Budgeting

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Budgeting Introduction

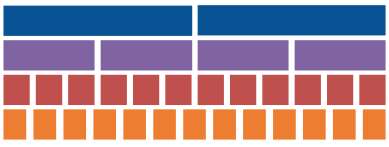
What is it?

"A financial or quantitative plan of operations for a forthcoming period"

How is it done?

Spending plans are drawn up for the accounting year and usually split into control periods, which could be:

- 2 x 6 month periods
- 4 x quarterly periods
- 12 x monthly periods
- 13 x 4 week periods



Why is it done?

- Planning
- Control

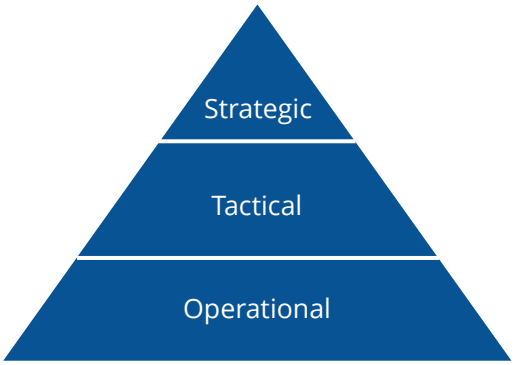
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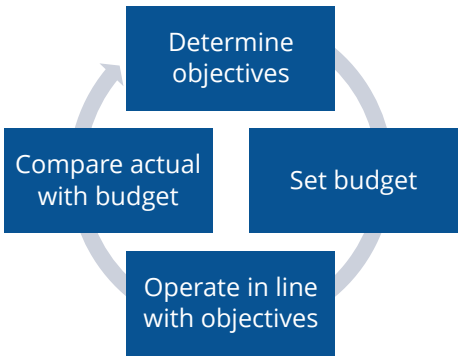
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Budgeting Objectives: Planning and Control

Planning takes place at different levels within a firm, leading to many budgets



Budgetary control keeps a system working steadily or enables it to change safely

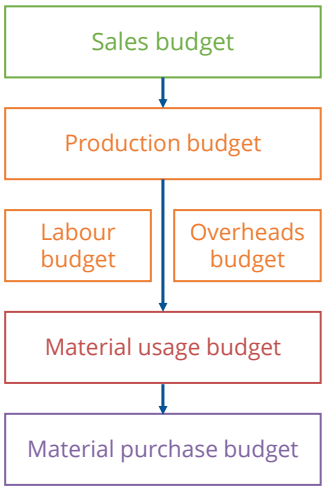


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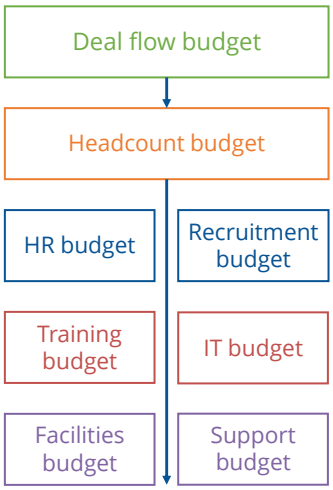
Interlinking of Budgets

Budget committee(s) coordinate the preparation and administration of budgets



Manufacturer

Investment bank



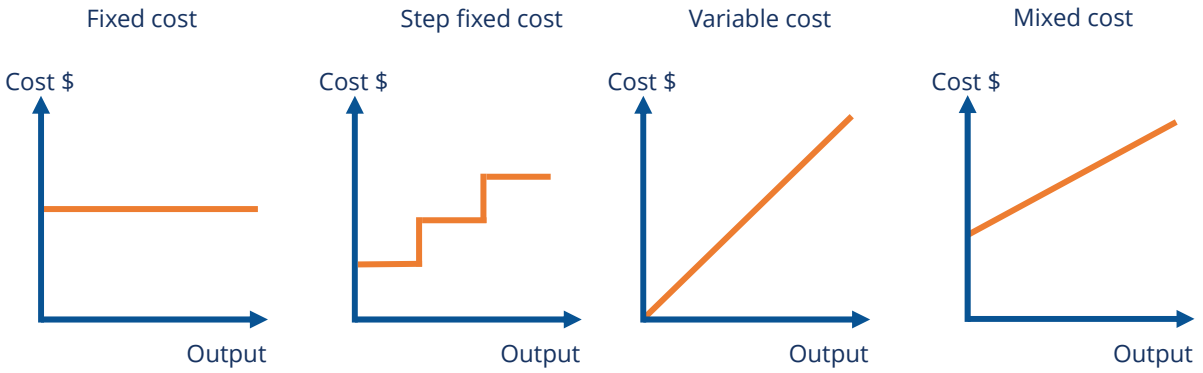
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Cost Behavior: Variable and Fixed Costs

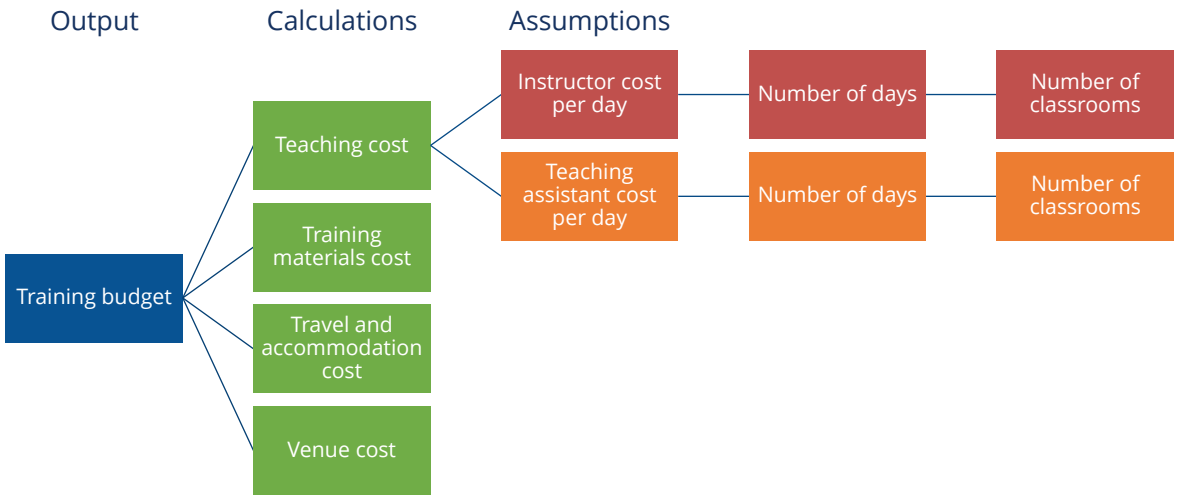
Companies needs to know how costs behave as activity changes
It is expected that costs increase as output increases, but different costs behave differently



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Identifying Costs for a Budget - Training

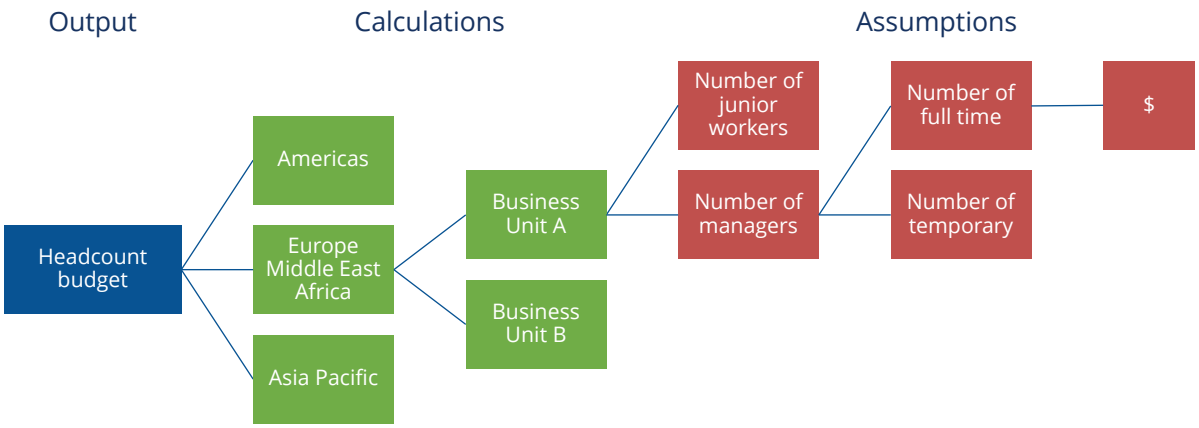


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Identifying Costs for a Budget – Headcount



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Flexible Budgets and Variances

The flexible budget is designed to change as volume of activity changes
It can also aid planning by taking into account different scenarios

Estimated employees

Updated for actual employees

	Original budget	Flexed budget
Number of new employees	100.0	105.0
Recruitment cost per employee	6.0	6.0
Training cost per employee	5.0	5.0
New employee cost	1,100.0	1,155.0

Budgeted "standard costs" remain in the flexed budget

More meaningful budget cost

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Flexible Budgets and Variances

Variances explain the difference between actual and expected results, and provide information for control purposes

Variances can be favorable or adverse

Meaningful variance
Favorable

	Original budget	Flexed budget	Actual figures
Number of new employees	100.0	105.0	105.0
Recruitment cost per employee	6.0	6.0	6.1
Training cost per employee	5.0	5.0	4.8
New employee cost	1,100.0	1,155.0	1,144.5

Meaningless comparison

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Budgeting vs Forecasting

A budget is what a company wants to achieve
A forecast is what a company thinks it will actually achieve

	Jan	Feb	Mar	Apr	May	Jun	Total
Budget	10.0	10.0	10.0	10.0	10.0	10.0	60.0
Actual and Forecast	**9.0**	**10.0**	9.5	9.5	9.5	9.5	57.0

Actual figures

Forecast figures

The budget is not changed, otherwise the budget provides no control
Instead the forecast is updated

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