

# Budgets

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**CALDWELL PENN**  
chartered accountants • chartered tax advisers

# Overview

Whether you are a start-up or an established business, preparing and keeping on top of a business budget is essential if you want to maximise profits.

Not sure where to start? No problem, we are here to help, and we are confident that this guide will provide you with all the tools you need to get up and running.

Prefer to leave it to the experts? Great! Get in touch for a free 15-minute consultation with one of our in-house management accountants today.

## What you need to know

### What is a budget?

A budget is an estimate of your income and expenditure over a set period of time which takes into consideration your long-term financial goals and future predicted transactions to allow you to create a plan to spend your money.

Creating this spending plan allows you to determine in advance whether you will have enough money for future spending. If money is tight, then you can use this planning process to prioritise your spending and focus your money on the things that are most important to you.

As time passes, you can then go back and compare your plan with your actuals and see how your business performed. Ultimately, a budget can provide you with the tools to make better, faster, and more informed business decisions.

### Why is it important to prepare a budget?

Following a budget will help you to improve your profit margins or help work your way out of debt.

Put simply, a well thought out budget can provide you with many benefits:

### The benefits

1. Provides you visibility on how your business is performing
2. Make sound, thought out business decisions
3. Helps shed light on bad spending habits
4. Identifies areas for growth and improvement
5. Helps you to achieve your financial goals

### What makes a good budget?

The best budgets are both simple and flexible.

Things change, that is a certainty. If your budget isn't simple and flexible, then when change inevitably happens, your budget won't be able to flex to give you a clear picture of where you now stand.

We suggest aligning your budget to your accounting software and/or year end financial statements. This helps to keep things simple and smooth the process of tracking your budget against actual results.

## Contact Us

For the latest news and advice please visit our Facebook, LinkedIn and website pages. If you have any immediate questions or if you would like to discuss anything further please contact us via email or give us a call on:

**01483 898 400**



# 5 Step Process

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How to prepare a budget

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# 1. Time frame

First, you need to discover your time frame. Now this is essential and will be bespoke to you, depending largely on the needs of your business and how often you want to track your actuals against your budget.

The most common time frames are:

- Monthly
- Quarterly
- Six monthly
- Annually

**TIP:** Where possible, we recommend against budgeting beyond one year (at least at first), as assumptions, no matter how well thought out, inevitably become less reliable the further into the future you look.



## 2. Preparation

Now it is time to prepare your budget (see last page for example). This is a two-step process, which goes as follows:

### (a) Determine your income

When building a budget, you need to figure out how much revenue your business is going to make in the year (exclusive of VAT) and where that revenue is coming from e.g. products or consultancy services.

Start with your actual revenue from your previous year results using accounting software and split this by revenue sources. If this varies, focus on the historical and seasonal patterns of your business.

Now factor in your expectations for additional revenue (prospect clients, average growth) and include this into your budget revenue.

### (b) Calculate your expenditure

Once you have determined your revenue, it's time to get a handle of your costs.

Review your accounting software and list your monthly expenditure by summarised headings (rent, light and heat, computer expenses). Remember, some expenses may not bill monthly when preparing a monthly budget.

You will need to consider both fixed and variable expenses.

You will have no problem budgeting for fixed expenditure, just process these based on historic actuals and take into consideration your maximum capacity i.e. for rent, how long you can use your warehouse or office space before you need to up-size?

You will need to focus on the impact growth may have on your business for variable expenditure e.g. an increase in revenue will inevitably mean an increase in cost of sales. Just like with revenue, you will need to factor in your historical and seasonal patterns to produce reliable estimates.

$$\begin{array}{c} \text{Historic revenue} \\ + \\ \text{Expected/desired} \\ \text{revenue increase/decrease} \\ = \\ \text{Budget income} \end{array}$$

$$\begin{array}{c} \text{Historic expenditure} \\ + \\ \text{Expected/predicted} \\ \text{expenditure increase/decrease} \\ = \\ \text{Budget expenditure} \end{array}$$

**TIP:** If you are just starting your business and don't have any financial data to review, make sure to use projected costs. For example, if you have signed a lease for office space, use the monthly rent you will pay moving forward.

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## 3. Insight

Now you have prepared your budget, you can now review the difference between your expected income and budgeted expenses – we call this Insight.

You will have one of two outcomes:

### (a) Your revenues exceed your expenses

If your revenues are more than you are spending, that's great. Are you happy with the amount of profit? If not, what unnecessary expenses can be eliminated or cut back? How can you look to expand your revenues?

### (b) Your expenses are greater than your revenues

If this is the case you have 2 options - either make more money, or spend less.

Generally, it's easier to reduce spending versus making more money. Look back at your budget and determine what can be reduced. Spending too much on entertaining? Office larger than you need? Unnecessary subscriptions?



## 4. Tracking

Now you have prepared your budget and considered your actionable changes (Insight), it's time to compare these against your actuals – we call this stage Tracking.

First, record your business' actual income and expenses during the budget period on your accounting software. Now calculate the difference between your budgeted amounts and your actual results.

Armed with Tracking, you can now track how you are spending your money, what needs to change, and if you're sticking to your financial goals.

**TIP:** Ask yourself these key questions:

- How did I get on?
- Was I too optimistic or did I miss any significant expenses?
- Am I on track to meet my financial objectives and what can you do better next time to produce a more accurate budget and improve my results?

## 5. Habit

Aim to track your actual results against your budget at least every quarter, this will help you to create a Habit.

Putting in the work to create your budget may seem like a hassle, but whilst it takes a bit of time and energy, it's worth the extra effort. Thorough business budgeting gives you the financial insights you need to make the right decisions for your business to grow, scale, and prosper in the future.



# Budget example

Below is a very simple example of what a budget will look like and how the first 4 steps of the 5 step process are used to create a budget.

## 1. Time Frame

Monthly, quarterly, annually?



### ANNUAL BUDGET

#### Sales

Consultancy	£200,000	£220,000	£190,000	£30,000
Product	£450,000	£495,000	£522,000	£27,000

#### Cost of sales

Direct costs	£60,000	£66,000	£69,600	£3,600
Direct wages	£100,000	£110,000	£116,000	£6,000

#### Overheads

Rent	£50,000	£50,000	£50,000	£0
Light & heat	£5,000	£5,500	£5,300	£200
Computer expenses	£2,500	£1,500	£1,800	£300
Accountancy	£2,700	£2,700	£2,700	£0
Telephone	£600	£610	£630	£20

<b>Profit</b>	<b>£429,200</b>	<b>£478,690</b>	<b>£465,970</b>	<b>£12,720</b>
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## 2. Preparation

Determine your current year budgeted revenue and expenditure using your prior year actual results as a start and then take into consideration any expected/desired/predicted increases and decreases.



## 3. Insight

Review your current year budget. Are you making a profit? Do any of the budgeted figures need adjusting?



## 4. Tracking

Compare your budget to your current year results. How did you do? Where can you improve?



