FUTURE BUSINESS LEADERS OF AMERICA
CALIFORNIA
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Budgets

What is a Budget?

Budgeting is a process. This means budgeting is a number of activities performed in order to prepare a budget. A budget is a quantitative plan used as a tool for deciding which activities will be chosen for a future time period.

A budget is an itemized summary of likely income and expenses for a given period.

Creating this spending plan allows you to determine in advance whether you will have enough money to do the things you need to do or would like to do. It helps you determine whether you can grab that bite to eat or should head home for a bowl of soup.

It is typically created using a spreadsheet, and it provides a concrete, organized, and easily understood breakdown of how much money you have coming in and how much you are letting go.

It's an invaluable tool to help you prioritize your spending and manage your money—no matter how much or how little you have.

Annual Budget

- Annual budget is any budget that is prepared for a 12-month period.
- An annual budget outlines both the income and expenditures that are expected to be received and paid over the coming year.
- Annual budgets are used by individuals, corporations, governments and various other types of organizations.
- Annual budgets can apply to either a fiscal or calendar year.
- These budgets help their creators to plan for the upcoming year and make the necessary adjustments in cash flow to cover expenses.
- Annual budgets help both individuals and organizations to accurately project their future cash flows and effectively manage their money.

Purpose of a Budget

A budget can be made for a person, a family, a group of people, a business, a government, a country, a multinational organization or just about anything else that makes and spends money.

Planning and monitoring your budget will help you identify wasteful expenditures, adapt quickly as your financial situation changes, and achieve your financial goals.

When you actually see the breakdown of your expenses, you may be surprised by what you find; this process is essential to fully grasping how things can add up.

Creating a budget will decrease your stress because, with a budget, there are no surprises. Unexpected car problems or medical bills? With a budget, you don't have to panic or wonder if you have the money—you already know. This sense of financial clarity is important not only in college, but throughout life.

Since budgeting allows you to create a spending plan for your money, it ensures that you will always have enough money for the things you need and the things that are important to you. Following a budget or spending plan will also keep you out of debt or help you work your way out of debt if you are currently in debt.

Your budget for any particular time period is a guide for how you want to spend your money so that you can achieve your financial goals -- both in the short-term and the long-term. When you set up a budget, you can see where your money could go, and then you get to decide in advance which options are most important for you.

For example, if you don't have a budget, that snazzy new outfit or top-of-the-line grill might catch your attention in the store and get you to buy it even though you should be putting your money elsewhere. However, if you have a budget, and you know you want to prioritize saving for a new car or a house down payment, you can turn down impulse purchases because you know the money is already earmarked for something more important.

Budgeting is something that everyone, regardless of income or net worth, can benefit from. No matter how much money you make, you can always go bankrupt if you spend more than you bring in. However, budgets are also very personal, in that you decide which goals are most important to you. For example, one person might put a high value on driving an expensive car and be willing to work an extra job or cut back on other expenses to have one, while another person might be content to drive a used car into the ground to save up for a special vacation.

How Do I Create a Budget

If you don't have enough money to do everything you would like to do, then you can use this planning process to prioritize your spending and focus your money on the things that are most important to you.

You need to know your income and your expenses. Income includes not only your paycheck, but also any other money you receive, such as rent from a rental property or interest on a bank account. Your expenses include anything you spend money on, such as housing, food, clothing, insurance, entertainment and travel. To make an accurate budget, it helps to have several months worth of your past spending documented so you can make realistic predictions about how much you spend in each category.

As much as some people might prefer to set their budget and forget about it, good financial planning requires you to reevaluate your spending over time and adjust your budget accordingly. For example, if you change jobs so that your commute is shorter each day, you may be able to reduce the amount you have budgeted for gas costs and increase your retirement savings. Or, if the cost of food goes up, you may have to cut back on the amount of times you eat out each month.

Steps to take to create a budget:

1. What are my goals?
2. Where is my money coming from?
3. Where is my money going?
4. Add it all up
5. Make adjustments if needed

Step 1: What are my goals?

- The first step in creating a budget is to set your goals. What are your financial goals? Do you have debts you need to pay off? Do you want to minimize the debt you graduate with? Are you trying to save for a car, a vacation, or your future? What do want to accomplish while you are in school and when you graduate? Budgeting involves tough choices, but having a goal will make budgeting a little less painful and allows you to start planning for the future.
- Your goals can be defined using these three categories:
  - Short Term: less than one year
  - Mid-Term: one to three years
  - Long Term: more than five years
- Every financial goal you set should be a SMART goal: Specific, Measurable, Achievable, Relevant, and Time Framed.
  - For example, let's say that you want to go on a vacation to Hawaii when you graduate to celebrate your accomplishment! Maybe you are graduating in three years. So you have 36 months to save for your vacation. You did your research and found that you will need to save at least $4,500 for the trip you plan to take. So, that means you will need to set aside $125 each month until you graduate.
    - Specific: You plan to go to Hawaii when you graduate to celebrate your success
    - Measurable: You know that you will need to save $4,500 to take your trip
    - Achievable: You will need to save $125 a month to meet your goal
    - Relevant: Your goal is relevant to you - you plan to take a trip when you graduate as a reward for your hard work
    - Time-Framed: You plan to reach your goal in 3 years

Step 2: Where is my money coming from?

- Where does your money come from? List the sources of your income (e.g., work, student loans, parents) and the amount that comes in from each source each month. If you get one disbursement per semester (e.g., student loans and scholarships), determine the monthly allowance by taking the amount that's left after paying nonrecurring costs (e.g., tuition, books, dorm room) and dividing it by the 5 months in a semester.
- Example: If you earn $400/month at work and you have $1000 left over from student loans after paying your once-per-semester costs, then your total monthly income is $600.

Step 3: Where is my money going?

- Do you check your bank account at the end of the month or semester and wonder where all the money went? Before you can manage your money, you have to know how you’re spending it. Use a spreadsheet to track and categorize your expenses for one month. Get in the habit of recording your expenditures once a day.
- It's useful to separate your expenses into three categories. Categorizing your expenses will help you balance your budget by identifying which expenditures should be cut back on first.
  - Fixed Needs – Necessary expenses that stay the same from month to month, e.g., rent, phone bill
  - Variable Needs – Necessary expenses that may vary from month to month, e.g., gas, food
  - Wants – Nonessential expenses, e.g., lattes, movies, eating out, electronics

- If you have a monthly savings goal, include it as an expense. It is much easier to save money if you've planned for it in your budget. And it's important, too: if you run into unforeseen expenses, you'll want to be able to pay them without going into debt. And even if nothing goes wrong, having some savings will help you follow your dreams in the future.

Step 4: Add it all up.

- When you compare your income and expenses, do you have a monthly surplus, or will you be needing another job and begging your parents for help by the end of the semester?
- If you already have a surplus in your budget, you can invest in your future.
- On the other hand, if your expenses exceed your income, Step 5 will help you make some adjustments.

Step 5: Make adjustments if needed.

- If you're over budget, you need a strategy for controlling costs. Balance your budget, starting with the "wants" identified in Step 3.
- When you added up your monthly expenses, did you notice any surprisingly large numbers? Did you spend $100 at restaurants or on yet another new outfit? Did you spend more on electronics than food?
- Begin with such "wants" that you may be overindulging in. For each type of "want," decide on a reasonable monthly limit that will help you balance your budget. Would it help you reach your goals if you limited yourself to spending $40 a month at restaurants and did more shopping at the grocery store? Can you get by without a monthly clothing or electronics expenditure, making such purchases only after you reach savings goals? Set a cap on your "want" expenses and see if you've balanced your budget.
- If you can't trim enough from your "wants" in order to balance your budget, you will need to reduce your variable needs expenditures in the short term and perhaps your fixed needs expenditures in the long term. This may mean taking the bus instead of driving and finding less expensive housing next year.

Budget Forecasting and Planning

Once you create your budget, begin to use it and get a good feel for how it can keep your finances on track, you may want to map out your spending plan or budget for 6 months to a year down the road. By doing this you can easily forecast which months your finances may be tight and which ones you'll have extra money. You can then look for ways to even out the highs and lows in your finances so that things can be more manageable and pleasant.

Extending your budget out into the future also allows you to forecast how much money you will be able to save for important things like your vacation, a new vehicle, your first home or home renovations, an emergency savings account or your retirement. Using a realistic budget to forecast your spending for the year can really help you with your long term financial planning. You can then make realistic assumptions about your annual income and expense and plan for long-term financial goals like starting your own business, buying an investment or recreation property or retiring.

Budgets and Business

The budget process begins by establishing assumptions for the upcoming budget period. These assumptions are related to projected sales trends, cost trends and overall economic outlook of the market. Specific factors affecting potential expenses are addressed and monitored. The budget is published in a packet that outlines the standards and procedures used to develop the financial tool. The procedures include the assumptions of the markets, key relationships with vendors that provide discounts and how certain calculations were made. Upon the completion of all budgets, top management reviews the budget and submits the budget for approval to the board of directors.

There are two major types of budgets: static budgets and flexible budgets. Both budgets are useful to management. A static budget evaluates the effectiveness of the original budgeting process, while a flexible budget provides deeper insight into business operations.

- Static Budget: remains unchanged over the life of the budget. Regarding of changes that occur during the budgeting period, all accounts and figures remain the same as the figures were originally calculated.
- Flexible Budget: has a relational value to certain variables. The dollar amounts listed on a flexible budget change based on sales levels, production levels or other external economic variables.

Budgets are developed for different divisions, subsidiaries and departments within an organization. For a manufacturing organization, a budget is developed for direct materials, labor and manufacturing overhead.

All budgets roll up into the master budget that encompasses all smaller budgets. The master budget also includes budgeted financial statements, forecasts of cash inflows and outflows, and an overall financing plan.

A budget is a microeconomic concept that shows the tradeoff made when one good is exchanged for another.

A budget is an internal tool used by management and is often not required for reporting by external parties.

In a business, the budgeting for operations will include the following:

- Preparing estimates of future sales
- Preparing estimates of future cash collections and disbursements
- Preparing estimates of the future day-to-day activities of the organization
- Summarizing these estimates into an income statement and balance sheet

The budgeted income statement and balance sheet are also known as pro-forma financial statements. Once prepared and approved, the budgeted income statement and balance sheet are used to control the future activities of the business.

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