**Budget**

**What Is a Budget?**

The term budget refers to an estimation of [revenue](https://www.investopedia.com/terms/r/revenue.asp) and [expenses](https://www.investopedia.com/terms/e/expense.asp) over a specified future period of time and is usually compiled and re-evaluated on a periodic basis. [Budgets](https://www.investopedia.com/budgeting-calculator-5101411) can be made for any entity that wants to spend money, including governments and businesses, along with people and households at any income level.

To manage your monthly expenses, prepare for life's unpredictable events, and be able to afford big-ticket items without going into debt, budgeting is important. Keeping track of how much you earn and spend doesn't have to be drudgery, doesn't require you to be good at math, and doesn't mean you can't buy the things you want. It just means that you'll know where your money goes, and you'll have greater control over your finances.

KEY TAKEAWAYS

* A budget is an estimation of revenue and expenses over a specified future period of time and is utilized by governments, businesses, and individuals at any income level.
* A budget is basically a financial plan for a defined period, normally a year that is known to greatly enhance the success of any financial undertaking.
* Corporate budgets are essential for operating at peak efficiency.
* Aside from earmarking resources, a budget can also aid in setting goals, measuring outcomes, and planning contingencies.
* Personal budgets are extremely useful in managing an individual's or family's finances over both the short and long-term horizon.

**Understanding Budgeting**

A budget is a microeconomic concept that shows the trade-off made when one good is exchanged for another. In terms of the bottom line—or the end result of this trade-off—a [surplus budget](https://www.investopedia.com/terms/b/budget-surplus.asp) means profits are anticipated, a [balanced budget](https://www.investopedia.com/terms/b/balanced-budget.asp) means revenues are expected to equal expenses, and a [deficit budget](https://www.investopedia.com/terms/b/budget-deficit.asp) means expenses will exceed revenues.

**How to Budget in 7 Steps**

The specifics of your budget will depend on your personal financial situation and goals. In most cases, though, the steps for creating a budget are the same. You can make a budget by following seven simple steps.

1. Add up your total [income](https://www.investopedia.com/terms/i/income.asp). This should include all sources, such as a paycheck, tips, Social Security, disability, alimony, or investment income.
2. Track your spending. Spend a month keeping track of everything you spend, whether you pay with a credit card or cash, to find what your real expenses are. Be sure to include automatic payments, subscriptions, and utilities.
3. Set financial goals. Do you want to save money? Pay off debt? Stop overspending? Decide on realistic goals. Remember, you can adjust these over time. Pick the most pressing goals, such as paying off debt or creating an emergency fund, first.
4. Calculate mandatory [expenses](https://www.investopedia.com/terms/e/expense.asp). These are expenses you must pay each month, such as rent, insurance premiums, taxes, childcare, or your cell phone bill. Subtract these from your total income.
5. Identify debt payments. If you are paying off debt, such as student loans or a credit card bill, find the minimum payment for each debt. Subtract that from your income as well.
6. Make a spending plan. The amount of income you have left is what you can spend on discretionary expenses. These can include your goals, such as debt payment or savings. It should also include things like groceries, entertainment, gas, or surprise expenses. Give every dollar a job, based on your goals and what you discovered when you tracked your spending.

Open a New Bank Account

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1. Adjust each month. Each month, look at your spending and goals, Reevaluate and adjust where you assign your discretionary spending. A flexible budget will help you avoid overspending.

**Corporate Budgets**

Budgets are an integral part of running any business efficiently and effectively.

Budget Development Process

The process begins by establishing assumptions for the upcoming budget period. These assumptions are related to projected sales trends, cost trends, and the overall economic outlook of the market, [industry,](https://www.investopedia.com/terms/i/industry.asp) or [sector](https://www.investopedia.com/terms/s/sector.asp). 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 it, including the assumptions about the markets, key relationships with vendors that provide discounts, and explanations of how certain calculations were made.

The sales budget is often the first to be developed, as subsequent expense budgets cannot be established without knowing future [cash flows](https://www.investopedia.com/terms/c/cashflow.asp). Budgets are developed for all the different subsidiaries, divisions, and departments within an organization. For a manufacturer, a separate budget is often developed for direct materials, labor, and overhead.

All budgets get rolled up into the master budget, which also includes budgeted [financial statements](https://www.investopedia.com/terms/f/financial-statements.asp), forecasts of cash inflows and outflows, and an overall financing plan. At a corporation, the top management reviews the budget and submits it for approval to the board of directors.

Static vs. Flexible Budgets

There are two major types of budgets: [static budgets](https://www.investopedia.com/terms/s/staticbudget.asp) and flexible budgets. A static budget remains unchanged over the life of the budget. Regardless of changes that occur during the budgeting period, all accounts and figures originally calculated remain the same.

A 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 factors.

Both types of budgets are useful for management. A static budget evaluates the effectiveness of the original budgeting process, while a flexible budget provides deeper insight into business operations.

ADVISOR INSIGHT

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The importance of budgeting cannot be understated. A budget, also known as cash flow, is arguably more important than the actual cash that you have in your bank and investment accounts. Your cash flow is what allows you to pay for everything (or not).

Without knowing your cash flow, you could be putting yourself into a bad financial situation and not even know it. You can only get by without knowing your cash flow for so long before you get into financial trouble, so make the time you know the flow of your cash. Budgeting should be something that everyone does, regardless of their financial situation.

**Personal Budgets**

Individuals and families can have budgets, too. Creating and using a budget is not just for those who need to closely monitor their cash flows from month to month because money is tight. Almost everyone can benefit from budgeting—even people with large paychecks and plenty of money in the bank.

Budgeting is a wonderful tool for managing your [finances](https://www.investopedia.com/terms/f/finance.asp), but many people think it's not for them. Below is a list of budget myths—the erroneous logic that stops people from keeping track of their finances and allocating money in the best way.

1. I Don't Need to Budget

Having a handle on your monthly income and expenses allows you to make sure your hard-earned money is being put to its highest and best purpose. For those who enjoy an income that covers all bills with money left over, a budget can help maximize savings and [investments](https://www.investopedia.com/terms/i/investment.asp).

If one's monthly expenses typically consume the lion's share of [net income](https://www.investopedia.com/terms/n/netincome.asp), any budget should focus on identifying and classifying all the expenses that occur during the month, quarter, and year. And for people whose cash flow is tight, it can be crucial for identifying expenses that could be reduced or cut, and minimizing any wasteful [interest](https://www.investopedia.com/terms/i/interest.asp) being paid on credit cards or other debt.

2. I'm Not Good at Math

Thanks to budgeting software, you don't have to be good at math; you simply have to be able to follow instructions. Many of these programs are free and legitimate. If you know how to use spreadsheet software, you can make your own ledger. It's as simple as creating one column for your income, another column for your expenses, and then keeping a running tab on the difference between the two.

3. My Job Is Secure

No one's job is truly safe. If you work for a corporation, being laid off due to downsizing or a [takeover](https://www.investopedia.com/terms/t/takeover.asp) always is a possibility. If you work for a small company, it could die with its owner, be bought out, or just fold.

You should always be prepared for a job loss by having at least three months' worth of living expenses in the bank. It's easier to accumulate this financial cushion if you know the amount you're bringing in and spending each month, which can be monitored with a budget.

4. Unemployment Insurance Will Tide Me Over

[Unemployment compensation](https://www.investopedia.com/terms/u/unemployment-compensation.asp) is not a sure thing. Let's say a bad situation at work leaves you with no choice but to quit your job. Unless you can prove [constructive discharge](https://www.investopedia.com/terms/c/constructive-discharge-claim.asp) (that is, you were virtually forced to resign), your departure will be considered voluntary, making you ineligible for unemployment insurance. Besides, the benefits may fall well short of the wages you're used to: for most states, they average between $300 and $500 per week.

5. I Don't Want to Deprive Myself

Budgeting is not synonymous with spending as little money as possible or making yourself feel guilty about every purchase. The aim of budgeting is to make sure you're able to save a little each month, ideally at least 10% of your income, or at the very least, to make sure that you aren't spending more than you earn.

Unless you're on a very tight budget, you should be able to buy baseball tickets and go out to eat. Tracking your expenses does not change the amount of money you have available to spend every month; it just tells you where that money is going.

6. I Don't Want Anything Big

If you don't have any major savings goals (upsizing your living situation, starting your own business, etc.), it's hard to drum up the motivation to stash away extra cash each month. However, your situation and your attitudes likely will change over time.

Let's say you and your partner [live in New York City](https://www.investopedia.com/articles/personal-finance/090115/living-new-york-city-coops-vs-condos.asp) in a small one-bedroom apartment and things are going fine for the both of you until your family dynamic changes. For instance, you may have a child or an in-law who comes to stay with you indefinitely, which means you'll probably need (and want) more room to accommodate the new addition. If you don't save up for anything big, you may not be able to afford this change in your living situation later on down the road.

7. I Won't Qualify for Student Financial Aid

Yes, the catch-22 of [student financial aid](https://www.investopedia.com/articles/personal-finance/061814/5-ways-get-maximum-student-financial-aid.asp) is that the more money you have, the less aid you'll be eligible for. That's enough to make anyone wonder if it isn't better to just spend it all and have no savings in order to qualify for the maximum amount of grants and loans.

But that catch mainly applies to [earned income](https://www.investopedia.com/terms/e/earnedincome.asp). Whether you are an adult student going back to school or the parent of a student headed to college, the [Free Application for Federal Student Aid (FAFSA)](https://www.investopedia.com/terms/f/federal-application-of-student-aid-fafsa.asp) form (used for [Stafford Loans](https://www.investopedia.com/terms/s/stafford-loan.asp), [Perkins Loans](https://www.investopedia.com/terms/p/perkins-loan.asp), or [Pell Grants](https://www.investopedia.com/terms/p/pell-grant.asp)), does not require you to report the value of your primary residence (if you own a home) or the value of your retirement accounts.1

So if you want to save money without compromising your financial aid eligibility, you can do so by using your savings to buy a house, prepay your [mortgage](https://www.investopedia.com/terms/m/mortgage.asp), or contribute more money to your retirement accounts. The savings you put into these assets can still be accessed if you face an emergency, but you won't be penalized for it.

Even if you employ all the available legal strategies to maximize your financial aid eligibility, you still won't always qualify for as much aid as you need, so it's not a bad idea to have your own source of funds to make up for any shortfall.

8. I'm Debt-Free

Good for you! But being debt-free without any savings won't pay your bills in an emergency. A zero balance can quickly become a negative balance if you don't have a safety net.

9. I Always Get a Raise or Tax Refund

It's never a good idea to count on unpredictable sources of income. This may be the year your company may not have enough money to give you a raise or as much of a raise as you'd hoped for. The same is true of [bonus](https://www.investopedia.com/terms/b/bonus.asp) money. [Tax refunds](https://www.investopedia.com/terms/t/tax-refund.asp) are more reliable, but this depends in part on how good you are at calculating your own tax liability.

Some people know how to figure how much they'll get in a refund (or how much they will owe) as well as how to adjust this figure through changes in payroll [withholding](https://www.investopedia.com/terms/w/withholding.asp) throughout the year. However, changes in [tax deductions](https://www.investopedia.com/terms/t/tax-deduction.asp), IRS regulations, or other life events can mean a nasty surprise on your tax return.

10. I Just Don't Have the Discipline

If you're still not convinced that budgeting is for you, here's a way to protect yourself from your own spending habits. Set up an automatic transfer from your [checking account](https://www.investopedia.com/terms/c/checkingaccount.asp) to a [savings account](https://www.investopedia.com/terms/s/savingsaccount.asp) you won't see (i.e., at a different bank), scheduled to happen right after you get paid.

If you are saving for retirement, you may have the option of contributing a set amount regularly to a [401(k)](https://www.investopedia.com/terms/1/401kplan.asp)or other retirement savings plan. This way, you can pay yourself first, have enough money for the transfer, and pay yourself the same predetermined amount that you know will help you meet your savings goals.

11. It's a Luxury When I Barely Have Enough for the Essentials

Sometimes budgeting just isn't a priority because you may have too many other things on your plate. But there are certain government programs that can help you manage your household expenses. For instance, the [Supplemental Nutrition Assistance Program (SNAP)](https://www.investopedia.com/supplemental-nutrition-assistance-program-snap-5187718) helps recipients of all income levels work with their food budgets to make their benefits go further.2

**First Steps in Building a Budget**

In general, traditional budgeting starts with tracking expenses, eliminating debt, and once the budget is balanced, building an emergency fund. But to speed up the process, you could start by building a partial emergency fund. This emergency fund acts as a buffer as the rest of the budget is put in place and should replace the use of [credit cards](https://www.investopedia.com/terms/c/creditcard.asp) for emergency situations.

The key is to build the fund at regular intervals, consistently devoting a certain percentage of each paycheck toward it, and if possible, putting in whatever you can spare on top. This will get you to think about your spending, too.

What's an Emergency?

You should only use the emergency money for true emergencies. For instance, if you lose your job and need to pay for expenses, you could tap into your rainy day fund until you join the workforce again. You can also use this money if you have an unexpected medical emergency that arises.

You would save money if you used your emergency fund to eliminate [credit card debt](https://www.investopedia.com/terms/c/credit-card-debt.asp), but the purpose of the fund is to prevent you from having to use your credit card for paying for unexpected expenses. With a proper emergency fund, you will not need your credit card to keep you afloat when something goes wrong.

Downsize and Substitute

Now that you have a buffer between you and high-interest debt, it is time to start the process of downsizing. The more space you can create between your expenses and your income, the more income you will have to pay down debt and invest.

This can be a process of substitution as much as elimination. For example, cancel any recurring subscriptions that you don't regularly use or need. Use half of the money you save to invest or pay off outstanding debts, and save the other half to begin building a home gym in your basement.

Although [eliminating expenses](https://www.investopedia.com/terms/c/cost-cutting.asp) entirely is the fastest way to a solid budget, substitution tends to have more lasting effects. So:

* Consider shopping with friends and family so you can split the cost, especially if you buy in bulk.
* Carpooling or taking public transport is another great way to cut down on your transportation costs.

People often cut too deep and end up making a budget that they can't keep because it feels like they are giving up everything. Substitution, in contrast, keeps the basics while cutting down costs.

Find New Sources of Income

Why isn't this the first step? If you simply increase your income without a budget to handle the extra cash properly, the gains tend to slip through the cracks and vanish. Once you have your budget in place and have more money coming in than going out (along with the buffer of an emergency fund), you can start investing to create more income.

It is better to have no debt before you begin investing. If you are young, however, the rewards of investing in [higher-risk, high-return](https://www.investopedia.com/terms/m/mutualfund.asp) vehicles like stocks can outweigh most low-interest debt over time.

**How to Build a Complete Budget**

Now that you know the steps it takes to build a budget, you'll need to know how to build it. We've outlined the basics of how to craft a comprehensive budget below. Some of the information listed here has already been discussed. But it helps to reiterate it.

1. Calculate your total monthly income. This includes any [wages](https://www.investopedia.com/terms/w/wage-expense.asp), salaries, tips, benefits, and any other money that you get on a regular, monthly basis.
2. Determine your normal monthly expenses. Some of these are predictable, which makes them easier to work, especially if they don't change every month. Think of your [mortgage](https://www.investopedia.com/terms/m/mortgage.asp) or rent, utility payments, transportation costs, and other similar expenses. Some may fluctuate each month like your food or clothing costs. In these cases, it's always a good idea to err. onside the caution and budget a little higher. Be sure to include your debt, as well, such as [loans](https://www.investopedia.com/terms/l/loan.asp) and credit card payments.
3. Plan for any extras, including spending money in case you want to dine out, order takeout, see a movie, or do any other activity.
4. Note down any amount that you'll set aside for savings if that's in your plan.

Now that you have these figures, calculate your plan and write it out. A budget doesn't (and can't) work if you don't put it in writing. If you see it, you'll have more incentive to stick to it. You may have to do some juggling, especially in the initial few months. This means adjusting here and there so you stay within your planned budget. But once you've passed this hurdle, it should be fairly problem-free going forward.

If you can, though, keep your receipts and average out how much you spend each month when you build your monthly budget. This can help you determine how much to budget for any expenses that may change from month to month.

**Sticking to a Budget**

Now you understand the finer points of budgeting. You've accomplished all of the above, even putting together a nice spreadsheet that lays out your budget for the next 15 years. The only problem is that sticking to that budget isn't as easy as you thought. That credit card still calls your name, your clothes category seems awfully small and you feel deprived. Budgets, you decide, are no fun.

The good news is you don't have to throw it all out the window just because you've messed up once or twice.

Remember the Big Picture

The point of the budget is to keep you out of overwhelming debt and help you build a financial future that will give you *more* freedom, not less. So think about how you want your future to be and remember that keeping to your budget will help you get there. Adding to your [debt load](https://www.investopedia.com/terms/d/debt-load.asp), on the other hand, will mean that your future could be even tighter.

Remove the Options That Allow You to Cheat on Your Budget

Make it more difficult for yourself to make impulse purchases. In other words, set up barriers so you have time to stop and think: "Is this purchase necessary?" Take yourself off retailer email lists. Remove your stored payment information on your favorite online shops so you can't just click to order.

Find Some Support

If you feel like you're the only one in your group who is on a budget, search and find some like-minded folks. It could be an online forum, a monthly meeting, or even just a couple of friends traveling the same budgetary road. You need to know you're not the only person setting sane financial limits for yourself. You can also have accountability with your frugal buddies, talking things over and each other out of temptation.

Go Old School

There's something powerful about handing over a stack of $20 bills for purchase: It causes you to really think about the amount of money you're about to spend. Swiping a [debit card](https://www.investopedia.com/terms/d/debitcard.asp), on the other hand, may not feel nearly as real. Similarly, paying bills by writing checks and promptly entering the sums into your register keeps you up-to-date on how your account is affected in a way that autopay doesn't.

You don't have to use cash exclusively or completely forgo online payments, but handling transactions in old-fashioned ways can make you realize how much you're spending and enhance the power of self-regulation.

Reward Yourself

If you constantly look at what you have to cut and give up, the very act of budgeting becomes distasteful. A mixture of long- and short-term gifts to yourself will help keep you motivated.

When you've been faithful to your budget for a month, give yourself a reward. Even small ones can help, such as a night out with friends, a concert or a little extra cash for spending.

Keep visual reminders of these rewards or the things you're saving up for. Start building associations in your brain—that sticking to your budget has a pleasurable result.

Schedule a Periodic Budget Evaluation

It's difficult to predict how much money you'll need in every category of life; a new job may necessitate a wardrobe change and your clothing budget may not cut it. That's why it's important to have a regular check on how you've created your budget. If it isn't working, tweak it. It is your budget, after all—just make sure you keep your long-term financial goals in the picture.

Educate Yourself

Instead of taking the more common road of instant gratification, which leads so easily to overspending and endless debt, learn all you can about finances, [money management](https://www.investopedia.com/terms/m/moneymanagement.asp), and how you can best invest in yourself. Talk to your financially savvy friends and get real-world tips and advice from people who are doing well with their money.

The more you learn about handling money wisely and its rewards, the more concrete the reasons for budgeting will be, and the better you will be at not only creating a budget that works for you, but also sticking to it.

**Ways to Budget When You're Broke**

Budgeting strategies sound fine, but if you're in dire straits financially or suffering from mounting bills and a lack of funds, there are some other possible steps to take.

1. Avoid Immediate Disaster

Don't be afraid to request bill extensions or payment plans from creditors. Skipping or delaying payments only worsens your debt—and besides, late fees ding your credit score.

2. Prioritize Bills

Go over all your bills to see what must be paid first and then set up a payment schedule based on your paydays. You will want to leave yourself some catch-up time if some of your bills are already late.

If this is the case, call the bill companies to see how much you can pay now to get back on track toward positive status. Tell them you are taking strict measures to catch up. Be honest about the amount you can afford to pay; don't just promise to pay the full amount later.

3. Ignore the 10% Savings Rule

Stashing 10% of your income into your [savings account](https://www.investopedia.com/terms/s/savingsaccount.asp) is daunting when you're living paycheck to paycheck. It doesn't make sense to have $100 in a savings plan if you are fending off [debt collectors](https://www.investopedia.com/terms/d/debt-collector.asp). Your piggy bank will have to starve until you can find financial stability.

4. Review Spending

To fix your finances, you need to get a handle on your outlay first. Online banking and online budgeting software can help you categorize spending so you can make adjustments. Many people find that just by looking at aggregate figures for [discretionary expenses](https://www.investopedia.com/terms/d/discretionary-expense.asp), they are spurred to change their patterns and reduce excessive spending.

5. Eliminate Unnecessary Expenses

Once you've got a sense of where the money goes, it's time to tighten up. All cutbacks should start with items you wouldn't miss or habits you should change anyway—like reducing your fresh food purchases if you find ingredients spoiling before you can eat them. Or preparing meals at home more instead of going to restaurants or getting takeout.

Some expenses you shouldn't drop but might be able to adjust could include reducing your auto insurance rate by switching carriers.

6. Negotiate Credit Card Interest Rates

There are other proactive ways to reduce expenses. Those killer interest rates on your credit cards aren't fixed in stone, for example. Call the card company and ask for a reduction in the [annual percentage rates (APR)](https://www.investopedia.com/terms/a/apr.asp). So if you have a good record, your request might be approved. This won't lower your outstanding balance, but it will keep it from mushrooming as fast.

7. Keep a Budget Journal

Once you've gone through these steps, monitor your progress for a few months. You can do this by writing everything you spend in a notebook, via [budgeting apps](https://www.investopedia.com/best-budgeting-apps-5085405) on your phone, or with the software you used in step 4 to review your spending.

How you track your money isn't as important as how much you are tracking. Focus on ensuring that every cent is accounted for by dividing your expenses into categories. Fine-tune and adjust the spending as needed after each month.

8. Seek New Income

For the time being, saving and investing money is out. But consider ways to increase earnings: working overtime, getting a second job, or picking up some freelance work.

A budget isn't a prison cell to keep you away from your money. Rather, it's a tool you use to make sure your future is better—and yes, richer, than your present.

How Do You Create a Budget?

Creating a budget takes some work. You'll need to calculate every type of income you receive each month. Next, [track your spending](https://www.investopedia.com/personal-finance/common-budgeting-challenges-overcome/) and tabulate all your monthly expenses, including your rent or mortgage, utility payments, debt, transportation costs, food, spending money, and others. And write it down. The only way to reinforce your budget is to see it in writing. You may have to make some adjustments initially just to stay within your budget. But once you've gone through the first few months, it should become easier to stick to it.

What Is the 50-20-30 Budget Rule?

The 50-20-30 budget rule was popularized by Sen. Elizabeth Warren (D-Mass.) in her book *All Your Worth: The Ultimate Lifetime Money Plan.*The plan entails dividing all of your after-tax income into 50% on your actual needs, 30% on anything you want, and 20% on savings.3

How Does Budgeting Help a Business?

Just like budgets help people, corporate budgeting helps [businesses stay on track](https://www.investopedia.com/terms/a/administrative-budget.asp). This way, they don't stray very far from what they've projected. They also help business leaders make very important (investment) decisions, manage and meet goals and objectives, and identify any hurdles that come their way.

**The Bottom Line**

The word budget often conjures up images of complicated financial documents. But it's a tool that can be used by various entities, including governments, businesses, and individuals/households of every income level. The key is to learn how to craft one and how to stick to it. Once you have these key points under your belt, you'll be better prepared at securing your financial future.

(Source: https://www.investopedia.com/terms/b/budget.asp)