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Let's Go Aero Travel Trailers: Incorporating the New Model of the Organization into the Teaching of Budgeting

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INTRODUCTION

Let's Go Aero manufactures travel trailers bought primarily by young families and retirees interested in a light, low-cost trailer that can easily be pulled by a mid-sized family car. The market for travel trailers has expanded nicely over the past few years due to the number of families seeking a relatively low-cost, outdoor vacation experience. But in the view of Let's Go Aero's president, Mark Newman, the real growth in the future is in the retiree market. Newman believes the vigorous health of the average retiree, coupled with the national trend toward a return to nature, will translate into continuing sales growth for Let's Go. As Newman loves to say, "camping recently moved from number seven to number six on the list of top 10 leisure activities in the United States, and the baby boomers are getting older every day."

THE RETIREE MARKET

Baby boomers (born between 1/1/46 and 12/31/64) carry a lot of consumer clout.

According to the National Opinion Research Center at the University of Chicago, 74% of boomers (aged 47—65) own their own home, 46% are satisfied with their financial situation, and 56% are married. The spending power of this demographic is likely to increase. People who are 50 years old and older are expected to inherit an estimated $14 to $20 trillion dollars during the next twenty years. Also, baby boomers make up a significant part of the total U.S. population. According to the U.S. Census Bureau, in 2006 baby boomers represented 26% of the populace. In that year there were just under 78 million boomers living in the United States, with the largest populations living in California, Texas, New York, Florida, and Pennsylvania.

Research indicates that for an organization to meet the needs of the senior market, including baby boomers, the following must be addressed:

- Independence and control,
- Intellectual stimulation and self-expression,
- Security and peace of mind,
- Quality and value.

Seniors respond to benefit-driven messages; to attract them, advertising has to communicate tangible benefits rather than features and amenities.

MARKETING AND SALES

The forecasted increase in Let's Go's sales can be seen in the company's sales projections presented in Exhibit 1 (actual for the years 2005 through 2010 and projected for the years 2011 through 2015). Although the weather can have a significant impact on the travel trailer industry (i.e., hurricane season, flooding, and even droughts have had negative effects on the sales and rentals of travel trailers), Let's Go's management believes these problems will be mitigated in the future by global warming. All sales projections are done by Mark Newman in his role as Let's Go's president.

To keep from losing sales, the company maintains finished goods inventory on hand at the end of each month equal to 300 trailers plus 20% of the next month's sales. The finished goods inventory on December 31, 2010, was budgeted to be 1,000 trailers. Jim West, Let's Go's vice president of marketing and sales, would rather see a minimum finished goods inventory of no less than 1,500 trailers. Jim refuses to talk to Tom Sloan, Let's Go's production manager. Tom is always trying to get Jim to consider adopting flexible inventory levels, which Jim is certain would affect his yearly bonus. The vice president of sales and marketing is eligible for a 20% bonus based on sales. Unfortunately, Jim did not receive a bonus in 2010. Sales were up, but Mark refused to give Jim the bonus, although it was earned, due to the high number of customer complaints. Jim was really steamed when he heard "no bonus." Didn't Mark know those complaints were for poor quality? All of Jim's efforts to grow sales and attract customers were, once again, destroyed by Tom Sloan and his production failures.

TRAILER PRODUCTION

Sheet aluminum represents the company's single most expensive raw material. Each travel trailer requires 30 square yards of sheet aluminum. The wholesale cost of sheet aluminum varies dramatically according to the time of year. The cost per square yard can vary from $15 in the spring, when new construction tends to start, to $8 in December and January, when demand is lowest.

The use of aluminum in vehicles, including travel trailers, is increasing rapidly due to a heightened need for fuel efficient, environmentally friendly vehicles. Aluminum can provide a weight savings of up to 55% compared to an equivalent steel structure, improving gas mileage significantly. The aluminum industry and suppliers are dispersed across four-fifths of the country, yet they are largely concentrated in four regions: the Pacific Northwest, industrial Midwest, northeastern seaboard, and mid-South. Although this is a broad geographic presence, Let's Go Aero will be affected by distribution costs.

Vicky Draper, Let's Go's vice president of purchasing and materials handling, is eager to implement just-in-time as a way of lowering Let's Go's aluminum cost. To offset the expense of distribution, Let's Go is located in Pennsylvania. Vicky's projected 20% bonus, recently announced by Mark and effective for year-end 2011, is based on her ability to lower total material cost. Initially enthusiastic about her job and ability to earn a significant bonus, Vicky has become discouraged and angry. She is unable to convince Let's Go's current aluminum supplier to sign a prime vendor contract, and her efforts to locate an alternative vendor, willing to accept the conditions of a just in-time contract, have similarly failed. She blames Tom Sloan. Let's Go's current aluminum vendor refuses to sign a just-in-time prime vendor contract due to Tom's uneven production schedule and his refusal to pay on time. Tom has been seen reading the help wanted ads, and Vicky over heard him talking to an employment agency.

In keeping with the policy set by Tom as Let's Go's production manager, the amount of sheet aluminum on hand at the end of each month must be equal to one-half of the following month's production needs for sheet aluminum. The raw materials inventory on December 31, 2010, was budgeted to be 39,000 square yards. The company does not keep track of work-in-process inventories.

Budgeted expenses for Aluminum and other materials, as well as wages, heat, light and power, equipment rental, equipment purchases, depreciation, and selling and administrative for the first six months of 2011 are given below.

	January	February	March
Aluminum	$816,000	$1,056,000	$888,000
Other materials	54,000	264,000	222,000
Wages	624,000	1,008,000	1,104,000
Heat, light, & power	130,000	195,000	220,000
Equipment rental	390,000	390,000	390,000
Equipment purchases	300,000	300,000	300,000
Depreciation	250,000	250,000	250,000
Selling & admin	400,000	400,000	400,000

	April	May	June
Aluminum	$552,000	$336,000	$240,000
Other materials	138,000	84,000	90,000
Wages	672,000	432,000	240,000
Heat, light, & power	135,000	110,000	110,000
Equipment rental	340,000	340,000	340,000
Equipment purchases	300,000	300,000	300,000
Depreciation	275,000	275,000	275,000
Selling & admin	400,000	400,000	400,000

Accounts for aluminum and other materials are paid in full during the month following their purchase. Accounts payable for aluminum and other materials purchased during December, 2010 totaled $850,000 combined. This amount will be paid in January, 2011.

COMPETITION

All forms of vacation and leisure activities, including theme parks, beach or cabin rentals, health spas, resorts, and cruise vacations compete with Let's Go Aero Travel Trailers for the consumer dollar. Other recreational purchases such as automobiles, snowmobiles, boats, and jet-skis are indirect competitors.

Travel trailer manufacturers such as Crossroads RV, Jayco, Coachman RV, and Scamp also offer a moderate-to low-priced travel trailer. Manufacturers that offer more diverse product lines such as high-end trailers with luxury accommodations could compete for the fairly affluent senior market.

Coachman RV, a direct Let's Go competitor, has become a leader in the recreational vehicle, motor home, and travel trailer industry through a commitment to quality and value based on excellence in engineering and attention to detail. Creative engineering, combined with high-accuracy analysis, reduced material costs at Coachman by more than 60% and labor costs by 78%.

BUDGET PREPARATION

To minimize company time lost on clerical work, Let's Go's accounting department prepares and distributes all budgets to the various departments every six months. Per Mark Newman, "Freeing departmental managers from the budgeting process allows them to concentrate on more pressing matters." In keeping with the recently announced bonus plan for the vice president of purchasing and materials handling, Newman has instructed the accounting department to budget aluminum at $8 per square foot. The accounting manager recently received a 20% bonus for having prepared the budgets on time with little or no help from the other functional areas.

CASH

Let's Go's vice president of finance, Becky Newman, has requested an $800,000, 90 day loan from the bank at a yet to be determine interest rate. Since Let's Go has experienced difficulty in paying off its loans in the past, the loan officer at the bank has asked the company to prepare a cash budget for the six months ending June 30, 2011, to support the requested loan amount. The cash balance on January 1, 2011, is budgeted at $100,000 (the minimum cash balance required by Let's Go's board of directors).

HUMAN RESOURCES

To accomplish the company's corporate strategic goals, Let's Go Aero Travel Trailers encourages upward communication among all its employees, from senior management to line employees. Decision making, although not an entirely democratic process, is based on a team approach. Newman, as Let's Go's president, encourages managers to think in terms of the marketplace and to look at the business of travel trailers as a whole rather than as functional department successes and decisions. In fact, Newman is so committed to the idea of cooperative management and teamwork that he has hired three separate human resource consultants in the past six months to lead the company's managers through team-building exercises.

REQUIRED

1. Discuss the validity and reasonableness of Let's Go's sale projections.
2. Prepare production, purchasing, and cash budgets for Let's Go for the first six months of 2011 using the formats below. (hint: spreadsheet programs are wonderful!):

PRODUCTION BUDGET

	Jan	Feb	March	April	May	June	Six Months
Budgeted Sales							
Add: desired ending inventory							
Total needs	-------	-------	-------	-------	-------	-------	-------
Less: beginning inventory	-------	-------	-------	-------	-------	-------	-------
Trailer production							

PURCHASES BUDGET	Jan	Feb	March	April	May	June	Six Months
Trailer production							
Sheet metal needs per trailer	-------	-------	-------	----------	-------	-------	-------
Total production needs							
Add: desired ending inventory	-------	-------	-------	-------	-------	-------	-------
Total materials needs							
Less: beginning inventory	-------	-------	-------	-------	-------	-------	-------
Total sheet metal purchases							
Cost per square yard	$____	$____	$___	$____	$____	$____	$____
Total cost	**$**	**$**	**$**	**$**	**$**	**$**	**$**

CASH BUDGET	Jan	Feb	March	April	May	June	Six Months
Cash beginning balance	$____	$____	$____	$____	$____	$____	$____
Add: cash collections							
Total cash available							
Less: cash disbursements							
xxxxx							
xxxxx							
xxxxx							
Etc.							
Total cash disbursements	------	------	------	------	------	------	------
Excess (deficiency)	____	____	____	____	____	____	____
Financing							
Borrowings							
Repayments							
Interest	____	____	____	____	____	____	____
Total financing							
Cash balance ending	**$**	**$**	**$**	**$**	**$**	**$**	**$**

Discuss the advantages and disadvantages of the budgets you have prepared. Who in the company does the budget help and whom, potentially, does it hurt. Does the budget help or hurt the sales department? What about production and finance? How are the various functional areas affected and why?

3. Andy Baxter, newly hired by Let's Go Aero from a competitor, suggests preparing the production budget assuming stable production. Prepare a second and third set of production, purchasing, and cash budgets. Hold production to a constant 3,000 trailers per month for the second set of budgets, and 3,500 trailers per month for the third set of budgets. The format for the purchasing and cash budgets should remain as presented in question 2. Use the following approach for the production budget:

Discuss the advantages and disadvantages of the second and third sets of production, purchasing, and cash budgets you have prepared. Who within the company do these budgets help and whom, potentially do they hurt? Do these budgets help or hurt the sales department? What about production and finance? How are the various functional areas affected, and why?

PRODUCTION BUDGET

	Jan	Feb	March	April	May	June	Six Months
Production (trailers)	3,000	3,000	3,000	3,000	3,000	3,000	18,000
Add: beginning inventory	____	____	____	____	____	____	____
Total available							
Less: budgeted sales	____	____	____	____	____	____	____
Ending inventory							

EXHIBIT 1.
ACTUAL AND PROJECTED SALES IN NUMBER OF TRAILERS

Actual sales	2005	2006	2007	2008	2009	2010
	13,765	14,880	15,991	17,809	19,634	23,322
Projected sales	2011	2012	2013	2014	2015	
	28,000	33,600	40,320	48,384	58,060	

4. What metric should Let's Go use to measure the performance of each manager in this case? What bonus system would you suggest that incorporates these measures and also encourages the managers to work as a team?

The detail sales for 2010 (actual) and 2011 (projected) by month are as follows:

	2010 Actual	2011 Projected
January	1,983	2,500
February	3,218	4,000
March	3,981	5,000
April	3,240	3,000
May	1,755	2,000
June	901	1,000
July	763	1,000
August	611	1,000
September	1,622	2,000
October	1,678	2,000
November	1,439	2,000
December	2,131	2,500
Total number of trailers	**23,322**	**28,000**

Actual sales in dollars for the last two months of 2010 and budgeted sales for the first six months of 2011 follow:

November 2010 (actual)	$1,439,000
December 2010 (actual)	$2,131,000
January 2011 (budgeted)	$2,500,000
February 2011 (budgeted)	$4,000,000
March 2011 (budgeted)	$5,000,000
April 2011 (budgeted)	$3,000,000
May 2011 (budgeted)	$2,200,000
June 2011 (budgeted)	$1,100,000

Past experience show that 25% of a month's sales are collected in the month of sale, 10% in the month following the sale, and 60% in the second month following the sale. The remainder is uncollectible.