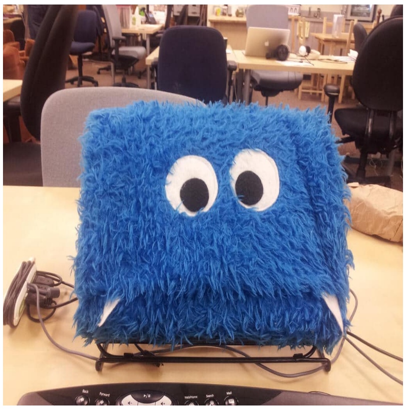

Fix Budget Variances in 5 steps

Description

"Oh No – it doesn't look like I thought it would!!!"

Don't Panic
follow these 5 steps to fix budget variances!

You built a budget, and took the time to get your actuals entered.- Now you can see there are differences between the two…

How to fix budget variances?Â …. Don't just stare at your Budget forlornly!

Tackle your Budget by working out exactly Where the problem is – then you can work out What, When, Why, and How to get all the information you need to deal with it.

Tip 1. WHERE are the Variances showing?

First identify which line items are out of whack, and then we can drill down further, this can be done simply by running your finger down your report and highlighting the areas that are different from what you expect.

Are there issues with Revenue are the issues with Costs, or is it the totals that have gone awry?

Establishing where there is a variance is important and reviewing what has happened against both what you were hoping for, and what you have done before helps examine how your business is tracking and how accurate your planning is.

A. Specific variances – actual figures v expected figures – this includes

- Actual v budget
- Actual v Forecast

It is unlikely that you will be perfect at budgeting (unless you have a crystal ball), so you are bound to get variances at least occasionally. Generally, small variances are simply part of doing business, large variances need investigating – but don't get complacent; think of it like testing for lumps, or checking moles â?? you need to get a foundation of what is NORMALLY a bit over or a bit under before you can understand WHAT IS ODDâ?¦ and this only comes with practice.

B. Trend variances – small, continual changes over time, that incrementally diverge from expected.

- this month's v last month's
- August 2020 v August 2021 – both acutals and budgets

What can seem normal, can seem so because we are used to it. Trend analysis is a bit like watching your weight; when you check your scales each day, it only seems like tiny changes, but if you look at this birthday compared to your weight last birthday that is when you notice the few extra kilos have snuck on … Trend analysis puts a spotlight on the changes that creep up on us little by little.

Tip 2. WHAT kind of Budget Variance do you have?

A very Key Point to consider here: – not all variances are bad things *some can actually be good*.

The trick at this point, is that for budgeting purposes it is important to consider the budget variance in terms of how it has impacted profits:

1. POSITIVE VARIANCES/IMPACTS â?? anything that boosts profits

- Better than expected result
- Costs lower than expected
- Revenue higher than expected

2. NEGATIVE VARIANCES/IMPACTS – anything that reduces profit

- Worse than expected result
- Costs higher than expected
- Revenue lower than expected

i.e. you always want to be INCREASING your Revenue and DECREASING your expenses (this may sound like telling you to 'suck eggs' – but it is the key goal to keep in mind when looking at a your reports; don't let the fact you are looking at numbers overwhelm you, remember there are facts and activities behind the numbers that are trying to tell you their story)

NOTE: this step can be VERY confusing if you simply think of negative numbers as bad and positive numbers as good – especially as different reports will set things out in different ways and it can be easy to get caught-out. So to fix budget variances stick to the above guidelines to first stop and check if a variance is good or bad so that you ensure you always:

1. take action when you need to
2. don't worry unnecessarily

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Tip 3. WHEN is there a difference?

Sometimes differences arise simply because of a lack of information entered into your systems.
What typically happens is that a relevant invoice has not yet been received or a payment relating to this period was made in an earlier period. In either case variances will arise in both the month the invoice was expected and not received, and the later month when the invoice is entered but not expected.
The idea of ‘Accrual accounting’ is to recognise all the income and outgoings for the period in that same period, irrespective of whether or not cash has actually passed between customer and supplier.
Timing variances “reverse” because what was short this period will appear in the next, or what was extra in this period will be missing next period. i.e. when the two months are added together, you end up in the right spot overall. As long as they are explainable as “reversing” in the next period, other than ensuring the expected reversal takes place then no further action need be taken.

Tip 4. WHY is there a difference?

The most powerful question you have at your disposal is **WHY did this variance occur?**. The difference could simply have arisen because of a data entry typo â?? donâ??t panic or go yelling and the wrong people for the wrong things! Begin by making sure what you are looking at is accurate.
In all other cases a Budget Variance is the result of either:

* A price that was different from expected/budgeted
OR

* A volume (amount) that was different from expected/budgeted

To be able to take any corrective action you must work out which element, or both, are involvedâ?¦
TRICK: Ask “WHY” more than once, it can take up to seven times of asking WHY to drill down to the real cause that needs to be addressed – stopping too soon may mean you don’t get to the bottom of the issue and this will mean that any changes you try to make will be targeting an incorrect area. This part requires quite a bit of patience from both the questioner and the answerer, a bit of lateral thinking and investigation, and also an understanding that “I don’t know” simply means more research is needed.

Tip 5. How to fix budget variances? – Take Action

So once the root cause of each variance is understood the final step is to take action – Reports should drive profitable decisions and variance analysis is no different.
What you need to do will be guided by the Where, When and Why of each variance. In some cases, especially with trend variances, no action needs to be taken until a pre-determined ‘tipping point’ is reached.

Some things to consider include:

- BUDGET – Do you need to adjust your projections because your budget was overly optimistic?
- REVENUE – Do you need to change your prices, volumes or sales process?
- CUSTOMERS – Do you need to increase your marketing, change product mix, focus on quality?
- WASTAGE – Do you need to adjust your processes to make them more efficient and effective?

The value of variance analysis lies in your ability to isolate changes and take remedial action quickly. Every business report exists to help you make better decisions; your budget is no different – if your business is not working as planned analysing your budget acts as a window enabling you to see what is going on and take the appropriate actions.

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