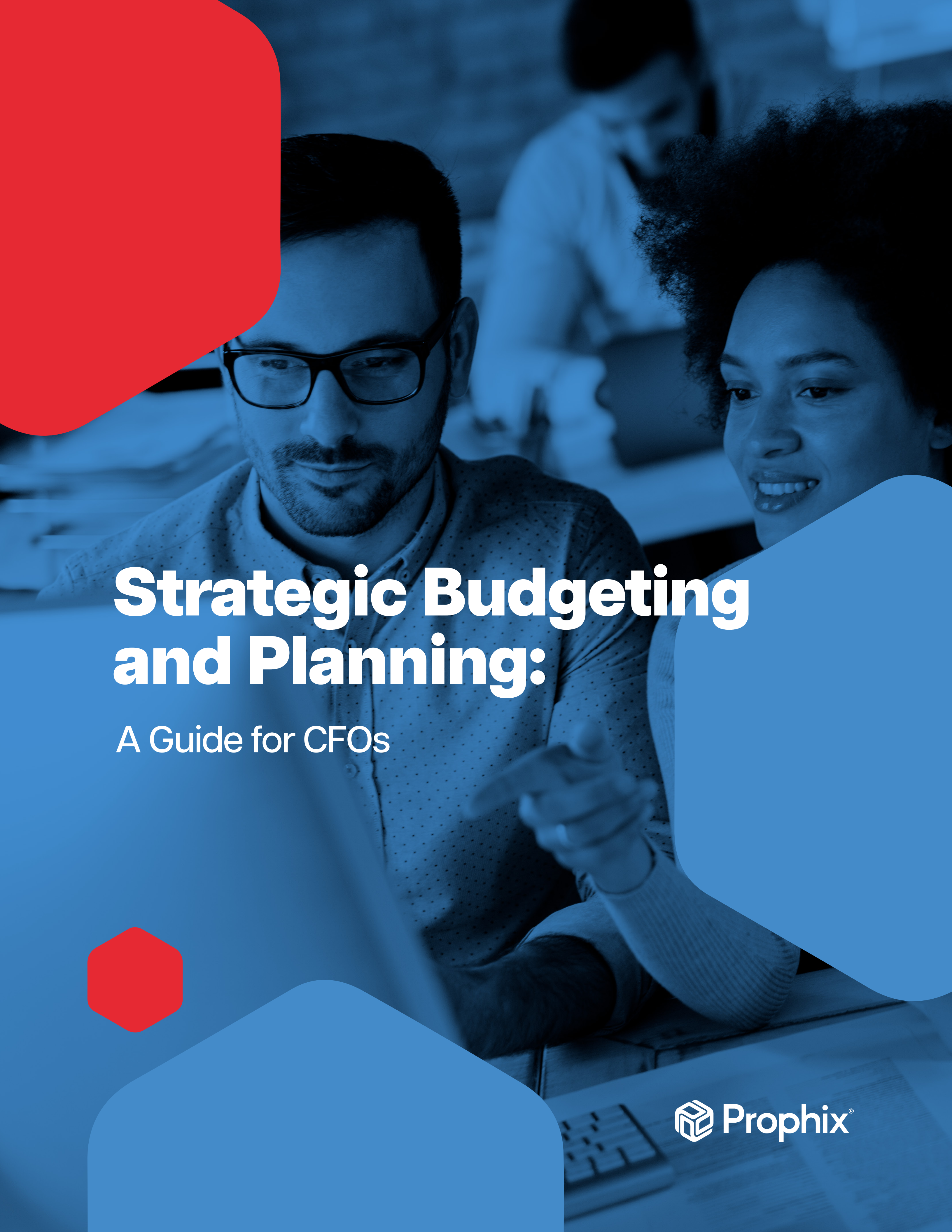

Strategic Budgeting and Planning:

A Guide for CFOs

Prophix

Introduction

Businesses are merging and growing at an unprecedented rate. This accelerated approach to digital transformation has highlighted the weaknesses of traditional budgeting and planning tools. Generic tools like Excel, that are prone to human error and don't foster collaboration, have proved themselves limited in their 'what if' scenario modeling capabilities.

And yet, good planning and budgeting depend hugely on creativity, collaboration, and quality of information.

If a focus on digital transformation has proven anything, it's that companies with the best data-driven, systemic approaches are the most adaptable, allowing the CFO and finance team to quickly identify and alert senior management to emerging opportunities.

This guide addresses these issues:

1. Exploring the strategic importance of budgeting and planning, giving examples of the different types of strategic budgeting.
2. Looking at the relationship between budgeting, strategic planning, and operational planning.
3. Providing a deeper understanding of the processes and platforms available.
4. Giving tips on improving processes.

How can budgeting help CFOs improve corporate strategy?

Executives these days are looking for CFOs to play a more strategic role. As leaders of the finance team, CFOs who rely on Excel are limiting their strategic capabilities by virtue of Excel's limited scope and accessibility, which in turn diminishes their value and risks them being perceived as mere number crunchers.

While a brilliant basic tool that has come a long way, Excel still falls rather short in the face of other options available today. Financial performance platforms facilitate all of these, allowing companies to manage finances better and act faster, moving forward to success and transformation quicker.

A budget is a vital tool for guiding strategy. Because CFOs have the data and insight into which initiatives create value, they can take on a more prominent role in guiding corporate strategy and, when supported by the right technology, can accurately forecast data and demonstrate potential ROI for countless projects.

Not analyzing a budget in a broader context can lead to companies missing out on opportunities for potential growth and even business transformation. This is why CFOs are crucial to companies in effectively strategizing within their means. They can spearhead a budgeting and planning transformation by challenging the status quo, setting targets for continual improvement, placing performance targets at the forefront of the budget, and using scenarios to time and size potential shifts.

What is strategic budgeting?

Somewhat self-explanatory, strategic budgeting accounts for long-term objectives and costs. The process includes preparing various budgets and forecasts for short-term expenses that align with the long-term goal. Once a strategic budget is set, a company can allocate specific funds to various activities.

A long-term strategic plan generally spans five years, broken down into single-year objectives. Strategic budgeting applies financial values to each of the activities listed in the long-term strategic plan and demonstrates that the company is focused on growth within its means. Informed budgeting is crucial to successfully using funds, and executing projects and goals.

Why budgets are important to strategic planning

While it is not vital to include a budget when creating a strategic plan, doing so provides a realistic financial scope for what a company can achieve.

Activities and spending must be in sync, otherwise valuable resources risk being wasted on short-term projects that don't contribute to long-term goals. Integrating the budget and strategic plan also makes it possible to modify both at the same time.

To boil it down to three key elements, strategic budgeting:

1. Allows a company to draw a goal map
2. Makes decision-making credible
3. Fits into formulating activities

What is the relationship between budgeting, strategic planning, and operational planning?

Planning is often the first step a company takes. Strategic planning is **what** the business hopes to achieve, and operational planning is **how** the business will achieve it.

A company outlines its goals and brainstorms ways to meet expectations. Once the plan is mapped out, the company budgets around the projects.

The budget allocates funds to projects on a monthly or quarterly basis and accounts for future revenue and expenses.

Companies will often revisit the budget every year to ensure they are on track and make alterations as necessary.

Examples of strategic budgeting

Strategic budgeting for product development

Planning for the development and launch of a specific product often includes research, design, and a rollout strategy. Including a long-term strategic budget allows companies to allocate their funds to the product accurately.

Strategic budgeting for company programs

This generally consists of a set number of short-term events that contribute to a long-term goal. Strategic budgeting provides an overview of which programs need what level of funding, allowing a company to avoid overspending or underspending, and to ensure it contributes successfully to the company's end goal.

Strategic budgeting for infrastructure

Companies that develop buildings, organizations, or cities require a plan that includes the budget. Large scale projects like railways, highways, or skyscrapers take several years to design and build, so having a budget in place is vital for accurate planning.

Strategic budgeting for productivity and capability

A five-year budget and plan created now can change drastically if a revolutionary technological advancement comes out in year three. With a strategic budget already in place, a company can easily adapt or revamp its plan based on the data gathered in the first three years of the initial plan.

Strategic budgeting methods

CFOs widely adopt one of four of the following budgeting methods:

Incremental budgeting

One of the most common budgeting methods due to its simplicity, incremental budgets account for a company's actual figures from the previous year and calculates the current year's budget by adding or subtracting a percentage from the figures. Incremental budgeting is ideal for companies whose primary cost drivers don't vary greatly year to year.

There are numerous drawbacks with this method. For one thing, it is a more inward-looking method that focuses on company performance, ignoring external drivers of activity and performance such as inflation. It can also promote inefficiencies and short-sighted solutions, in particular unnecessary spending. If a budget is increased by a certain percentage every year, that money will simply be spent with a view to maintaining the increase year on year, regardless of how it's spent. Incremental budgets are therefore only best placed if a company takes a strategic approach to using the extra money in the budget.

Activity-based budgeting

This is a top-down approach that allows a company's strategic plans to influence the budget by calculating the financing needed to support a target or output goal. For instance, if a company sets an output objective of $100 million, the management team then decides what steps are necessary to achieve the goals and how much each activity will cost. The projected cost of activities determines the budget.

Value proposition budgeting

This method ensures that every cost listed in the budget adds value to the company, asking questions such as:

- Why is this amount used?
- Who does it create value for – customers, staff, or stakeholders?
- Does its value outweigh its cost? If not, is it justified?

The goal of value proposition budgeting is to eliminate unnecessary expenditure and increase a company's ROI.

Zero-based budgeting

This is a bottom-up approach that assumes the budget resets to zero every year, starting from scratch and justifying every cost. These budgets are very tight and do not allow for extraneous spending. It is a common method because it avoids all expenses that aren't considered necessary to a company's profitable operation.

Even if finance teams don't use zero-based budgeting year to year, it can be a useful temporary measure when belts need to be tightened quickly, such as during financial restructuring or a widespread economic downturn. Zero-based budgeting primarily focuses on addressing discretionary costs rather than fundamental operating expenses. Although the process is time-consuming and detail-oriented, it offers the best option for conserving funds.

The strategic budgeting process

The process for strategic budgeting follows four stages:

Objectives

Defining what to achieve for a specific project or program, or for the company as a whole. A company can have an overarching goal list that is broken down into smaller objectives for each department.

Goals should be specific, quantifiable, and measurable, so a company can track the progress and effectiveness of its plan. Most companies establish five to seven objectives.

Strategy

Developing a strategy to reach the set goals, while also determining the importance of each part of the plan and defining who does what.

Outlining how often to measure growth, e.g. using a monthly conversion rate percentage for the goal of increasing customer engagement.

Putting safety measures into place for unexpected variables or risks.

Once the plan is complete and budgets are allocated to each project, all company departments should review it. When everyone is satisfied, implementation can begin.

Measures

Strategy implementation and progress tracking. The relevant departments collect, compile, and analyze all the relevant data to assess the plan’s effectiveness.

Four measurable performance dimensions include financial performance, internal business processes, customer relations, and organizational learning and growth. Each category has its own list of indicators ranging from ROI to length of operating cycle to customer complaints to employee motivation.

Targets

Evaluating whether goals have been reached on time. The compiled data is assessed to evaluate which aspects of the plan have worked and what needs improvement. If a company is doing a routine check-up on the plan, it can make alterations moving forward. If observing the data at the end of the budgetary period, the information can be used to set new goals and create a new plan.

The strategic budgeting process

In five steps, companies can make a strategic budget that informs the business' long-term strategy and helps make better business decisions.

Eliminate budget and strategy silos

Combining budget and strategy instead of keeping them separate allows companies to see the bigger picture, encourages more conservative spending, and facilitates quicker decision-making.

The most efficient way to combine budgeting and strategy is to automate processes. An integrated platform that caters to every use and user provides real-time data for more accurate decision-making.

Create a clear process and workflow

Automation platforms or budgeting technology create transparency in processes and workflow, ensuring that everyone easily understands their responsibilities and deadlines.

They also give CFOs and budget supervisors visibility on how many contributors are working, how many have submitted their data, and who needs assistance. The system further allows them to accept or reject submissions or make edits.

Businesses with multiple locations or subsidiaries need a cloud-based or hybrid solution that automatically integrates contributors' inputs, no matter where they are.

Draft the budget

With the strategy in mind, the company can begin drafting the budget with driver-based metrics and prior financial data. Driver-based metrics allow companies to focus on areas that improve business performance. Companies can use whichever budgeting method they prefer but should focus on aligning the values with their goals.

As the CFO or budget supervisor drafts the budget, they should consider their team's inputs and feedback, so as to attach a narrative to each number. At the same time, it's essential to find a balance between necessary details and detail overload.

Additionally, it can be beneficial to consider non-financial data when developing the budget. Items such as efficiency metrics, customer retention rates, customer conversion rates, employee productivity rates, customer support tickets, the average time to hire, and more, can help executives craft more constructive budgets.

Test scenarios and simulations

Once the numbers are in place, the company can use its finance platform to run tests to see how their budget would play out in various scenarios. Depending on the results, managers can make adjustments or create backup plans.

Reforecast throughout the year

Although companies create their budget for a year, a finance platform can help teams run analytics to reforecast and make monthly adjustments to the budget as needed. At the end of the year, a finance platform automatically compiles the data from the previous year, so the process can begin all over again.

Platforms and tools

Budgeting, planning, and forecasting platforms consolidate and centralize a company's financial information. In some cases, it can automate the budgeting process or simply provide a clearer picture of what the finance team has to work with. Strategic platforms can be purchased independently or as an integrated part of a financial performance management system.

A finance performance platform supports finance managers by giving them the tools to streamline the processes of accurate budgeting and what-if scenario analysis. Since success relies on being able to accurately guess (or adapt to) what will happen tomorrow, a finance platform can make it easier for IT, operations, logistics, and business managers to make accurate predictions.

How can technology help improve budgeting?

Technology can streamline the strategizing process by acting as a central database for all information. Using a tool saves precious time and effort that can otherwise be spent on executing the plan.

Technology also makes it possible to obtain automatic import and processing of information from this centralized database. Users can manage multiple versions and make immediate decisions that align with the company's long-term strategy.

Using technology also optimizes a company's workflow with more cross-functional collaboration and a multitude of possible interactions between users. Everyone has access to the same data in real-time, promoting inter-departmental collaboration.

What to look for in a budgeting and planning platform

One major tip here is to get a platform that goes beyond simply budgeting and planning. Invest in a platform that streamlines entire processes, which can help your company run seamlessly.

A few useful questions to ask about your potential platform:

Speed

Will the platform speed up the budgeting process by removing complications? Does it provide data in real-time to effectively track strategic objectives? Can it perform simulations, make scenario calculations while taking exchange rates into account, create different versions of the plan, and define criteria to measure the strategy's effectiveness?

Centralization

Does the platform provide consistent and unified operational and financial data in one place? Can it standardize import formats and data aggregation, automatically report transmission and allocate criteria, and present flash forecast calculations based on actual and budget numbers?

Multi-approach

Does the platform offer several approaches to budget creation based on a company's specific needs and entity profiles? Can it create budgets with top-down/bottom-up/activity-based approaches?

Cloud vs. on-site vs. hybrid

Is the platform strictly cloud-based or location-based? Does it offer a hybrid model with a central drive located at company HQ and the cloud, making the data accessible by employees anywhere?

Transversal

Can the platform fully integrate all company data while remaining accessible and easy to understand? Does it offer a multi-dimensional and detailed view of company activities and several display options based on allocation criteria? Does it provide easy dashboard functionality to facilitate data interpretation and automatic forwarding of customized reports based on user profiles? Does it allow for the management of several projects, including each project's assumptions, implications, profitability, management analysis, and reporting?

About Prophix

Your business is evolving. And the way you plan your business activities and report on them should evolve too. To empower mid-market companies to achieve their goals, Prophix provides an integrated, cloud-based platform to the Office of Finance; one that delivers planning, budgeting, reporting, forecasting and consolidation solutions. With Prophix, finance leaders improve profitability and minimize risk and puts the focus back on what matters most – uncovering business opportunities. Prophix supports your future with AI innovations that adapts to meet your strategic realities, today and tomorrow. Over 2,500 active customers around the globe rely on Prophix to transform the way they work.

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