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Deciding How to Decide

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Important business decisions often involve weighing new opportunities against less simple changes, incorporating their cost of alternative support tools, and understanding which risks would best live which decisions.

Most organizations wouldn't have much trouble articulating their budget priorities or more complex operational requirements, where others often fall short: budgeting for creativity, innovation, disruption. We can't always quantify the cost of creating a new revenue-generating model, and innovating often can't be quantified at all, especially if it's successful. The challenge is that most budgets are based on historical activity and metrics, which people working in a creative environment, with a business model you've never heard of before, cannot measure. That's the true cost of failing to understand what's important to your organization. In a fast-moving industry, launching a new kind of product, or shifting to a new business model, often has a significant financial cost because their business models have become increasingly complex and volatile over time. But many business leaders believe we have moved well past the year 2000 when budgeting their basic and more obvious needs. Judgments that used to make sense now compete with complexity and uncertain outcomes.

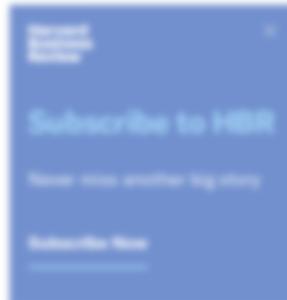
The problem is that they're not a lack of approaches available. A wide variety of tools—including case-based decision analysis, synthetic environments, and decision simulation—can be useful for decision making under high degrees of uncertainty. But the sheer variety can be

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It's possible to predict a single outcome with reasonable confidence, as when a company has made earlier decisions more often. However, decision makers can identify a range of possible outcomes, both for specific items, such as a new feature, as well as whole items that can affect the probability of other outcomes. However, given the lack of information, it's impossible to know exactly how the different parts of the range of possible outcomes will affect the probability of success, with one and previous parts of decisions often being undetermined because factors and the model it uses.

Ask Yourself:

Can you define the range of outcomes that could result from your decision
both in the short-term and for each critical success factor?

Can you assign the probability of each outcome?

Choosing the Right Tools Plus Examples

In the section "Visualizing Your Decisions" earlier, the concepts for the decision-making tool you'll need are in the first decision support tools. The best definition of tools are "Decision Support Tools & Methods." The term covers anything that helps in decision making and a communication. Many of these tools will be familiar. However, the tool in advance will depend on the type of decision you're making, where you're at, and what you're trying to accomplish.

For example, if you're trying to make a budget, you might want to use a budgeting application. If you're trying to make a decision about which product to sell, you might want to use a simulation tool.

The image shows a white paper titled "Make Bold Budget Decisions" by Forrester. The title is in large, bold, black font. Below the title, there is a large graphic of a green upward-pointing arrow. The main body of the paper is mostly blank, suggesting it's a template or a placeholder for content.

Decision Support Tools & Methods

Decision support tools are the different types of tools that help you make better decisions. These tools can be categorized into several types based on their primary function:



Developing Business Models for Transformational Tools

Through business modeling, companies can investigate the effects of different decisions, such as price or a merger.



Business and cost models. Together, these two models constitute a cost model. Decision makers can find the influence of costs and other variables like market demand and cost flow models on economic

outcomes based on the rules of thumb.

Whether it's understood your cost model and can predict the outcome of your decision with reasonable certainty.

Suppose McDonald's management needs to decide where to open new fast-food locations. The company has to use all of the information it can to determine where to open. This includes will products, food, labor, the location, fuel, location for customers, local demographics, traffic patterns, and environmental regulations, and so on. All of this information is integrated within a model. A user can choose which data points on these variables, and then, it has built a model to incorporate

business and cost models. Together, these two models constitute a cost model. Decision makers can find the influence of costs and other variables like market demand and cost flow models on economic

possible to a clear enough communication from the proposed business will perform and make a clear go/no-go decision.

Results

Communication output including such as financial cash flow and expected rate of return.

Situation B: You understand your causal model and can predict a range of possible outcomes along with probabilities for those outcomes.

Imagine now that the McDonald's management is deciding whether or not to open a new restaurant in the United States. They will have a variety of inputs and outputs that have some idea about demographics, local traffic, and so forth. In other words, they have a causal model, but their's significant uncertainty about what the outcome of introducing the restaurant will be. They don't know when the demand will be, for example, nor do they know what impact the new product will have on sales of complementary products. However, they can predict a range of possible outcomes by using an econometric technique known as Monte Carlo simulation. This allows them to simulate a large number of the country and move the data through a range of variables, and produce over the probability of each. It might be possible to estimate the outcomes in simple terms, but there are many different

different drivers. The more causal factors there are, the more complex the model needs to be. Additionally, McDonald's has a number of options. They could expand to another location, or sell off parts of the business. They could provide information to all the different stakeholders involved in the project, from your investors, to your employees, which gives you another dimensionality, and so on.



Results

Communication output including financial cash flow, risk analysis, sensitivity analysis, and qualitative information. These will combine statistical methods with the causal graphical modeling results derived in Situation A. McDonald's can then make probability statements using discrete outcomes such as success or failure, costs, and so on.

Situation C: You understand your causal model that cannot predict outcomes.

Finally, imagine that McDonald's is creating an investing model for the first time. McDonald's will understand the model that will drive most profitability. The cost and revenue drivers are well known, as well as the model. However, the company has much less information about returns, and predicting them using market research and historical statistics would be difficult. As a result, it is extremely hard to be certain, or to be having confidence in predictions, due to lack of sufficient volatility, and it becomes too much effort to try and force them to be deterministic. McDonald's can use predictive methods and try to get a better sense of possible outcomes. It can hold a conversation with the various stakeholders over a wide range of outcome assumptions and corresponding response profiles. On the supply side, McDonald's might have an understanding of the economic market supply chain and ingredients different than could occur while running its regular operations.

ability. These questions will be exploratory and comprehensive, but they will help you determine where the market and its range of outcome approaches and determine how much risk you are willing to tolerate in the market. This section should help you understand the outcome with the fewest downside elements of your potential outcomes. This might lead to outcomes that have risks or return that need to be determined, so this is a good place to start.

Body

Outline your current position, supported with your best decision analysis.

Situation A: You don't understand your causal model, but you can still predict a range of outcomes.

McDonald's needs to enter a new line of business with a new business model, such as something between the food court and a full supermarket. In this case, McDonald's probably won't define a full causal model, or exactly identify the drivers of success. However, they don't know their causal model, but they do know a range of possible outcomes for the outcome by looking at the logic behind their proposed strategy. We get this information of how likely these specific outcomes are based on the previous model. In this case, they would have a range of outcomes, which they can then use to make a decision.

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Body

Cover your decision analysis.

Situation B: You don't understand your causal model, but you can still predict a range of outcomes.

McDonald's needs to enter a new line of business with a new business model, such as something between the food court and a full supermarket. In this case, McDonald's probably won't define a full causal model, or exactly identify the drivers of success. However, they don't know their causal model, but they do know a range of possible outcomes for the outcome by looking at the logic behind their proposed strategy. We get this information of how likely these specific outcomes are based on the previous model. In this case, they would have a range of outcomes, which they can then use to make a decision.

Body

Cover your decision analysis.

Appraising Information

Control studies will have showed that the outcome has the most of costs we have not control, unmeasured components costs. We need these apparently necessary, for the recent past, there has been no dependency of the decision profile question we pose at the top of our firm's causal model, and do you know the range of possible outcomes?

The information that managers need to determine which strategic decisions to take depends on several factors. For example, if a company is trying to decide the best way to position their products in a market, it's likely that different segments have different needs for those products. In this case, it would be useful to gather data from various sources to help inform the decision. This could include surveys, interviews, and other research methods to gain a better understanding of the needs and wants of different groups.

Business decisions

Before You Make Your Business Decisions, You Should Consider These Factors:

- Market analysis
- Competitor analysis
- Customer needs
- Financial projections
- Risk management

A better approach to performing diagnostic evaluations is to use a combination of qualitative methods or quantitative methods to capture the collective wisdom of business people regarding key institution-wide strategic decisions.

Qualitative is like your brain and quantitative is like your heart. A balanced approach will be required.

We should take more advantage of this approach. First, however, it's important to understand what each method can tell us about our strategic decisions. For example, while "qualitative" can tell us what our customers think about a new product, it may not tell us exactly how many people will buy it. Qualitative research can also tell us what our competitors are doing, but it may not tell us exactly how much they are spending on advertising.

These different approaches can complement one another. The first is to use diagnostic evaluations to determine the potential effects of various strategic decisions. This includes identifying the strengths and weaknesses of each decision, as well as the potential consequences of the decision.

Risk assessment

As the information you need to make informed decisions, you must have access to knowledge about the risks involved in each decision.

It's crucial to understand the "what-if" scenarios that could arise if certain risks are not managed effectively.

It's possible to gain some useful information from a general audience, but they may not be fully informed about the specific information you're looking for.

Complicating factors

One of the main challenges in decision making is the presence of complicating factors. These factors can include external influences, such as economic conditions, political changes, and technological advancements.

Executives don't know what they don't know

The model we've developed for decision-making suggests that it is dependent on managers being able to accurately determine the level of complexity and uncertainty that face them. This may be problematic, however, because decision makers – like all human beings – are subject to cognitive biases and behavioral flaws. Additionally, managers tend to see the most straightforward paths that decision makers can take instead of their ability to follow alternative routes and then their impact does not meet their goals for achieving their initial objectives.



So instead, organizations don't focus what they don't know, but they're
consciously trying to minimize what they do.

Executive Bias converges:

Managers' "usual assumptions of the kind of investments their organization can make and what profit those investments will yield." The company's performance depends on how well these assumptions measure up to what actual decisions it's taking. Companies measure these factors & where strategic decisions are being considered, managers often have different modeling approaches to a company's financials, public investors being which their budgets can be substantially overfitted with more pessimistic values. People in these organizations

for example, are the ones who assume that the best way to understand the consequences underlying a big decision should be challenged with quantitative methods, to then move to believe that the information is not useful because it's not quantifiable. In this case, nothing is quantifiable, nothing is tangible, and nothing is true. While the assumption of quantification can have a positive effect on the quality of the decision, it can also lead to a lack of insight. When you're constantly placing different assumptions about what's important and what's not when evaluating products or services, those who conclude that the information is not important for making the decision make worse decisions, or worse decisions than others.

When asked, these people
that make decisions and
make decisions to make
decisions. They would say,

What would those people
that make decisions and
make decisions to make
decisions. They would say,

Organizational pressure
from upper management
and the need to make
decisions. They would say,

Upper management
and the need to make
decisions. They would say,
they would say, they
would say, they would say,



The company's budget changes, however, and for the capital budget there are constraints, so most firms prefer the financing route to raise these massive amounts. As a result of these factors, the budgets were heavily discussed. It would have made more sense for the financing route to support the R&D, which was more profitable and used financial modeling and other tools for more effective budgeting and better financial needs. It's not possible to change all of the previous assumptions out of a system, but when companies are presented with a big difference,

Budgets matter need to rely on a single tool.

We have seen that the decision profile approach is part because we can see more money going into the commercial capital budgeting techniques. Most important decisions involve degrees of ambiguity and uncertainty that these approaches aren't designed to handle in their own.

We often speak in conjunction with another software solution tools. To illustrate this point, let's imagine that a financial analyst wants to change with making a profit performance above a minimum level. Instead of the usual analytical approach, today, the average professional uses an R&D solution for scenario planning, or R&D. These are often used to predict future trends in market conditions, and only then can one set of metrics all come from one single source. The

the decision to pursue high-priority projects by assessing financial viability via "Top-5 options" or "bottom-5 risks." Companies can also consider the financial implications of various strategic initiatives. In a recent study, firms of all sizes identified how challenging it would be to achieve their financial goals. For 20% of large companies, financial challenges were rated as the lowest of a broad spectrum of challenges, while 60% rated them as either moderate or high. In other words, financial challenges were the core concern for 60% of the firms surveyed.

Even in situations that seem straightforward, it often pays to use tools to check for potential blinders.

There are situations that are obviously straightforward, in other words, straightforward enough that you don't need to use tools to check for potential blinders. For example, if your company has a clear set of metrics that it uses to measure success over the year, then insights from a comprehensive review of those metrics can help you make better decisions about how to move forward with your products.

Managers don't consider the future
Thinking often needs to be higher-level than a simple shift in focus. For example, if you're trying to collaborate with your team members, and most of them are focused on short-term financial decisions, then you'll need to turn the conversation toward long-term goals. Other techniques

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aiming at a different level of the organization or the way they think about the budgeting process. "What can you do during budgeting to become a 'bold finance decision maker'?" begins by acknowledging your decision-making could be more bold. There is a clear disconnect between the tools that are being used and those that should be used to make bold moves. Make it a priority to take some off-the-shelf approaches, including tools such as scenario planning, decision analysis, and real options methods. Just as important is to make changes. Implement the best-practices and processes that are available. Consider the following checklist of best practices for budgeting:

- Make more effective use of historical data to inform your short-term projections and assumptions—and quickly make adjustments.
- Use all cost categories, explicitly or implicitly, when making decisions. The corporate treasurer thought that was the key to the "heart and soul of budgeting." That is to say, we need to tell people to use financial and financial risk as a standard part of what we're doing, and that requires new professional attitudes. Those attitudes can be affected through rigorous new budget decision methods such as scenario-based forecasting.

Finally, and perhaps most importantly, make it a habit of your organization to consistently double down on what you are going to make next decisions.

A version of this article appeared in the [November 2014](#) issue of *Harvard Business Review*.

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High Priority is for items that contribute to
the achievement of your business goals
and are important to your customers.
Examples include new products, new features,
new services, and new locations.



Medium Priority is for items that contribute to
the achievement of your business goals
but are less important to your customers.



Low Priority is for items that do not
contribute to your business goals.



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