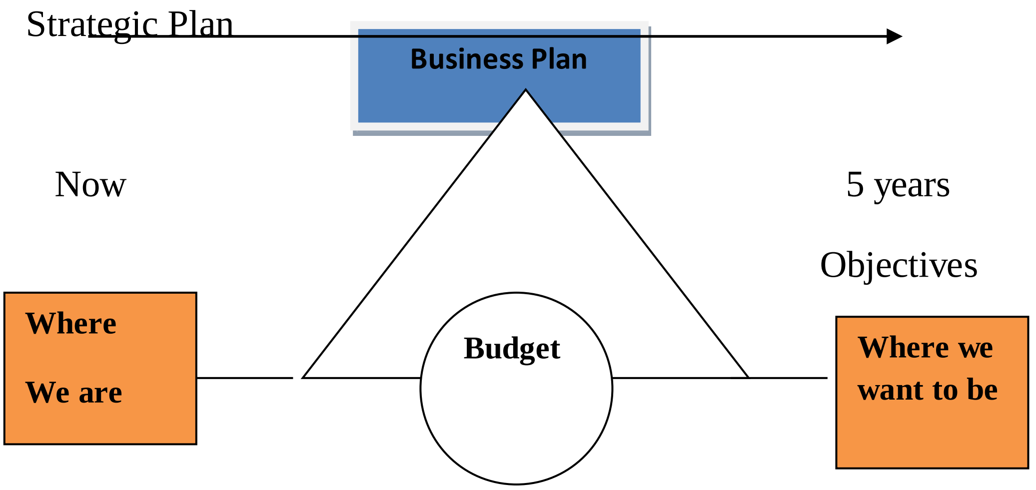
Budgeting

What is Budgeting?

Budgeting is the tactical implementation of a business plan. To achieve the goals in a business's strategic plan, we need a detailed descriptive roadmap of the business plan that sets measures and indicators of performance. We can then make changes along the way to ensure that we arrive at the desired goals.



Translating Strategy into Targets and Budgets

There are four dimensions to consider when translating high-level strategy, such as mission, vision, and goals, into budgets.

1. **Objectives** are basically your goals, e.g., increasing the amount each customer spends at your retail store.
2. Then, you develop one or more **strategies** to achieve your goals. The company can increase customer spending by expanding product offerings, sourcing new suppliers, promotion, etc.
3. You need to track and evaluate the effectiveness of the strategies, using relevant **measures**. For example, you can measure the average weekly spending per customer and average price changes as inputs.
4. Finally, you should set **targets** that you would like to reach by the end of a certain period. The targets should be quantifiable and time-based, such as an increase in the volume of sales or an increase in the number of products sold by a certain time.
5.

Objectives	strategies	measures	targets
What are you trying to achieve ?	How are you going to achieve it ?	What are the input and output measures ?	Quantifiable and time-based

•Increase spent per customer	•Expend product offerings •Source of new suppliers •Promotion and marketing •Pricing	•Average weekly spend/customer •Spend by product type •Average price changes	•$ increase •Volume increase •% staff trained in new products

Goals of the Budgeting Process

Budgeting is a critical process for any business in several ways.

1. Aids in the planning of actual operations

The process gets managers to consider how conditions may change and what steps they need to take, while also allowing managers to understand how to address problems when they arise.

2. Coordinates the activities of the organization

Budgeting encourages managers to build relationships with the other parts of the operation and understand how the various departments and teams interact with each other and how they all support the overall organization.

3. Communicating plans to various managers

Communicating plans to managers is an important social aspect of the process, which ensures that everyone gets a clear understanding of how they support the organization. It encourages communication of individual goals, plans, and initiatives, which all roll up together to support the growth of the business. It also ensures appropriate individuals are made accountable for implementing the budget.

4. Motivates managers to strive to achieve the budget goals

Budgeting gets managers to focus on participation in the budget process. It provides a challenge or target for individuals and managers by linking their compensation and performance relative to the budget.

5. Control activities

Managers can compare actual spending with the budget to control financial activities.

6. Evaluate the performance of managers

Budgeting provides a means of informing managers of how well they are performing in meeting targets they have set.

Types of Budgets

A robust budget framework is built around a master budget consisting of operating budgets, capital expenditure budgets, and cash budgets. The combined budgets generate a budgeted income statement, balance sheet, and cash flow statement.

1. Operating budget

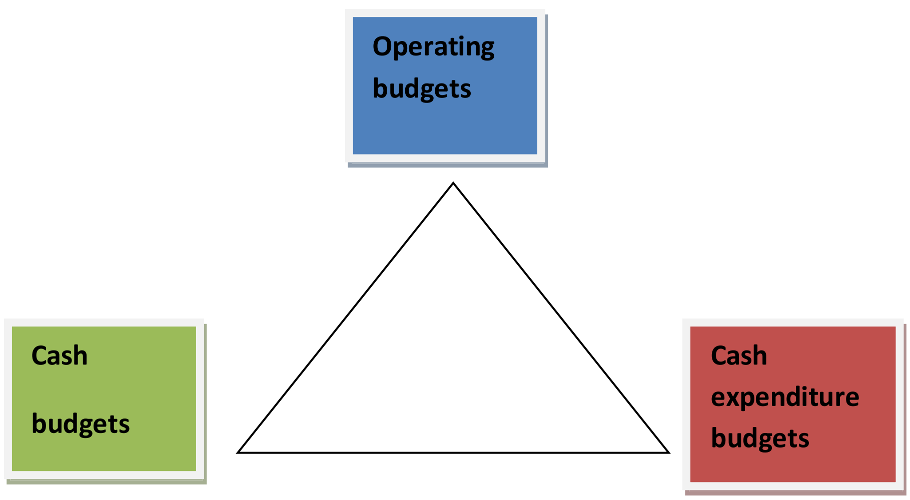
Revenues and associated expenses in day-to-day operations are budgeted in detail and are divided into major categories such as revenues, salaries, benefits, and non-salary expenses.

2. Capital budget

Capital budgets are typically requests for purchases of large assets such as property, equipment, or IT systems that create major demands on an organization's cash flow. The purposes of capital budgets are to allocate funds, control risks in decision-making, and set priorities.

3. Cash budget

Cash budgets tie the other two budgets together and take into account the timing of payments and the timing of receipt of cash from revenues. Cash budgets help management track and manage the company's cash flow effectively by assessing whether additional capital is required, whether the company needs to raise money, or if there is excess capital.



The Process

The budgeting process for most large companies usually begins four to six months before the start of the financial year, while some may take an entire fiscal year to complete. Most organizations set budgets and undertake variance analysis on a monthly basis.

Starting from the initial planning stage, the company goes through a series of stages to finally implement the budget. Common processes include communication within executive management, establishing objectives and targets, developing a detailed budget, compilation and revision of budget model, budget committee review, and approval.

Additional Resources

What is an Operating Budget?

An operating budget consists of all revenues and expenses over a period of time (typically a quarter or a year) that a corporation, government (see the U.S. 2017 Budget), or organization uses to plan its operations. An operating budget is prepared in advance of a reporting period as a goal or plan that the business expects to achieve. Below is an example of a downloadable budget template and an explanation of how to prepare one.**(see attached document**)

Projecting Balance Sheet Line Items

Projecting balance sheet line items is typically done in conjunction with projecting income statement line items. Both of these skills are necessary when mastering the art of financial modeling. This guide breaks down, step-by-step, how to calculate and then forecast each of the line items necessary to forecast a complete balance sheet and build a 3 statement financial model. **.(see attached document**

Additional Resources

CFI is a global provider of financial modeling courses and of the FMVA Certification. CFI's mission is to help all professionals improve their technical skills. If you are a student or looking for a career change, the CFI website has many free resources to help you jumpstart your Career in Finance. If you are seeking to improve your technical skills, check out some of our most popular courses. Below are some additional resources for you to further explore:

- Careers
- CFI's Most Popular Courses
- All CFI Resources
- Finance Terms

The Financial Modeling Certification

Accounting Crash Courses

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