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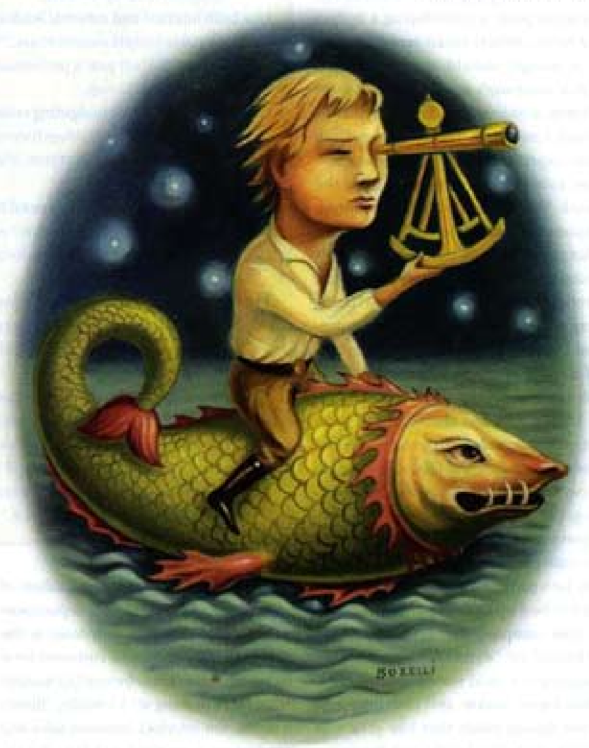
BUDGETING AND PLANNING

STAYING ON COURSE

It's hard to weather an economic slowdown without a sound budget to steer by.

BY KAREN M. KROLL



CaseCentral, a San Francisco–based litigation support firm, may seem as recession-proof as a business can be. It provides an electronic platform for evidence management to companies battling lawsuits—not a sector likely to see a precipitous falloff in business. Even so, CaseCentral isn't immune to corporate belt-tightening, says CFO Terry Wynn. "Legal fees have acquired a high profile," he explains. "There's greater pressure on corporations to look harder at overall litigation costs."

Thus it's no longer unheard of for the company's customers to try to renegotiate their contracts. While Wynn can't ignore their phone calls, he can readily estimate just how a change in terms will affect CaseCentral's projected financial performance. For that, he credits the firm's robust budgeting-and-planning (B&P) process.

CaseCentral prepares an annual budget in the fall, laying the foundation for performance goals and compensation for the coming year. But that's just the beginning. Each month, departmental leaders review actual results and reforecast 90 days out. If the forecast is diverging from the budget, they'll take corrective action. Once a quarter, senior management makes new forecasts for the rest of the current year and all of the following year, looking for trends in pricing and revenue.

Because he continuously links budgeting to planning, Wynn can quickly estimate the financial impact of every decision, be it a price cut for a large customer or hiring a senior employee. The B&P process enables managers "to see how the decisions they're making impact the bottom line," says Wynn.

FROM BURDEN TO BOON

Sounds sensible enough, but it's far from common. More than half the respondents to a 2008 survey by the BPM Forum, a business performance management group, said that their budgeting process is overly burdensome. In general, employees "don't buy into the fact that [budgeting] is an important part of the strategic-planning process," says Daniel A. Szpiro, professor of accounting at Cornell University.

That apathy can exact a heavy price when the economy hits a rough patch. To navigate a downturn, Szpiro says, managers and employees need to understand the key activities that drive financial results. If sales are trending flat, how will expenses change? How will rising fuel prices pinch gross margins? Can the organization afford a new salesperson? What if he or she needs six months to ramp up?

To get employees more involved, try speaking their language, advises Bryan

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Hall, practice leader in the finance advisory group at consulting firm The Hackett Group. Rather than asking plant managers about financial ratios, talk instead about the number of overtime hours or level of scrap materials they are anticipating, he says. Focusing on the data points that are most top of mind for them can be a starting point for developing a budget that better reflects actual performance.

A budget should also be aligned with a company's strategy, says Samuel Weaver, a finance and law professor at Lehigh University. This can temper the urge, especially strong during a recession, to make sweeping cuts across the board. The problem with that common response is that most strategic undertakings are cross-functional, points out Philip Peck, director of the Palladium Group, in Lincoln, Massachusetts. "A simple directive to cut R&D by 10 percent over six months may chop the legs off a major strategic initiative" that involves the entire company.

Ideally, a budget should reflect links between different departments, says Bill Soward, president and CEO of Mountain View, California-based Adaptive Planning, the provider of the budgeting-and-reporting software used by CaseCentral. For example, if marketing plans an all-out blitz for a particular product line, sales will need to beef up its resources accordingly.

One company that takes this "driver-based" or "dynamic" approach to planning is Kahiki Foods, a Columbus, Ohio-based maker and distributor of Asian frozen foods that has grown at double-digit rates for the past five years. Its B&P process begins in late summer, when salespeople contact current customers to get an idea of their plans for the following year. Department heads then budget monthly for the following year and annually for the next two years, according to Fred Neibauer, vice president of finance and assistant treasurer.

PLANNING FOR A SLOWDOWN

>>How to tackle budgeting and planning in a rocky economy

If business isn't booming, try starting with a "lights-turned-on budget," recommends Lawrence Serven, president of budgeting-software company XLerant. Keep all expenses flat except for salaries. Then, budget for incremental project costs.

Use both internal and external leading indicators, such as industry trends, to guide budget assumptions. "When you look forward, use something other than last year's performance," says Bryan Hall, a consultant at The Hackett Group.

Give responsibility for budgeting resources to the managers who will be using them, says Serven. When finance comes up with the numbers and business managers only review them, it's too easy to point fingers if actual results differ from budget.

Remember that a plan doesn't need to be spot-on to be of value, says Jim Winett, managing partner with ICCS Partners in Los Angeles. The process of creating one forces management to think about the company's direction.

Put "some teeth in the budget," Winett says. Even though it's important to reforecast regularly, managers should commit to their numbers. That way, they're more inclined to use all the tools at their disposal to meet their goals.

Find a balance between using the budget as a planning tool and as a performance-measurement tool, says Daniel A. Szpiro, a professor of accounting at Cornell University. If too much compensation is tied to the numbers, budget padding is inevitable; if too little, managers have little motivation to strive harder. Identify the results an individual can control and base compensation on them. —K.K.

Tim Tsao, Kahiki's vice president of sales and marketing, says his department works with finance "to drill down to the unit level, case level, and customer level by month, so we know forward 12 months what we're looking at." Crucially, "there's a significant interlock between sales and production as we plan," says Tsao. For example, if sales decides to expand a line of appetizers, operations needs to weigh in and figure out if Kahiki's current capacity can accommodate that planned growth.

Such information cascades through production, says Neibauer. Because many ingredients have a long lead time, the company places orders based on the forecast; it can't wait until it has purchase orders in hand. Meanwhile, to offset Kahiki's rising freight costs (10 to 15 percent over the past 18 months), the company's logistics manager carefully plans truck routes to minimize less-than-full loads.

IT'S A JUNGLE IN HERE

Of course, even a top-notch B&P process can't replace managerial judgment. Once finance and business-unit heads provide a clear picture of the company's direction, a leader still has to determine where to cut and where to invest.

At the San Diego Zoo, CFO Paula

"A simple directive to cut R&D by 10 percent over six months may chop the legs off a major strategic initiative" that involves the entire company, says Palladium's Peck.

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Brock and the divisional heads review expense trends every four weeks, with an emphasis on revenue. "We budget for top-line growth," says Brock. That way, the zoo can fulfill its larger mission of supporting the 150 conservation projects it has under way in 40-plus countries.

While the economic slowdown doesn't appear to have affected attendance so far, the wildfires that surrounded the zoo last fall did. As a result, managers began paying more attention to nontraditional revenue sources, says Brock. One idea: expand the zoo's "Roar and Snore" events, in which guests stay overnight. Another: create a cheetah-run safari, where guests get a close-up view of a cheetah sprinting after a mechanical rabbit. By regularly adding such offerings, management hopes to generate more visits not only from zoo members, but also from international travelers who are taking advantage of the declining dollar.

That may be the real key to employee engagement: get them to think about ways to expand the pot of money being budgeted. CFO

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