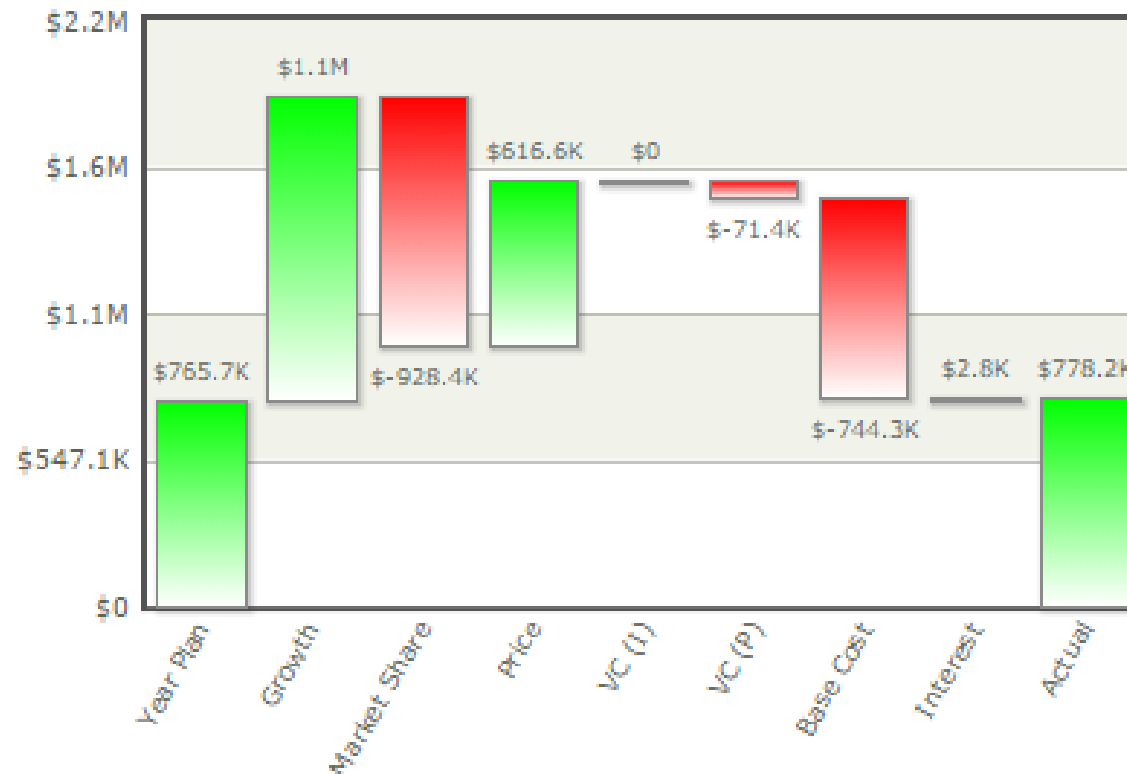
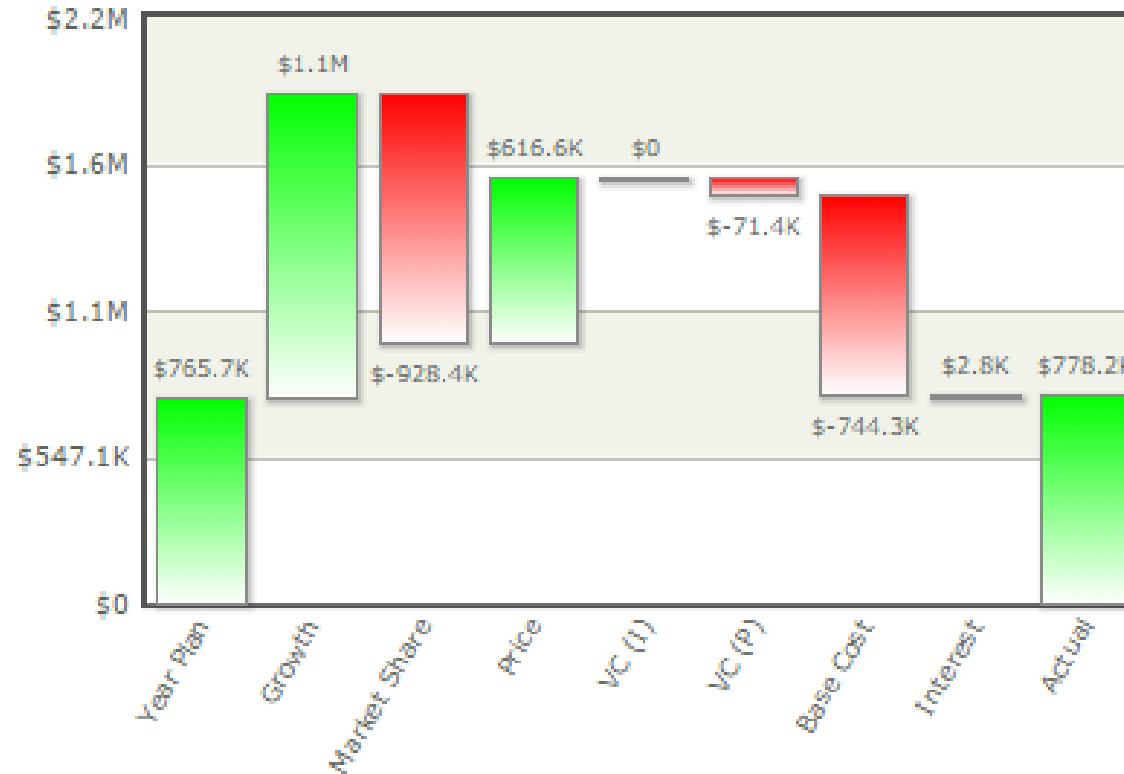


How to Analyze the 'Pre-Tax Income: Year Plan vs. Actual (or Actual + SRO)' Chart

Pre-Tax Income: Year Plan vs. Actual

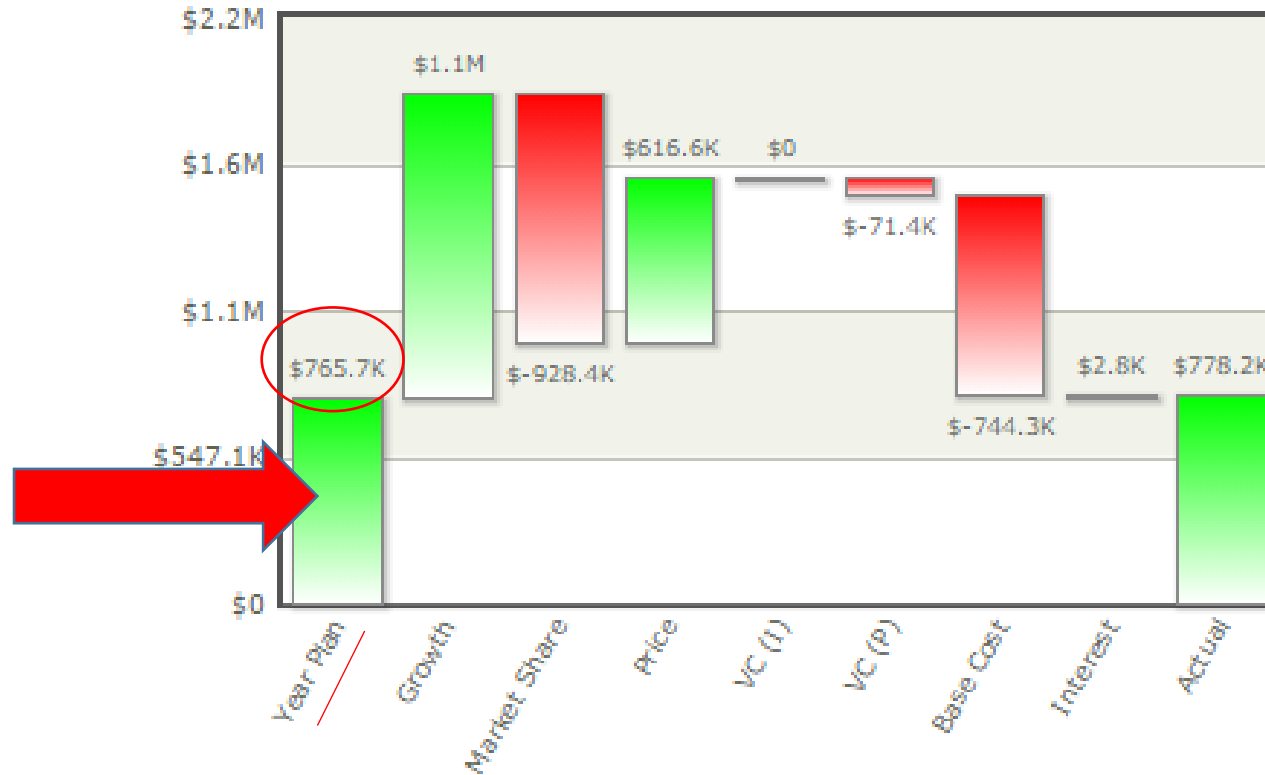


Pre-Tax Income: Year Plan vs. Actual



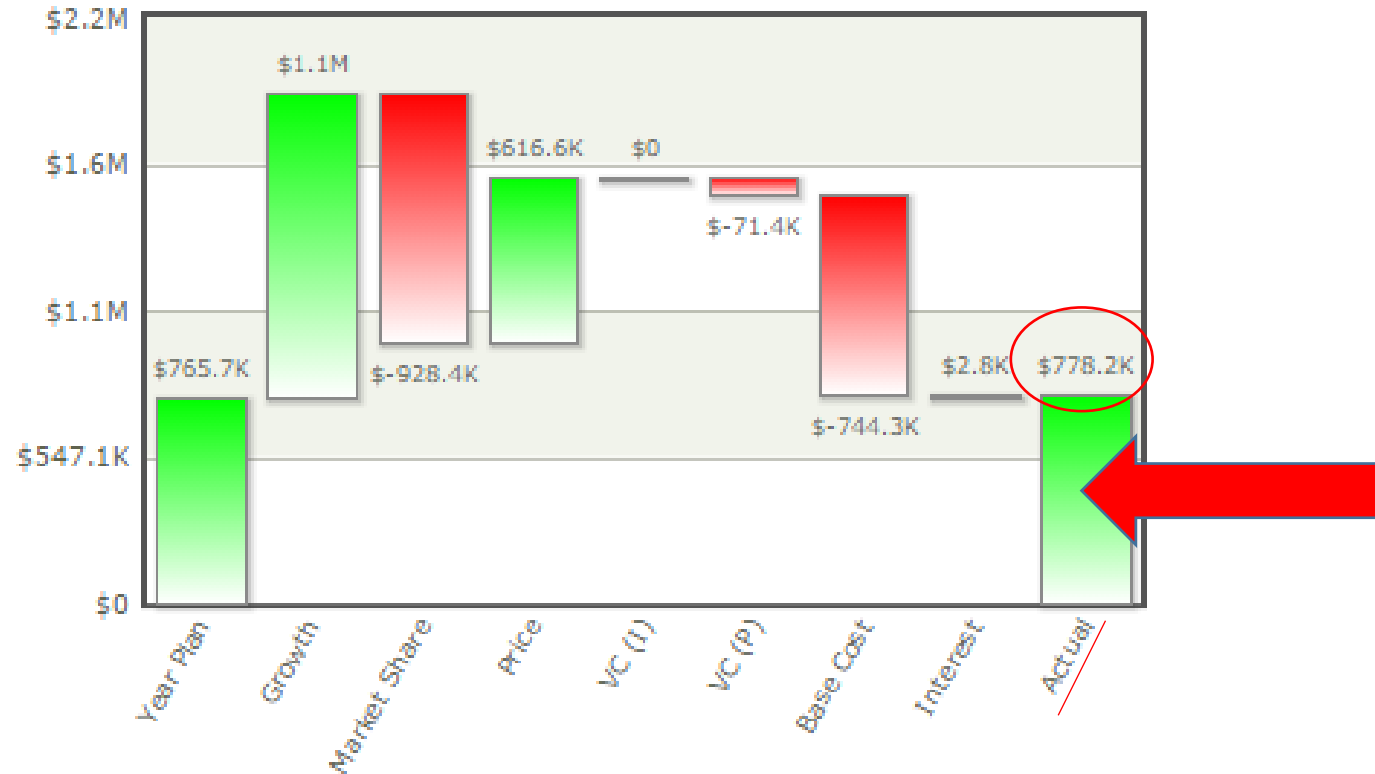
This chart tells you what your expected Net Income will be (if you have not completed all four quarters) or is (if you have completed all four quarters), and what the differences are between the plan and the actual. Key words to use when analyzing this chart are whether an item is **favorable** or **unfavorable** to plan.

Pre-Tax Income: Year Plan vs. Actual



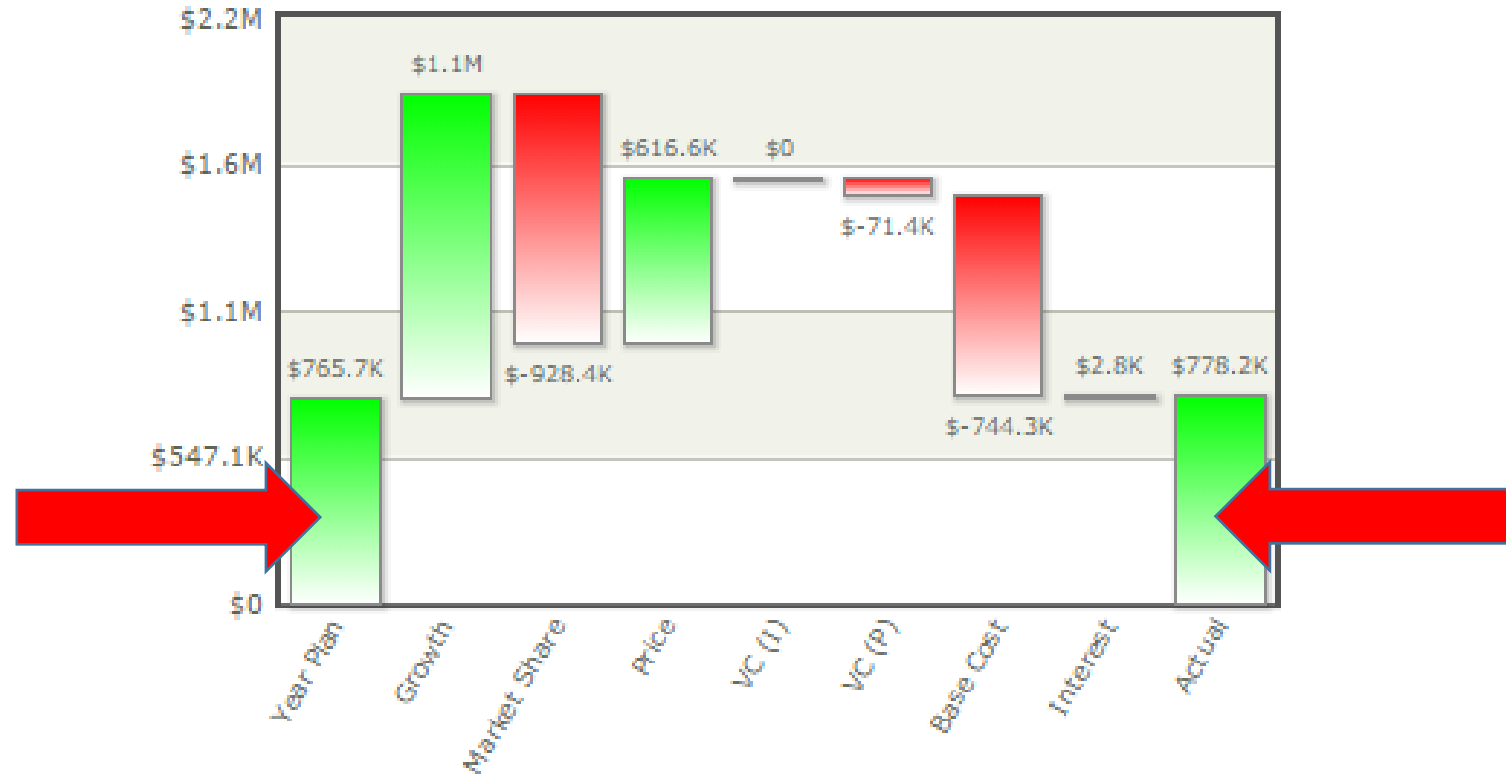
In this example, the Planned Net Income – your expected Net Income when you set your original plan – on a pre-tax basis – was \$765k. With a 50% tax rate, your planned after-tax Net Income was about \$382k, which is within the owner’s range of \$300k to \$400k. Remember that this chart will always show you the pre-tax amount, so you need to multiply by 50% to get the post-tax amount.

Pre-Tax Income: Year Plan vs. Actual



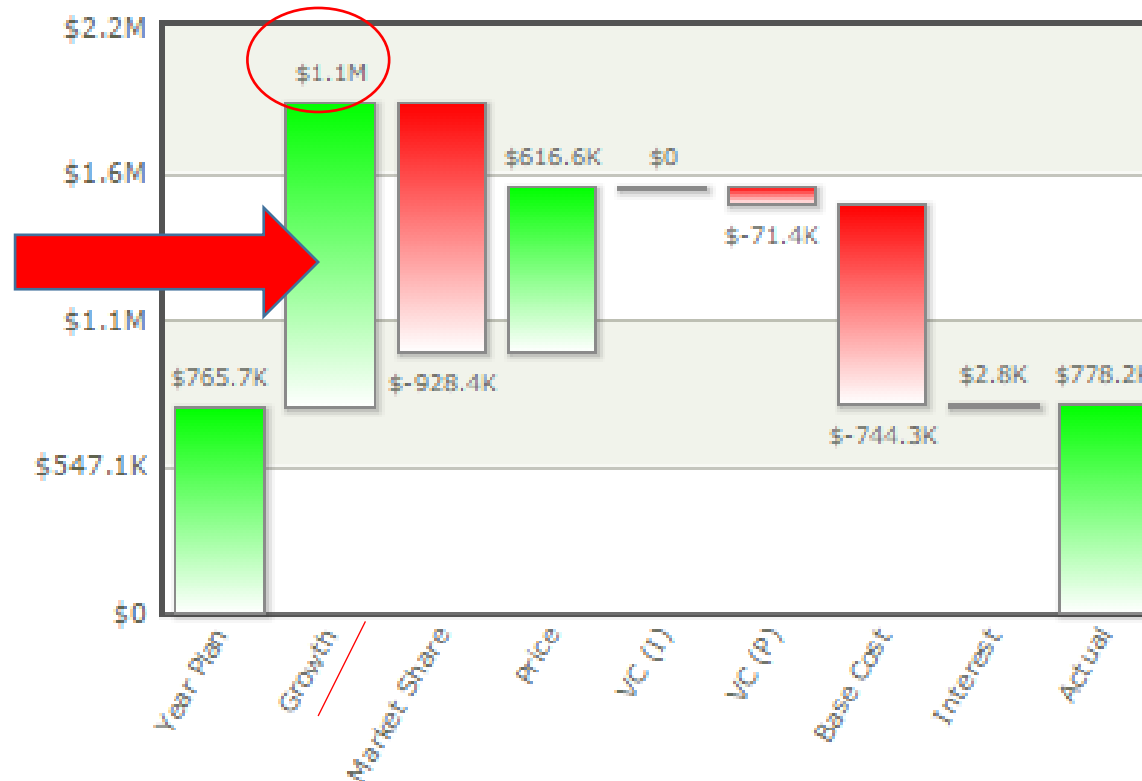
Because the title of the chart says 'Actual' instead of 'Actual + SRO', we know that all four quarters have passed, and these are the final results of the year. Here, our actual Pre-Tax Net Income is \$778k. With the 50% tax rate, our actual after-tax net income is about \$389k. We can see this actual number on the Income Statement.

Pre-Tax Income: Year Plan vs. Actual



The net difference between the pre-tax net income plan and actual is \$12.5k. After tax, that's \$6.25k, which means the estimate was very close to plan. However, when we break down the categories of variances, we see some big differences. Green means there was a 'favorable' variance to plan (which added to net income), and red means there was an 'unfavorable' variance (which took away from net income).

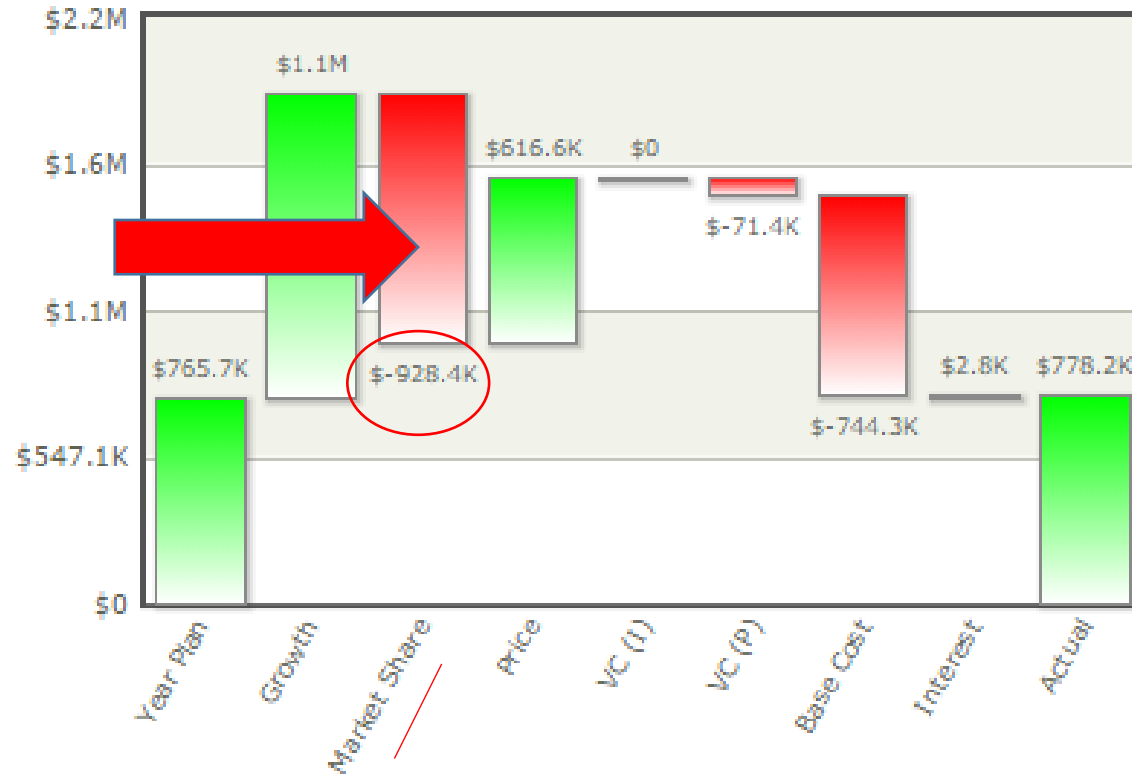
Pre-Tax Income: Year Plan vs. Actual



The first category is 'Growth' and the second category is 'Market Share'. They are related. 'Growth' asks, if you hit your planned market share, what did the total market demand do? In this case, the total market demand grew more than the plan anticipated, so there was 'upside' of over \$1mm in pre-tax net income added over the planned NI.

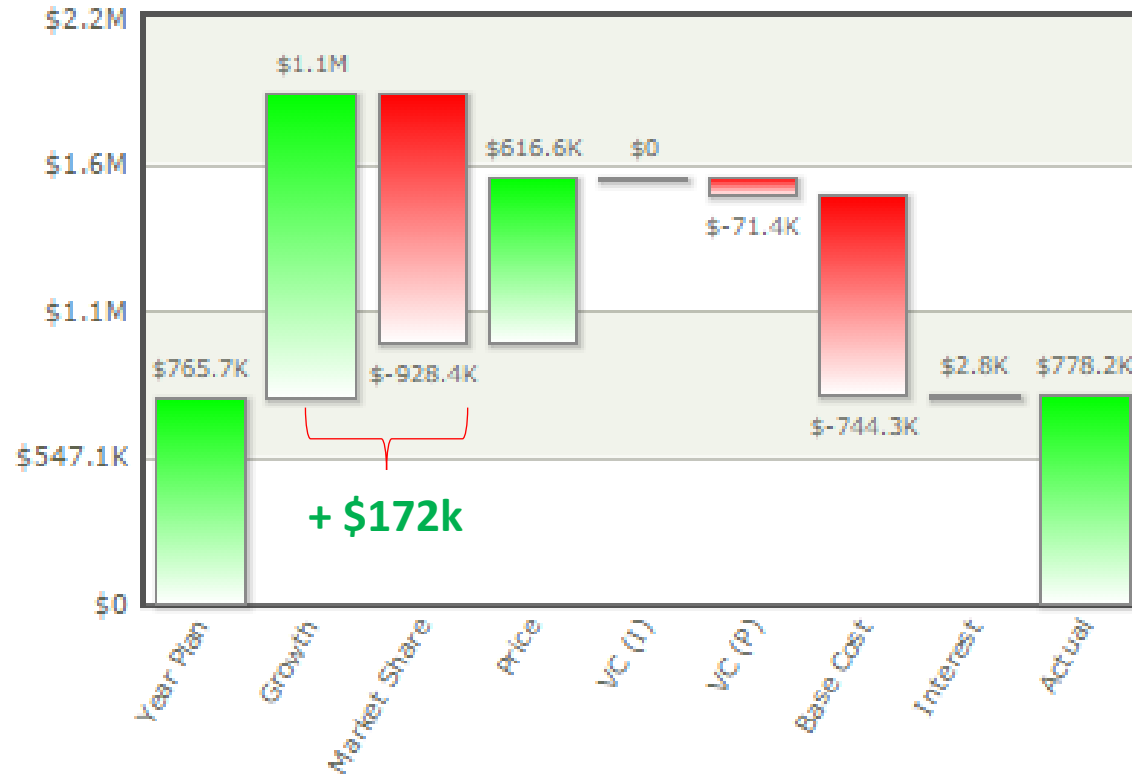
In your explanation in the QBR, you must identify *why* there is a favorable variance based on your analysis. For example, you might say 'Growth shows a favorable variance due to the launching of Project 3, which was not accounted for in the Plan. Total Market Demand grew X% over plan in Q3 due to the launch of the Project.'

Pre-Tax Income: Year Plan vs. Actual



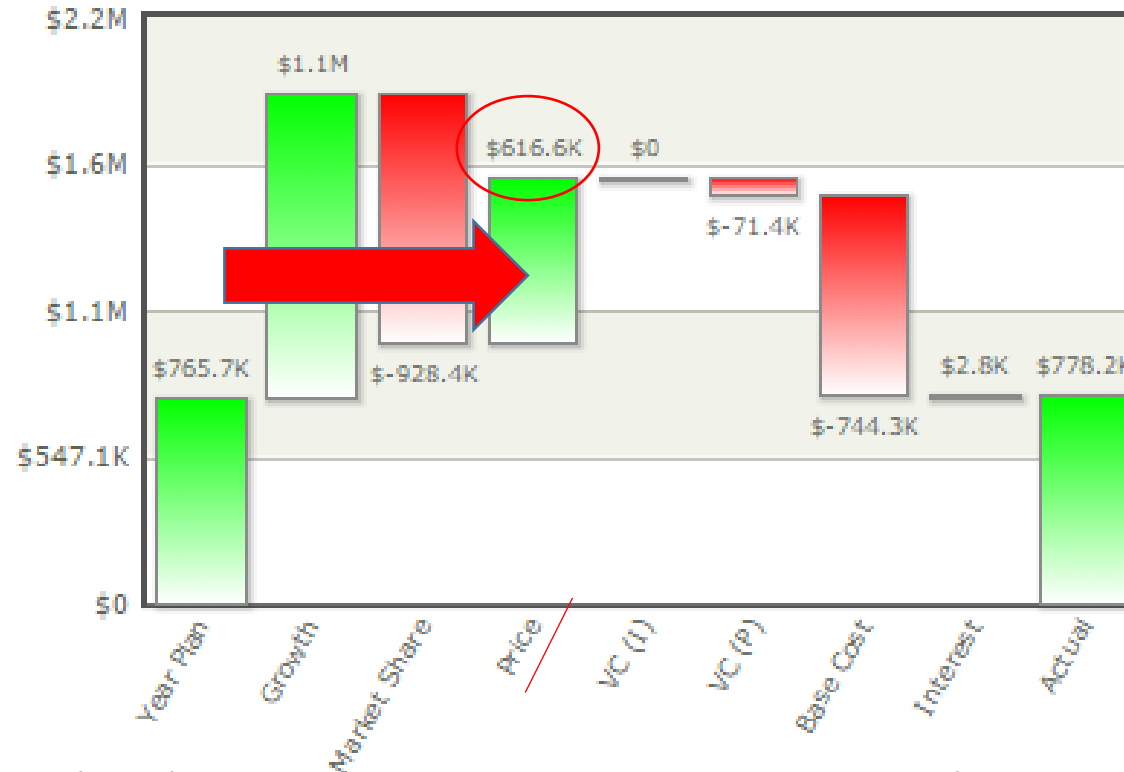
‘Market Share’ asks, if Total Market Demand (‘Growth’) was what you expected, how well did you estimate your Market Share? In this case, we overestimated our market share, so there was \$928k less net income than expected because of that. In your explanation in the QBR, you must identify **why** there is an unfavorable variance based on your analysis. For example, ‘Market Share is showing an unfavorable variance due to a decrease in Marketing Expense of \$X (Y%), which was necessary due to cash constraints.’

Pre-Tax Income: Year Plan vs. Actual



When you net 'Growth' and 'Market Share', you see that the under-estimation of Total Market Demand and the over-estimation of the market share result in an addition to pre-tax net income of about \$172k. The net will not always be positive. You must identify *why* there is an unfavorable variance in your explanation based on your analysis. For example, 'The net of the volume increase was favorable to Plan by \$172k (Z% over Plan), primarily driven by A, B, and C reasons.'

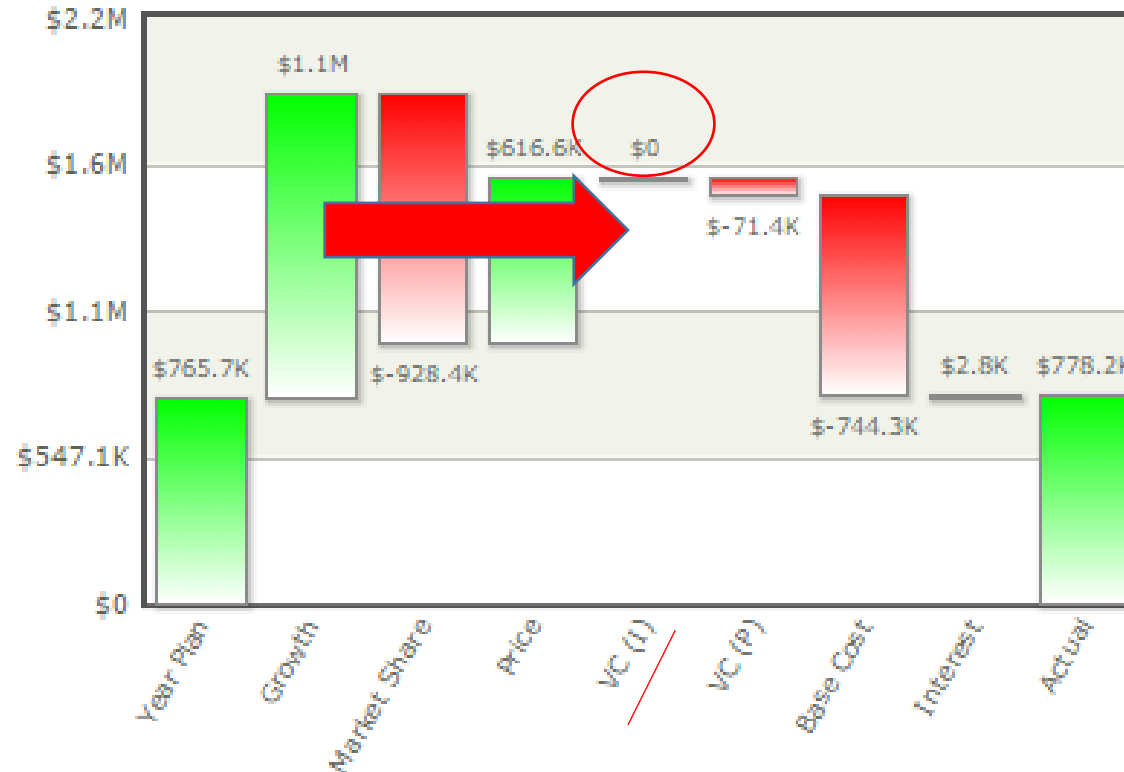
Pre-Tax Income: Year Plan vs. Actual



'Price' simply means that there was an increase in unit price over Plan some time during the year.

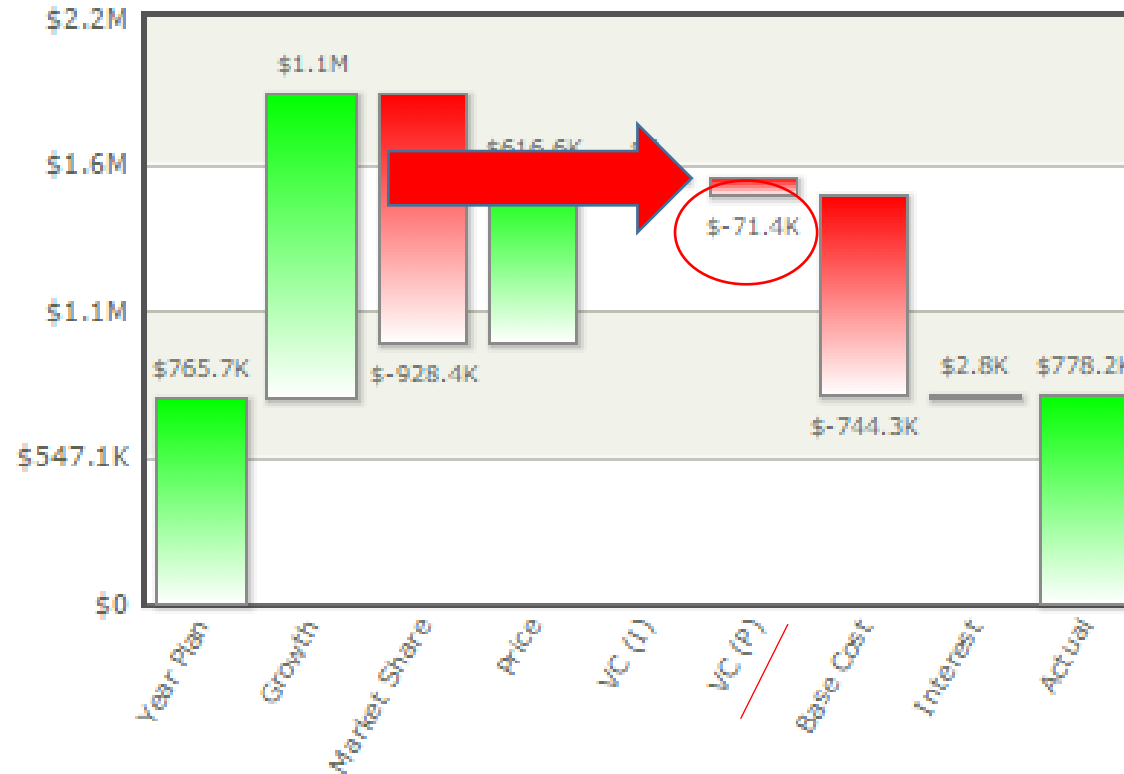
A price increase adds to Net Income over plan; in this case, there was an additional \$616.6k of pre-tax net income added to the plan estimate due to a price increase. Remember, increasing price may have a negative effect on the number of units a company sells, so market share may be negatively impacted due to a price increase. Your explanation should be similar to, 'Price was increased over Plan by \$X (Y%), resulting in a favorable variance to Plan of \$616.6k.'

Pre-Tax Income: Year Plan vs. Actual



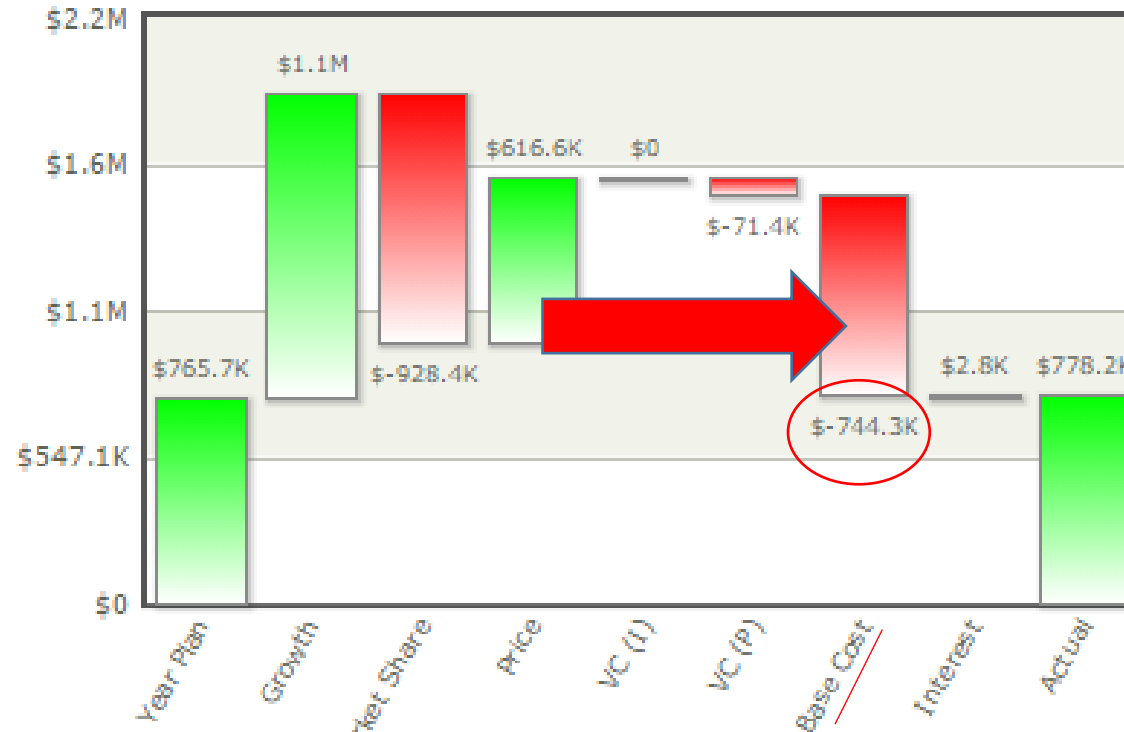
‘VC(I)’ stands for ‘Variable Costs (Inflation)’. It refers to your estimate of the price you are paying for your raw materials and labor. Usually, we want the variable costs to be less than, or on target with, the plan. In this example, the price of the raw materials and labor was exactly as planned. If there had been a negotiation with the raw material supplier, we would see a green bar in this category, meaning that we had a favorable variance to plan by reducing our variable costs. Assuming there was a favorable variance, your explanation should be similar to, ‘VC(I) generated a favorable variance to plan due to negotiations with Mr. A, resulting in a decrease in cost of ABC of X%.’

Pre-Tax Income: Year Plan vs. Actual



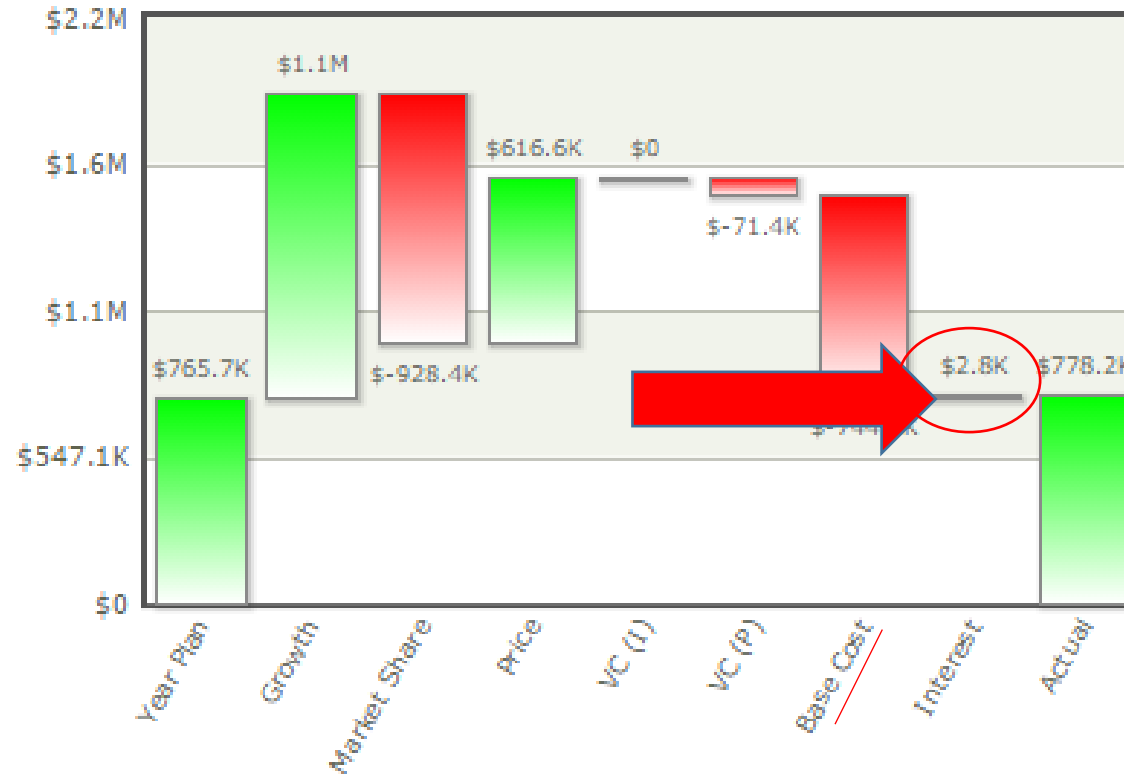
‘VC(P)’ stands for ‘Variable Costs (Productivity)’. It refers to your estimate of how productive your employees were. For Hisco, productivity is seen as ‘Processing Time’. Above, there is a red bar, which means that productivity was unfavorable to Plan, which means we over-estimated the processing time in our Plan. It took longer to make our readers than planned, which cost us \$71k in pre-tax net income. In your explanation, you must identify **why** there is an unfavorable variance based on your analysis. For example, ‘VC(P) was unfavorable to Plan by \$Y (X%) due to the impact of XYZ.’

Pre-Tax Income: Year Plan vs. Actual



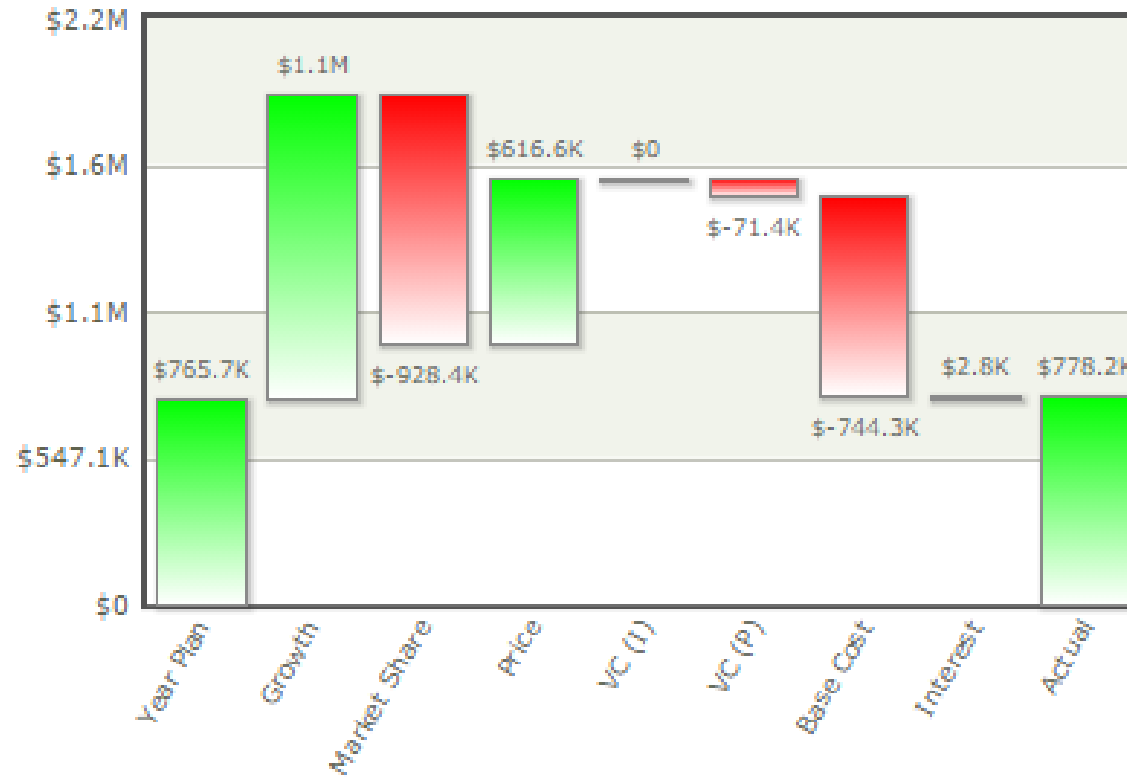
‘Base Cost’ is the sum of discretionary expenses. Because there are many costs that can contribute to this category, we would need to do some investigation to find out what specifically caused this large unfavorable variance. In some cases, there is good reason for this difference, such as funding a project that was not originally planned for. Underestimating Building Lease and Utilities is a common reason for a large negative variance here. Overall, it means we spent more in Base Costs than the Year Plan called for. Your explanation should include **specific** details about which costs impacted the results, and why. For example, ‘Base Cost shows an unfavorable variance to plan, primarily driven by investment in Project 1 of \$X, which was not in the Plan, and additional spending of \$Y in Engineering Quality, to improve reader quality.’

Pre-Tax Income: Year Plan vs. Actual



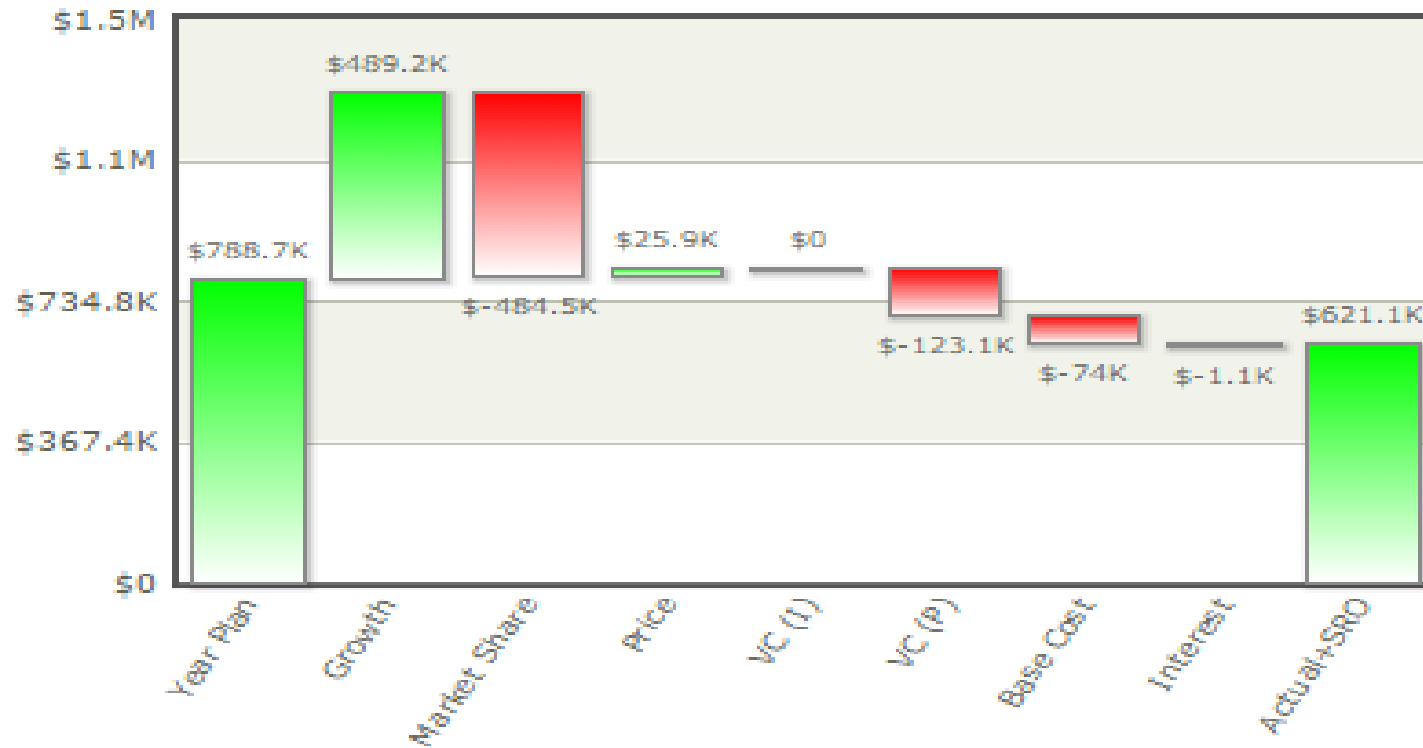
‘Interest’ is simply how much interest on our debt we planned on vs how much interest we actually paid. Here, we have a favorable \$2.8k, which means we spent less on interest than planned, which means we took on less debt than the original planned estimated. This favorable variance added \$2.8k – pre-tax – to our net income plan. Your explanation should include details about the variance. For example, ‘Interest was favorable to plan by \$2.8k (X%), due to less debt being used than Plan.’

Pre-Tax Income: Year Plan vs. Actual



In the QBR, you are asked ‘Using the ‘Pre-tax NI Walk: Plan vs. Actual’ chart, explain the key drivers of the variances that account for the difference in Plan to Actual.’ It is critical that you include data, numbers, and other measures to give your reader an idea of scope, and to support your explanations. Use of the correct terminology (favorable or unfavorable to plan) demonstrates comprehension of the impact of the drivers shown in the chart.

Pre-Tax Income: Year Plan vs. Actual+SRO



The difference between the 'Actual' and 'Actual + SRO' chart is that while the 'Actual' chart shows what has already happened, the 'Actual + SRO' chart (above) shows you what has happened so far, plus what will happen if you hit all future quarters EXACTLY as planned. Keep in mind that it is virtually impossible to come in exactly on target for all future quarters. This chart will help you determine what to consider as you make your decisions for future quarters. For example, if we are looking at the chart after Q2 decisions have been submitted, the 'Actual + SRO' includes Q1 Actuals, Q2 Actuals, Q3 SRO, and Q4 SRO. You will be able to add the Net Income from the Income Statement for all four quarters of the year and see that it ties to your after-tax Net Income. Here, on the Income Statement, we would see \$310.5k.