

Christina Chase was appointed CEO of Oshkosh Systems at the end of 20X3. Oshkosh manufactures several popular products, but is only achieving marginal financial success. Christina's first mission is to review operations and attempt to refine processes to improve financial condition and profitability.

On the following pages are the budgeted financial statements for the upcoming year.

Christina has identified three specific strategies to improve performance as follows:

- 1 Adopt strategies to reduce ending inventory levels by half. Assume that 80% of this reduction will be offset by a reduction in notes payable, and 20% will be offset by a reduction in accounts payable. The debt reduction is expected to decrease interest incurred and paid by \$150,000. Any benefit to income will be offset by a 40% tax cost, and the tax effect will result in a corresponding change in cash. This strategy will be achieved by reducing cost of goods manufactured to \$3,500,000.
- 2 Adopt strategies to reduce corporate facilities used for SG&A. The company could immediately sell one of its buildings for \$700,000. The building currently has a cost of \$1,000,000, and accumulated depreciation of \$300,000. The budgeted balance sheet (as of the end of the year) includes the building at \$1,000,000, with accumulated depreciation of \$350,000. The budgeted SG&A includes \$50,000 of anticipated depreciation during 20X4. The \$50,000 increase in income, via the reduction of depreciation, will result in a corresponding \$20,000 (40%) increase in taxes. The net after-tax cash generated from this transaction would be held in the Cash account.
- 3 Adopt strategies to accelerate collection of accounts receivable. The company currently carries about 90 days sales in receivables, and desires to reduce this to 60 days. The extra cash generated will be used to reduce accounts payable by \$300,000, and the remainder will be held in the Cash account.

Revise the budgeted income statement and balance sheet to reflect the preceding strategies. Evaluate the impact of Christina's three proposed actions.



	A	B	D	E
1	Oshkosh Systems			
2	Budgeted Income Statement			
3	For the Year Ending December 31, 20X4			
4	Sales		\$10,000,000	
5	Cost of goods sold			
6	Beginning finished goods	\$2,000,000		
7	Cost of goods manufactured	<u>5,000,000</u>		
8	Goods available for sale	\$7,000,000		
9	Less: Ending finished goods inventory	<u>3,000,000</u>		
10	Cost of goods sold		<u>4,000,000</u>	
11	Gross profit		\$ 6,000,000	
12	SG&A		<u>5,500,000</u>	
13	Income before interest and taxes		\$ 500,000	
14	Interest		<u>300,000</u>	
15	Income before taxes		\$ 200,000	
16	Income taxes (40%)		<u>80,000</u>	
17	Net income		<u>\$ 120,000</u>	
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	A	B	C	D
1	Oshkosh Systems			
2	Budgeted Balance Sheet			
3	December 31, 20X4			
4	Assets			
5	Current assets			
6	Cash	\$ 700,000		
7	Accounts receivable	2,400,000		
8	Raw materials inventory	1,000,000		
9	Finished goods inventory	<u>3,000,000</u>	\$7,100,000	
10	Property, plant, & equipment			
11	Plant and equipment	\$ 4,250,000		
12	Less: Accumulated depreciation	<u>(1,700,000)</u>	<u>2,550,000</u>	
13	Total assets		<u>\$9,650,000</u>	
14	Liabilities			
15	Current liabilities			
16	Accounts payable	\$ 800,000		
17	Notes payable	<u>4,700,000</u>	\$5,500,000	
18	Stockholders' equity			
19	Common stock	\$ 1,400,000		
20	Retained earnings	<u>2,750,000</u>	<u>4,150,000</u>	
21	Total liabilities and equity		<u>\$9,650,000</u>	
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