The Value Of An (Updated) Budget: Getting Your Business on Track for Success

6 min read

Key Takeaways

- Budgeting Forecasting: Once you have a basic budget, use it to forecast best-case and worst-case scenarios for the upcoming financial period.
- Make Your Traditional P&L Actionable With a Budget: Compare your expectations with reality to determine whether your business's performance met, exceeded, or failed to meet the expectations outlined in your budget.
- How Budgeting Affects Employee Performance: The goals and plans outlined in a budget should be communicated throughout your company to employees at every level.

Is a budget useless? Unrealistic?

Rather than being a perfect prediction of the coming quarter or year, **a budget should act as a financial target or destination for your business.**

With a budget, you should strive to outline your expectations for your business's near future by combining your company's historic performance with reasonable growth goals and industry trends.

A budget should act like a roadmap or GPS designed to keep your business on course for meeting short-term benchmarks and achieving long-term goals. It's about clarity on your expectations of where you are operating financially.

So, you can see that budgeting is not a waste of time. Instead, it's an exercise in setting goals and mapping out an actionable plan to meet them.

How an Updated Budget Can Guide Your Business to Success

It's easy to get lost without a map. Taking the time to put together a thoughtful budget will mean that you know where your business is going and how you plan to get it there, financially speaking.

Where Are We Going? Achieve Your Budget Goals by Writing Them Down

Simply the act of generating a budget and some budgetary goals and writing them down will increase your chances of succeeding.

Writing goals stores them externally, meaning they exist somewhere outside of your brain. Writing down your goals also forces your brain (and your team members' brains) through the process of idea generation which increases thought analysis, comprehension, memory, and recall of your ideas or, in this case, your business goals. [1]

As a result, you'll have an improved collective memory of what you want to do, why you decided to do it, and how you plan to do it.

Map a New Course: Consider Zero-Based Budgeting

The traditional method of budgeting is historically based. In other words, you look at expenses, revenue, and profit from the previous year and base your goals for the upcoming year on those historic numbers by applying a rate of increase to past figures.

With zero-based budgeting, you do not automatically carry over any expenses or revenue from the previous period. Instead, you analyze each cost and each revenue stream individually, deciding whether the expense is necessary or whether you should anticipate the revenue stream continuing to produce going forward. Then determine whether or not the expense or revenue should be included in your budget.

Zero-based budgeting allows business owners to cut costs every time they map out a new budget while also ensuring budgeted revenue is realistic. Rather than automatically incurring expense growth year over year, zero-based budgeting helps rein in cost increases by considering each expense before going into a new financial year. It also helps business owners avoid overestimating budgeted revenue.

Anticipate Traffic Jams and Green Lights: Budget Forecasting

After budgeting comes budget forecasting.

This will help you be better prepared to handle economic downturns, unexpected challenges, or cash flow shortages while making the most of upturns, better-than-expected profits, or new opportunities.

Once you have a basic budget, use it to forecast best-case and worst-case scenarios for the upcoming financial period. Play around with a variety of "what if?" situations to develop contingency plans just in case things go worse than you think they will or better than you anticipate.

Remember that budget forecasting is not the same as cash flow forecasting. Budget forecasting analyzes costs, revenue, and profits – not cash flow. For comprehensive forecasting and contingency planning, business owners should look at a cash flow forecast along with a budget forecast.

> "My financials used to keep me up at night. I knew what my bank account said, but I didn't know how long that was going to last. **GrowthForce helped me understand how to build a budget and worked to teach me how to read and interpret my new reports**. I felt the fog lifting as they helped me be a stronger leader and, overall, a better business owner."
>
> *- Ryan Jennings, President, Sentinel Builders LLC. Read the full story on how this business went from Crisis Survival to Sustainable Growth 👉 Here.*

Take the Right Turns and Know When You've Arrived: Make Your Traditional P&L Actionable With a Budget

Actual financials don't mean much without a set of expectations to compare them to, and expectations are exactly what a budget provides. With a budget, you can compare your performance expectations with your business's actual performance over the previous period to analyze variances between your budget and actuals. These variances effectively transform a traditional profit and loss statement from mere information into actionable data.

Compare your expectations with reality to determine whether your business's performance met, exceeded, or failed to meet the expectations outlined in your budget. To identify business drivers and pull their levers to improve future performance, look for the following types of variances:

- Revenue
- Cost of Goods Sold
- Gross Profit
- Expense

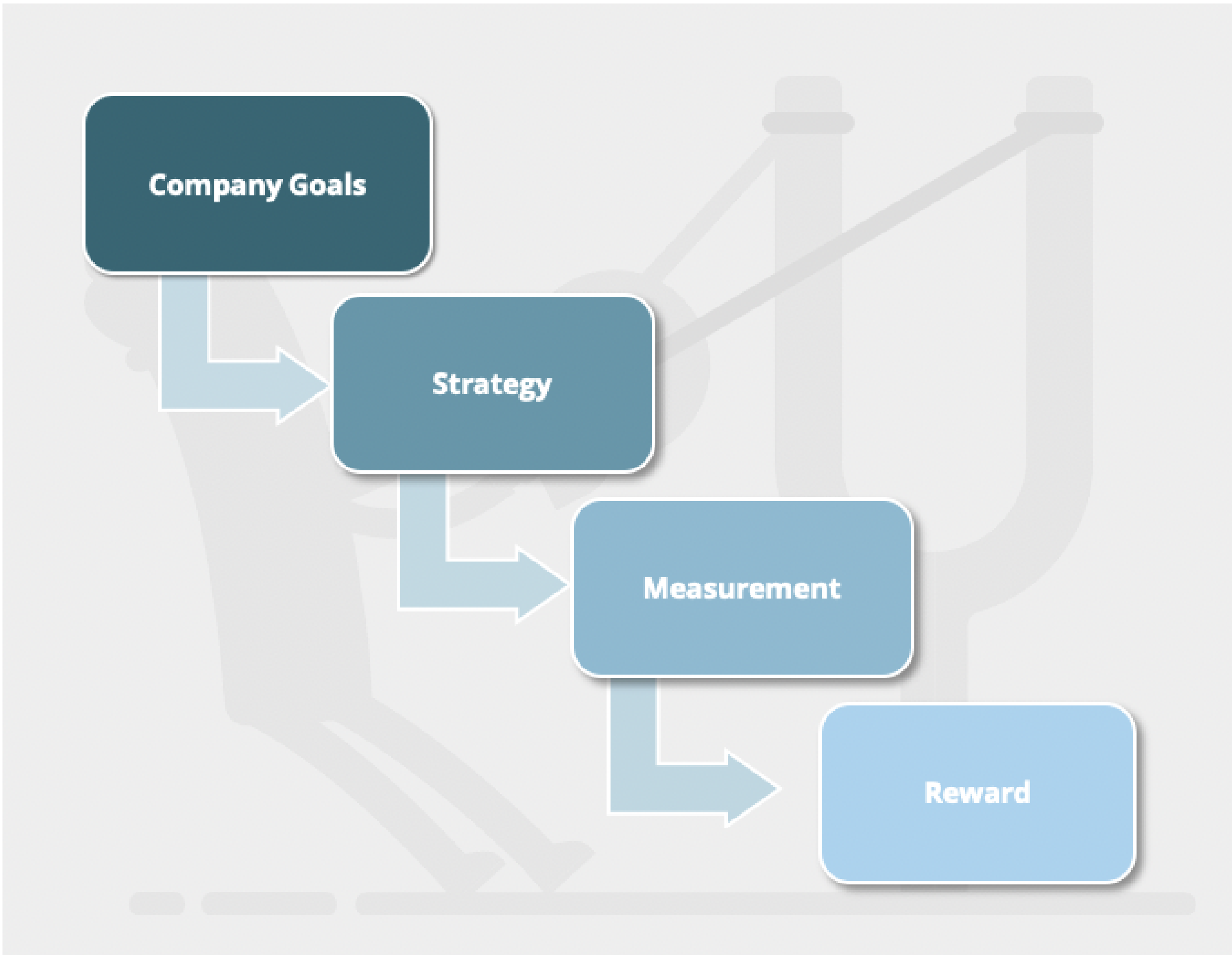
When assessing variances in these categories, consider why the numbers turned out differently than expected, determine whether the variance represents an ongoing trend or a one-time occurrence, and determine whether or not you need to take action (and what actions to take) to address the variances.

Focusing on variances will help you create a roadmap that guides your business decisions from start to finish. Budgeting and analyzing variances will enable you to outline your goals, identify the necessary work to reach them, and keep you on track for achieving the outcomes you desire.

Discretionary Effort: How Budgeting Affects Employee Performance

In addition to providing a road map for your business to achieve its goals, budgeting also has the power to improve employee performance by unifying your people around common goals and helping all the individual parts of your business work in the same direction.

This is where the concept of cascading goals comes in: allocating smaller, related objectives to departments, teams, and individuals that all work to achieve the overall operational objectives. Communicating each employee's direct role in and responsibility to the budget and the company's greater goals gives each person working in your company ownership of the business's success or failure. This personal responsibility, in turn, encourages discretionary effort.



[*Cascading goals are a crucial part of a lean business model and should be a focal point of your management strategy.*]

Neglecting to include all levels of employees in conversations about the business's budget and goals can diminish workplace morale, employee motivation, happiness, and productivity. According to a study reported by Harvard Business Review, simply looking at employee happiness and/or employee effort separately does not provide an adequate indication of overall employee engagement. [3]

According to the study, employee perceptions of the workplace and work directly affect employee engagement in addition to the individual's behavior or work ethic. For example, a high performer with a negative perception could be considered a martyr, while an all-star employee is both positive and hard working.

You can use your budget to increase employee engagement to improve perception and behavior overall. The goals and plans outlined in a budget should be communicated throughout your company to employees at every level.

Ensure that your department managers can adequately communicate the role each employee plays in helping the company achieve the goals outlined in the budget. Additionally, talk with your people about what the budget means in terms of the business's and your employees' bigger pictures. Encourage your employees by showing them how their work contributes to company growth, promotions, raises, expansion, and increased opportunities.

Get the Expertise to Get Your Budget Right

Budgeting with bad data is nearly impossible. It's important that your accounting system is designed to give you accurate data so your reports are as valuable as they should be.

With a professional's assistance, you can bridge the gap between the raw data and understanding what it means for your business. When you actually know your business's numbers, you're budgeting will be more reliable, and finally, start making confident data-driven decisions to lead your business in the direction of success.

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[1] https://www.forbes.com/sites/markmurphy/2018/04/15/neuroscience-explains-why-you-need-to-write-down-your-goals-if-you-actually-want-to-achieve-them/?sh=63c93f4a7905

[2] https://www.wanderlustworker.com/the-harvard-mba-business-school-study-on-goal-setting

[3] https://hbr.org/2015/12/the-two-sides-of-employee-engagement