positive after the base year.

Substituting the value of in straight line equation

$$y = a + bx$$

$$\begin{aligned}\text{Where } a &= \frac{\sum y}{n} = \frac{46065.6}{6} \\ &= 7677.6\end{aligned}$$

$$\begin{aligned}b &= \frac{\sum xy}{n} \\ &= \frac{419627.64}{6} \\ &= 6937.94\end{aligned}$$

$$y = 7677.6 + 6937.94x$$

The trend line indicators the positive sales figure for future if the sales trend of previous year continue in the future. The sales will be increased by 6937.94 in every year.

#### **4.3.1 Sales budget and Profitability:**

From the above different analysis, it is clear that there is no consistency in sales achievement of N.T.C. Although, there is comparative in sales budget. Although past sales has high achievement, enterprise has not carried out any corrective actions like modification in sales budget or revision in sales budget based on past year actual result. So it seems that N.T.C unable to plan its sales in realistic basis.

Since sales budget are unrealistic, it creates negative impact on whole operation of the business as well as profitability. Based on sales all the other functional budget are prepared because sales budget is overestimated, other functional budget are also over budget and it tends to increase the functional expenses which makes low morale of the employees because that is unable to meet the target. These factors ultimately affect the profitability of the N.T.C. generally fixed expenses facilities are not optimally utilized due to not meeting the target.

Calculation of mean, standard deviation coefficient of variation and probable error of actual revenue and profit of NTC.

**Table 4.4**

**Mean and Standard deviation of Actual sales and Actual Profit**

Description	Actual Sales	Actual Profit
Mean (x)	76.77	13.76
S.D	21.087	5.867
C.V.	0.275	0.426

From the above statistical analysis it is clear that actual sales has high degree of deviation compared to profit. There is actual mean sales of Rs 76770 million and profit has a mean of Rs 13760 million. Actual sales have a standard deviation of 21087 million where as profit has a deviation of Rs 5867 million we can use correlation of coefficient as a statistical tool to analyze the relationship between actual sales and profit. It should be positive coefficient of correlation between actual sales and profit i.e. actual sales should increase as profit also increase and vice versa. For this, we can take help of Karl Pearson's coefficient of correlation and is denoted by  $\gamma_{xy}$ . By calculating  $\gamma_{xy}$ . We can examine whether there is positive correlation between sales and profit or not.

For purpose of calculation  $\gamma_{xy}$  actual sales figure denoted by 'X' are assumed independent variable and profit figure denoted by 'Y' are assumed to be dependent variable. The profit will be large if actual sales are large and vice versa. After this, significant of  $\gamma_{xy}$  is tested with probable error of "r". The detailed calculation of  $\gamma_{xy}$  and probable error or 'r' is presented here.

$$\gamma_{xy} = -0.76$$

$$PE(r) = 0.116$$



Hence, there is fairly high degree of negative correlation between actual sales and profit. So, in general profits have increased with in increased in actual sales.

#### **4.4 Growth Analysis:**

Profit and loss account of any organization shows the operating result for any specific time period. This is the "Scoreboard" of the organizational performance. The main objectives of preparing profit and loss account are to see the operating position of an organization generally, in profit, making organization profit and loss account is prepared which shows profit or loss during any period. In non-profit making organization income and expenditure account is prepared which shows net surplus or deficit for any specific time period.

##### **4.4.1 Profit and Loss Analysis:**

Nepal Telecom Company limited is obtaining profit every year. Below is the table which shows the historical profit and loss situation of Nepal Telecom Company limited.

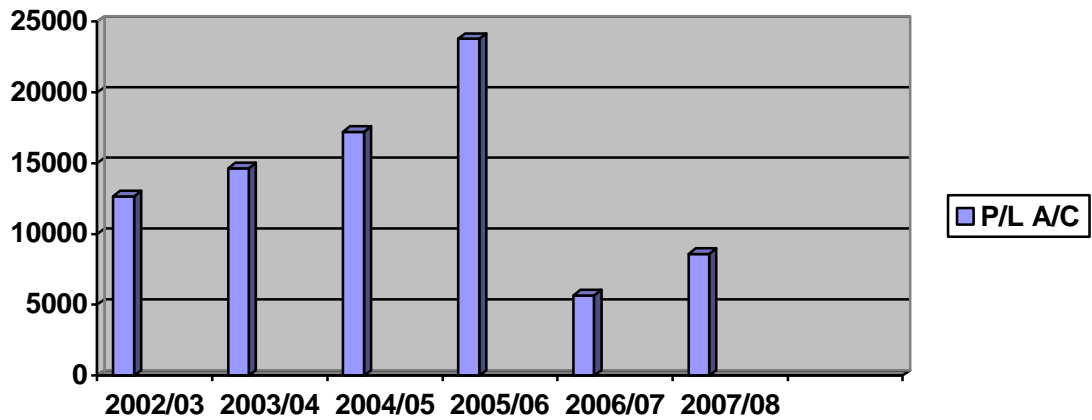
**Table 4.5**  
**Growth of Profit** **(Rs in million)**

Year	Profit	%Change
2002/03	12666.923	-
2003/04	14639.473	15.57
2004/05	17227.695	17.68
2005/06	23781.938	38.04
2006/07	5665.407	-76.17
2007/08	8602.369	51.84

Source: Annual report of N.T.C.

Above profit and loss trend can be presented as below in diagrammatic form for better pictures of the change.

**Figure 4.2**  
**profit and loss**



Source : Table 4.5

Above trend line shows that N.T.C. is in very good performing position because it has been obtaining heavy income from FY 2002/03 to 2007/08. In comparing among years, in fiscal year 2003/04 has heavy profit than other. But in FY 2005/06 to 2007/08 N.T.C. has made repayment of retained earning to Nepal Government so this period shows less profit than other.

**Actual Overhead budget :**

After analyzing the sales budget and production budget the service utility PES analyze the overhead budget, N.T.C. prepared the overhead budget in a combined way and which is named operating and maintenance expenditure budget. This budget includes (a) employment cost (b) bonus (c) incentive package (d) depreciation (e) administrative express (f) loss gain on foreign currency (g) Royalty (h) loss on sake of telephone and other goods etc.

N.T.C. does not prepare the separate budget like manufacturing overhead administrative overhead and selling distribution overhead budget. It reveals that N.T.C. does not have practice of preparing overhead budget in systematic way. N.T.C. aggregates all the expenditures and prepares the "Operation and maintenance expenditure budget" that is why there is difficulty to analyze its overhead budget separately.

The past trend of N.T.C. in operation and maintenance expenditure is presented in the following table

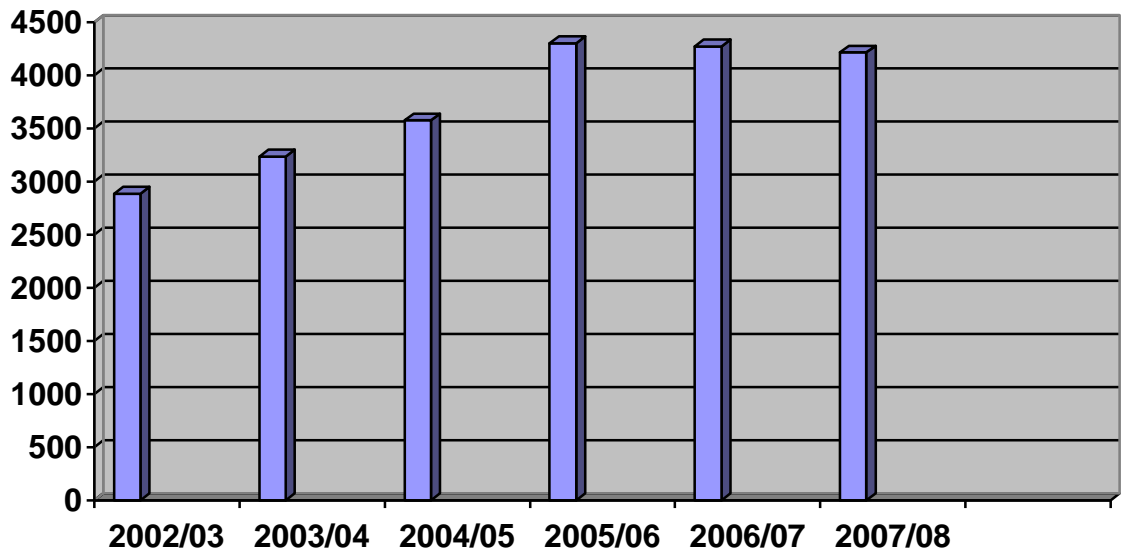
**Table: 4.6**  
**Actual overhead budget**

(Rs million)

Year	Op. expenses	Change %
2002/03	2885.633	-
2003/04	3235.929	12.1
2004/05	3576.165	10.5
2005/06	4304.367	20.4
2006/07	4272.768	0.7
2007/08	4215.188	1.3

Source: Annual report of N.T.C.

**Diagram: 4.3**  
**Actual Overhead**



Source : Table 4.6

Figure 4.3 reveals overhead expenditure trend from 2002/03 to 2007/08. As per figure, the aggregate overhead expenditure is increasing each and every year. The above table shows the actual overhead budget of Nepal Telecom Company. In FY 2002/03, the actual overhead was Rs 2885.633 millions and it slightly increased and reached to Rs 3235.929 million in FY 2003/04 and the percentage change over the fiscal year 2002/03 was 12.10%. It increased only 10.50% and reached to Rs 3576.165 millions in F/Y 2002/03. In 2003/04, it increased amazingly 20.40% and reached to Rs 4304.367 millions. Likewise, it slightly decreased and reached to Rs 4215.188 millions in F/Y 2007/08.

#### **4.5.1 Relationship between sales and overhead**

Overhead budget is the second step in process of revenue planning for the formation of revenue plan; the sales requirement is to be translated into overhead budget plan. In case of service concern, the sales plan is to be compulsorily translated in overhead plan.

N.T.C. is the utility concern. It prepares the value generate for increases sales revenue but similarly overhead is also fluctuated like. Revenue earned from telephone related service and bank deposits. Inter administration is accounted for as per statement/invoice period/received to from inter administration. These types of revenue are accounted for accrual basis.

**Table 4.7**  
**Relationship between Actual sales and Overhead**

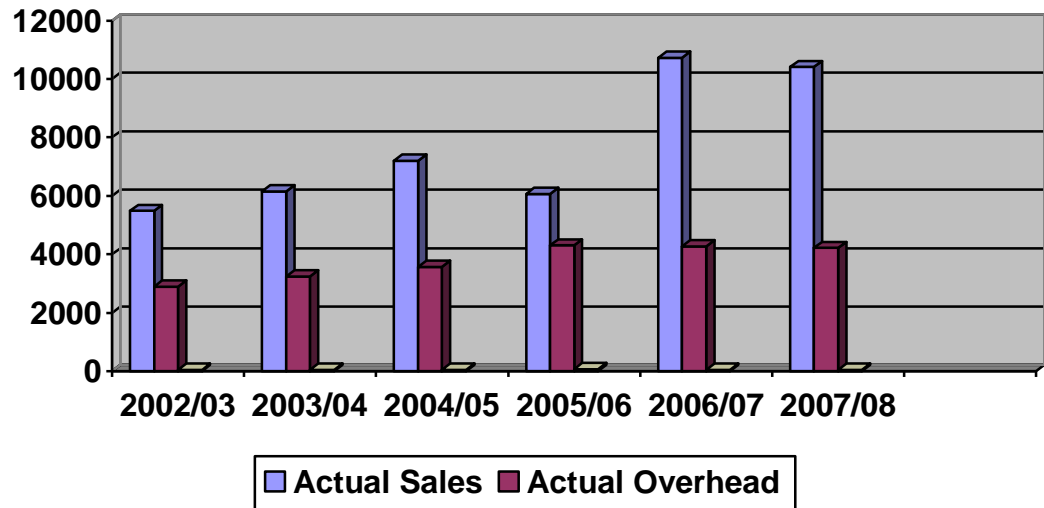
(Rs million)

Year	Actual Sales	Actual Overhead	% of Ov. in sales
2002/03	5487.79	2885.633	52.58
2003/04	6159.20	3235.929	52.53
2002/03	7208.87	3576.165	49.60
2003/04	6070.42	4304.367	70.91
2004/05	10725.96	4272.768	51.22
2007/08	10413.36	4215.188	49.10

Source: Annual report of N.T.C.

Table 4.10 shows percentage of overhead in sales revenue. According to above figure in period 2003/04 the overhead percentage in sales is very high in order to compare other years. In figure 4323.18 min year 2007/08 is very high where actual sales is also high in the same year. In year 2002/03 actual sales of NTC was Rs 5487.79 millions but actual overhead was quite low that was only Rs 2885.633 million which represents 52.28% of actual sales. Similarly, in fy 2003/04 actual sales was Rs 6159.20 million and the actual overhead was Rs 3235.929 million which represent 52.53% of actual sales. In fy 2002/03 actual sales increased slightly and reached to Rs 7208.87 million but actual overhead also increased and reached to Rs 3576.165 million which was 49.60% of actual sales. Likewise, in fy 2004/05 actual sales figure of NT increased amazing and reached to Rs 10,725.96 million whereas actual overhead slightly decreased and reached to Rs 4272.768 million in the same period which was 51.22% of actual sales.

**Figure 4.4**  
**Actual Sales and Overhead**



#### **4.6 Cost plan Analysis:**

The cost is the amount which is expenses for production of goods and services or used in operation. When we take any goods or services we have to pay some amount for that organization has to bear various type of cost like variable cost, fixed cost or semi variable cost. Variable cost can be controlled, so it also called controllable cost. But fixed cost can not be control and it is known as uncontrollable cost. For operation of business cost is required but it should control to earn profit. Different organization bears different type of cost. For the cost volume profit analysis production and operation cost should be segregate. Variable cost and fixed cost is very much necessary to find for C.V.P. analysis. Every organization must determine the level of BEP to save them from loss. Level of cost and sales revenue become equal at break even point so, the organization can segregate their various type of cost into fixed and variable. NTC has different types of cost or expenses. But the public enterprises in Nepal have not practice C.V.P analysis so they didn't have segregate the cost into fixed or variable.

**Different types of cost under different heading are shown below.**

**Expenditure of NTC**

1. Employee Cost :
  - Salaries and wages
  - PF contribution.
  - Earned leave salary
  - Clothing and Other allowance
  - Overtime allowance
  - Medical expenses
  - Pension and Gratuity
  
2. Operating and Maintenance cost
  - Maintenance office equipment
  - Maintenance Building
  - Maintenance plants Machinery.
  - Power heating and lighting
  - Fuel for vehicles.
  - Freight & carriages.
  - International channel rent.
  
3. Administrative expenses
  - Traveling express
  - Rent rates
  - Special charge
  - Bank charge
  - Entertainment
  - Office furnishing
  - Insurance
  - Statutory & fax audit fee
  - Bad debts

- Provision for doubtful debt
- Commission
- Meeting fees expenses
- Printing and stationery
- Advertisement
- Training expenses
- Postage
- Subscription and donation
- Legal and professional fees.
- Expenses on cost of goods.
- Royalty / Contribution on rural development fund.
- Miscellaneous expenses
- Obsolete and damaged fixed assets
- License fee
- Deterred Revenue expenditure
- Security expenses
- Membership fee.

#### **4.7 Variable cost:**

Variable cost varies in proportion to change in output or activities level but per unit, variable cost is constant with in a certain period. Variable cost are controllable cost so management has to give priority to control variable cost. In NTC CVP analysis is not practicing. So, costs are not segregate into variable and fixed. Based on the nature of the cost and assumption various types of cost is segregate into fixed and variable cost. Variable cost of NTC are as follows:



**Table 4.8**  
**Variable Cost of NTC**

<b>particular</b>	<b>02/03</b>	<b>03/04</b>	<b>04/05</b>	<b>05/06</b>	<b>06/07</b>	<b>07/08</b>
Operating & Maintenance cost	45381	503303	490886	463300	452162	655127
Commission exp.	453831	503303	9110	11183	20138	22690
Total variable cost	453831	503303	500796	474483	572300	677817
Charge %	453831	10.9%	(0.50%)	(5.25%)	2060%	10.07%

Sources: Annual report of NTC

Operating and maintenance cost and commission are taken as variable cost in NTC

From above table, no.4.11 shows the variable cost of NTC. Total variable cost of N.T.C is operating and maintenance cost and commission expenses. Total variable cost in the year 2002/03 is Rs.453831 thousand and increased 10.9% in this year. In year 2003/04 variable cost are decreased by 0.50% and 5.25% in 2003/04. Nevertheless, in year 2004/05 variable cost of N.T.C is increased by 20.60%. Variable cost is controllable cost. So, management should try to reduce this cost.

#### **4.8 Fixed cost:**

Fixed cost remains constant in total despite the changes in the level of activities with in every year. When production cost or service cost are changed but fixed cost remains same. The per unit fixed cost may decreased while the number of production units are increased. Though fixed cost in total may vary for different fiscal year. The fixed cost of N.T.C is presented here are based on the assumption and nature of cost. Because of cost segregation tools are not applied in these enterprises. Fixed cost of NTC is presented in table below.

**Table 4.9**  
**Fixed cost Analysis** (Rs 000)

<b>Particular</b>	<b>2002/03</b>	<b>03/04</b>	<b>04/05</b>	<b>05/06</b>	<b>06/07</b>	<b>07/08</b>
Employee cost	773630	664192	717408	927254	1136819	1164811
Adm. exp	577402	949569	861460	1443939	920773	442821
Interest on subscribers deposit	67396	68375	82249	86650	57036	63938
Interest on loan	143654	38407	15955	3292	696	1108
Depreciation	799491	863863	931685	1016309	1048436	1195081
Bonus	170396	174982	180670	183763	187999	195349
Incentive Package	107825	131231	120969	125449	93713	126691
Loss/gain on foreign currency	(207992)	(157993)	162000	28443	(251124)	(280005)
Total fixed cost of NTC	2431802	2732626	3072396	3815069	3194348	2909794
% change		12.37%	12.43%	24.17%	(16.27)	(8.91)

Sources: Annual report of NTC

From the above table there is increasing trend in the fixed cost of NTC. In the year 00/01 total fixed cost is Rs. 2431802 thousand and increased by 12.37% it has increased to 12.43% in 004/05 but in year 2005/06 fixed costs increased by 24.17%. It is more than other year. In year 2006/07, total fixed cost of NTC is Rs.3194348, which is less than the previews year. The company is able to reduce the fixed cost by 12.27% in the same year

#### **4.9 Semi variable cost analysis:**

Semi variable cost is combined cost of both fixed cost and variable cost. Fixed cost should bear for certain level and is the level of output or services is increased excess amount should spend that cost can be taken as variable cost. For example repair and maintenance, supervision, fuel energy etc. Cost consists both fixed and variable cost.

NTC has not segregated the cost into variable and fixed. So, semi variable cost also accumulated in total cost.

#### 4.10 Cost volume profit analysis:

Cost volume profit analysis is a popular and very reliable management accounting tool to measure and analysis the financial performance of the organization. It is a part of profit planning and control. CVP analysis can be extended to cover the effects on profits of changes in selling price or service fees, cost, income tax rate and production mixed. CVP analysis provides the management with a comprehensive overview of the effects on revenue and costs of all kinds of short run financial changes. CVP analysis helps to determine the minimum sales volume to avoid losses and sales volume at which the profit of the company will increase. When the management has detail information about variable and fixed cost, selling price and sales volume of the product then the company can determine the break even level of its product. Income statement shows the picture of company, how it is earning profit. Here, the income statement of NTC is shown below based on its revenue, variable cost and fixed cost.

**Table 4.10**  
**Income Statement (Rs millions)**

<b>Particular</b>	<b>2002/03</b>	<b>03/04</b>	<b>04/05</b>	<b>05/06</b>	<b>06/07</b>	<b>07/08</b>
Operating income	5487	6160	7208	8312	8585	10413
Total variable cost	454	503	501	474	572	678
C.M.(1-2)	5033	5657	6707	7838	8012	9735
Total fixed cost	2432	2733	3072	3815	3194	2909
Profit.(3-4)	2601	2924	3635	4023	4818	6826
Other income (no n - operating )	441	396	461	543	610	645
Profit including no n-operating income (5-6)	3042	3320	4096	4566	5428	7471
Profit % on Revenue	47.40%	47.47%	50.43%	48.40%	56.13%	65.55%

From above table, the income statement figure of NTC can understand. NTC is earning profit in increasing trend. Variable and fixed cost is also increasing. Profit on sales is 47.40% and 47.47% in year 2002/03 and 2003/04 respectively. In year 2004/05, profit was 50.43%, which was more than previous year. In fiscal year 2005/06 company, profit was reduced by 2% and only able to earn 48.40% but in year 2007/08, company earned 56.13% profit on sales revenues. It was also higher than previous year in fish can year 2007/08 the profit was amazingly increased to 65.55%.

#### **4.11 Analysis of contribution margin (profit volume) Ratio, BEP, margin of safety:**

In cost volume profit analysis, we have to compute various ratios, which are important in revenue planning C.V.P analysis aim will fulfill when we are able to analyze all these parts of CVP's tools. Contribution margin is the difference between sales revenue and variable cost. This amount equals with fixed cost and profit. Contribution margin = sales - variable cost. Contribution margin is known as profit volume ratio (p/v ratio) or cm ratio. This can compute by dividing the sales to contribution margin. Break-even point (Level) is "no profit no loss" point. Where cost and sales revenue become equals. It is very necessary to know the BEP for every organization. BEP can compute in Rs or (level of output) unit.

$$\text{BEP in Rs.} = \frac{\text{Fixed cost}}{\text{P/v ratio}}$$

Margin of safety is the excess of budgeted or actual sales over the break even sales volume. The firms do not incurred loss on safety margin because it is higher than BEP. The firms earn profit in this level.

**Table no 4.11**  
**Computation of various ratios of NTC and analysis**

<b>particular</b>	<b>2002/03</b>	<b>03/04</b>	<b>04/05</b>	<b>05/06</b>	<b>06/07</b>	<b>07/08</b>
Sales	5487	6160	7208	8312	8584	10413
Contribution margin	5033	5657	6707	7838	8012	9735
P/V ratio (cm /sales)	0.92	0.92	0.93	0.94	0.93	0.93
fixed cost	2432	2733	3072	3815	3194	2909
BEP (fixed cost \ p/v ratio)	2643	2939	3303	4059	3434	3111
BEP on %	48.17%	47.715	45.82%	48.83%	40%	30%
Margin of safety (AS-BE)	2844	3221	3905	4253	5150	7302
MOS as percentage of sales	51.83%	52.19%	54.18%	51.17%	60%	70%

According to the above table we can interpret that the sales of NTC in F/Y 2002/03 was Rs. 5487 million. Growing gradually it was 10413 million in F/Y 2007/08 likewise contribution margin of NTC in F/Y 2002/03 was 5033 million. Growing gradually it was 9735 million in F/Y 2007/08. BEP ( Fixed cost, P/V ratio) in F/Y 2002/03 was 2643 million. Growing gradually it was 4059 million in F/Y 2005/06. But it became gradually less and it was 3111 million in F/Y2007/08. likewise margin of safety (AS-BE) in F/Y 2002/03 was 2844 million. Growing gradually it was 7302 million in F/Y 2007/08.

**Table 4.12**  
**BEP considering other income and other expenses**  
**BEP Rs = fixed cost – other income + other expenses**  
**P.V or CM ratio**

<b>Descriptions</b>	<b>2002/03</b>	<b>2003/04</b>	<b>2004/05</b>	<b>2005/06</b>	<b>2006/07</b>	<b>2007/08</b>
Fixed cost	2432	2733	3072	3815	3194	2909
Non operating income (other income)	441	396	461	543	610	645
Fixed cost after deducting other income	1991	2337	2611	3272	2584	2264
PV ratio	0.92	0.92	0.93	0.94	0.93	0.93
BEP	2164	2540	2808	3781	2778	2434
Margin of safety (AS. BES)	3323	3620	4400	4831	5806	7979
MOS as % of sales	60.56%	58.77%	61.04%	58.12%	67.64%	76.62%

Table No. 4.15 shows the detail cost volume profit system of NTC. Relationship among various variables shows the actual position of NTC about contribution margin, BEP level and safety margin and its percentage. As well as BEP volume of NTC is computed including other income this shows different break even volume than when excluding it in previous part.

Contribution margin of NTC is 0.92, 0.92, 0.93, 0.94, 0.93 and 0.93 in fiscal year 2002/03 to 2007/08.

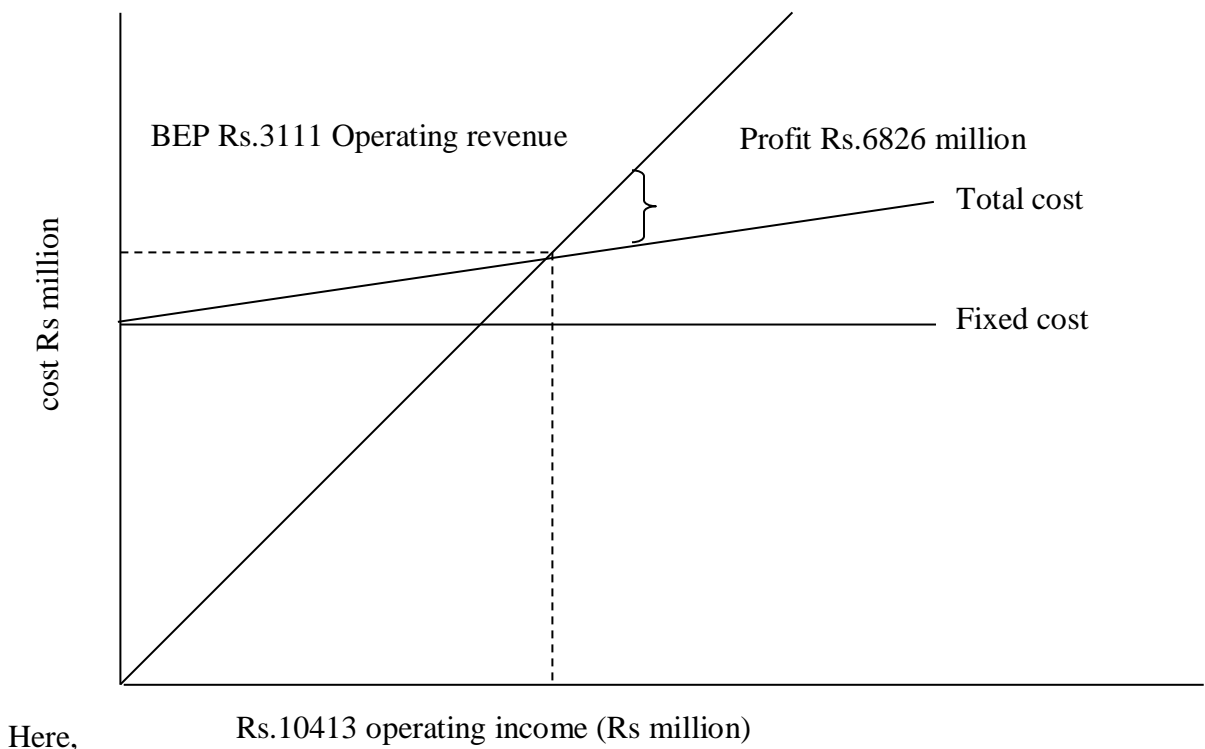
Company is in profit position because its margin of safety is above the break even sales volume. Percentage of BEP on sales are 48.17%, 47.71%, 45.71%, 45.82%, 48.83%, 40% and 30% from fiscal year 2002/03 to 2007/08 respectively. NTC has Rs 2844 million-safety margin in 2002/03 which is 51.53% of actual sales. The MOS are 52.29%, 54.18%,

54.18%, 51.17% 60% and 70% in that respective year. MOS is Rs 7302 million in year 2007/08.

Other income, which is non-operating income of NTC is included in fixed cost and computed BEP and margin of safety. It has reduced the BEP volume and increased the safety margin and its percentage. Lower the break even point / volume is good for the company to earn profit.

The computation can be presented in graphical form, which is as follows graphical presentation of BEP (Rs) for the fiscal year 2007/08.

**Figure 4.5**



- Variable cost = Rs.678 million
- Fixed cost = Rs 2909 million
- Total cost = Rs.3587 million
- Sales revenue = Rs.10413 million

BEP sales = Rs.3111 million

Profit = Rs. 6826 million

A simple break-even chart of NTC for the fiscal year 2007/08 is show above. Sales revenue is shown is x-axis and cost amount is shown in y-axis.

From the above chart, the total fixed cost of the company is Rs.2909 million. It is parallel to x-axis variable cost directly varies of with cost of production therefore it is slopping upward to right side. If not operation of the company variable cost become zero but the company should bear the fixed cost. Total sales revenue cost curve originates from the origin because sales revenue is zero, when sales volume zero. Moreover, service or sales volume increase sales revenue increase. The equilibrium point where sales revenue and total cost line is crossed this point line is called break even level or volume. Below this point the company can not cover its cost as a result it suffers loss. In addition, above this point sales revenue exceeds the total cost, which provides the profit to the company. In the figure, NTC has higher sales revenue than cost.

The sales revenue is Rs.10413 million where as total cost is Rs.3587 million. As a result, NTC is able to earn Rs.6826 million point.

#### **4.12 Major Findings**

Every research work is done to find something new, based on the objective of the study. From analysis of various data collected by primary and secondary sources, the major findings of the study are as follows:

1. Actual operating income of the NTC is increasing in fluctuating trend. Sales plan of NTC is not systematic. So, it has not achieved its target to increase operating income.
2. NTC has not adopted of practice of preparing monthly revenue earning reports.
3. The revenue plan prepared by the branches and sub branches were not taken as reference for preparation of central revenue plan.



4. Segregation of fixed, variable cost is ignored by this enterprise CVP analysis is not practicing by NTC. No any method has been adopted to segregate cost into fixed and variable.
5. There was consistency between planned sales and actual sales, their correlation was high.
6. Variable cost of NTC is very less compared to its fixed cost. Contribution margin ratio of NTC is very high.
7. Fixed cost of NTC is high in the comparison to variable cost. Employee cost and administration expenses are high.
8. Contribution to Revenue:
  - a. International trunk was highest contributor in revenue.
  - b. Domestic category was the second highest contributor in revenue and remained profitable.
  - c. Mobile phone also contributed 18.39% in revenue in 2007/08.
  - d. Card phone and coin phone categories were the smaller contributor in revenue.
  - e. CDMA phone contributed negligible part in revenue. Where as others sources contributes 6.28% in revenue.
9. Collection period and debtors turnover showed decreasing trend.
10. NTC is maintaining its periodic performance report systematically.
11. High PV ratio of NTC reduced the break even level of the company and margin of safety is near about 55% in average.
12. NTC has launched various services to its customers to increase revenue but in rural area it is not able to fulfill the demands of customers for communication services.
13. Profit position of NTC is good but lack of systematic plan. Operating profit is satisfactory but net profit is not good. A popular and reliable accounting tool. CVP analysis is not applying to analyze the financial performance.
14. NTC has a practice of preparing both strategic long term and tactical short run revenue plan. But the study is mainly focused on tactical short-run revenue plan of NTC.

## CHAPTER - V

### SUMMARY, CONCLUSION AND RECOMMENDATION

#### 5.1 Summary:

After the Second World War many countries got political independence. Their desire of repaid growth to reach at the level of developed countries gave way to planned economy and establishment of PEs Nepal, being an under-developed country, adopted this principle an several PEs were established, Realizing that the repaid development of the country depends on industrialization, development of agricultural and proper utilization of abundantly found water resources, HMG established NTC for development Communication between public to government, a major infrastructure requirement for development.

NTC's market was monopoly but nowadays there are many competitive of NTC. It was continuously facing problem of liquidity due to the improper management of revenue and overdue account receivables. Foreign aid and loans had always solved the problem of liquidity. If NTC had been able to manage revenue efficiently, foreign loan would not have increase less rapidly. Thus NTC should mänge its revenue more efficiently for the interest of NTC and nation.

Planning is the essence of management and without it efficient management can not be imagined. Planning is the job of making things happens that would not otherwise occur. Management planning provides the base of performance of the four other managerial functions of organizing, staffing, leading and controlling. It is said that planning is the primary managerial function, which logically precedes all other functions.

Business or corporate planning is reasoning out how a business will get where it wants to go. The essence of corporate planning is to see opportunities and threats in the future, and exploit the opportunities and combat the threats.

Business budgeting or profit planning and control are a systematically devised tool to help management for corporate planning, it is a process of established goals, planning for attainment and subsequently comparing actual performance with performance goal. A budget formal statement of plans generally forth Rs, and paisa.

In NTC, revenue result from the sales of Telecom and is measured by change made to customers, Revenue is influenced by both external and planning with coordinates the efforts of revenue department Production department and all other departments.

Many factors should be considered for revenue planning including revenue trends, Limitation supply, potential competitors and general level of economy NTC must consider revenue planning as the starting point its overall planning.

The long-term objective of NTC is to generate economic production, CDMA sets and sky phone sets of telecom and proper utilization of huge amount of communication like as internet service, web SMS similarly ISD and STD phone sewa. NTC has articulated its mission as "Nepal Telecom as progressive, customer spirited and consumer responsive entry, is committed to provide nation-wide reliable telecommunication services to serve as an impetus to the social political and economic development of the country".

NTC has been adopting planning to fulfill its mission and objectives, Revenue planning is the most essential aspect as revenue is the base on which future of the authority depends.

As for as revenue planning in NTC is concerned there are some major flaws. The starting point is the revenue planning i.e. demand forecast lacks consideration of some major demand determinates. Though NTC has achieve the target` of planned revenue in overall basis, category-wise planned figure have not been achieve and NTC has not adopted the practice of preparing monthly budget. The communication required for planning is not proper. The trend of revenue is increasing and management has to manage hugger amount of revenue in future. Thus, NTC should apply corrective measures to eradicate the flaws revenue planning.

## **Prepaid Calling Card (PCC) Service**

The Prepaid Calling Card (PCC) Service, which is commercially known as "Easy Call", has become very popular. Like its commercial name it is very easy to make Local, STD and ISD calls from Nepal to any place around the world using PCC cards, PCC service for making ISD calls was previously accessible from Nepal Telecom's PSTN phones, Payphones and fixed Post Paid CDMA phones only. For the benefit of the people, this service has been made accessible even from Postpaid Mobile phones from 17<sup>th</sup> September 2006.

PCC Cards of face value Nrs. 1000, 500 and 200 are available in the market with a validity period of 18, 12 and 6 months respectively from the first date of using the card.

Thus, NTC should try to reduce technical loss by improving its transmission system and non-technical loss by adopting legal, managerial, Social and other measures.

### **5.2 Conclusions:**

After analyzing the present practice of revenue planning and impact on profitability, the following conclusions are made:

1. NTC has not considered demand deterrents such as family income, price of call of one minutes, connection charge, cost of alternative available, cost of auto generation of telecommunication and reliability of NTC service which forecasting demand.
2. NTC has not prepared planned and programmed for distributions SIM cards to their consumers.
3. While setting the target sales for next year, NTC has not considered other factor such as growth of consumer and other relevant factors.
4. Target growth in sales revenue is achieved but not proper planned.

5. There is consistency between planned sales and actual sales as a whole. The analysis of category-wise revenue planned shows that achievement in domestic, international commercial and non-commercial categories are highly constants. But the achievement in remaining categories is highly fluctuating.
6. NTC has better trading profit comparatively other public enterprises.
7. While preparing future plan of NTC, suggestions of branches and sub-branches are ignored.
8. NTC has the practice using 10% increment over the figure the past year to forecast next year's sales as "benchmark".
9. Average consumption of such category differs by each year. NTC has efficient capacity fulfill the demand of its customers. But NTC has not been practiced for fulfilled customer's demands. This may be one of the reasons of it's operate low capacity.
10. Analysis of consumption or use of mobile, there is no good networking system some times consumers faced network problem similarly in land line phone.
11. The loss accrued due to the technical and non-technical reason. That may be attributed to the irresponsible and unauthorized use of telephone. Other factors contributing to non- technical losses are faulty billing devices in use, on accountable public installation such as coin telephone and card phone, and NTC's inefficiency to records its own consumption.
12. NTC's overdue of receivable is increasing year by year. It denotes inefficiency of NTC to collect its revenue in time.
13. NTC has no clear cut boundaries to separate cost into fixed and variable. The classification of cost is not scientific and systematic. Therefore, NTC has not been able to make realistic budget.
14. NTC has not adequately considered controllable and non-controllable variables affecting the organization.

### **5.3 Recommendation:**

After analyzing the present's practices of revenue planning in Nepal Telecom Company, the following recommendations are made:

1. NTC planners should be trained about revenue planning.
2. NTC should be considered demand determinants such as family income, price of telephone sets, SIM card and cost alternatives available, cost of self-mobile service such as voice mail cost, message cost. And reliability of NTC service while forecasting demand.
3. NTC should prepare plans and program for consumer and solve network problems.
4. To achieve target growth rate in sales revenue NTC should make realistic forecast.
5. NTC should start to practice of preparing monthly budget for sales revenue.
6. While preparing central budget of NTC, it should take suggestions made by branches and sub-branches.
7. NTC should avoid the practice of using 10% increment as benchmark figure in the preparation of budget.
8. NTC should introduce programmed and action plans to solve network problem and stolen telephone lines and misused of telephone call reduction the loss of technical and non-technical.
9. NTC should effectively check and control the unauthorized use of telephones.
10. NTC should put more effort to manage the supply to the profitable sectors such as domestic, national and international wise.
11. There should be provide more facility to their customer than other telecommunications such as Mero Mobile and United Telecom.
12. NTC should set clear boundaries about fixed and variable cost.
13. Cost volume relationship should be considered while formulating the revenue plan.

An effective cost control programme is necessary in NTC.

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**Used Formula:**

i) Arithmetic mean of budget sales

$$\text{mean } (\bar{x}) = \frac{\sum X}{N} = \frac{453.143}{6} = 75.524$$

ii) Arithmetic mean of actual sales

$$\text{mean } (\bar{Y}) = \frac{\sum Y}{N} = \frac{460.655}{6} = 76.776$$

iii) Standard deviation of budgeted sales

$$\begin{aligned} \text{S.D } (\sigma_x) &= \sqrt{\frac{\sum x^2}{N}} \\ &= \sqrt{\frac{844.780}{6}} = \sqrt{140.796} \\ &= 11.865 \end{aligned}$$

iv) Standard deviation of Actual sales

$$\begin{aligned} \text{S.D } (\sigma_y) &= \sqrt{\frac{\sum y^2}{N}} \\ &= \sqrt{\frac{2668.03}{6}} \\ &= 21.087 \end{aligned}$$

v) Coefficient of Variation for Budgeted sales

$$\begin{aligned} \text{CV of } x &= \frac{\sigma_x}{\bar{X}} = \frac{11.865}{75.524} \times 100 \\ &= 15.71\% \end{aligned}$$

vi) For Actual Sales

$$\begin{aligned} \text{CV of } y &= \frac{\sigma_y}{\bar{Y}} = \frac{21.087}{76.776} \times 100 \\ &= 27.46\% \end{aligned}$$

Vii) Coefficient of correlation using Karl Pearson's correlation coefficient between x and y

$$\begin{aligned}r &= \frac{\sum xy}{\sqrt{\sum x^2} \times \sqrt{\sum y^2}} \\&= \frac{1158.163}{\sqrt{844.780} \times \sqrt{2668.03}} \\&= 0.77\end{aligned}$$

Viii) Probable error of r

$$\begin{aligned}\text{PE (r)} &= 0.674 \times \frac{1-r^2}{\sqrt{N}} \\&= 0.674 \times \frac{1-(0.77)^2}{\sqrt{6}} \\&= 0.674 \times 0.1653 \\&= 0.111\end{aligned}$$

14.