

# Zero Based Budgeting

## 1. What is zero based budgeting?

Zero-based budgeting (ZBB) is a method of budgeting in which all expenses must be justified for each new period.

The process of zero-based budgeting starts from a "zero base," and every function within an organization is analysed for its needs and costs. This means that the budgets or the costs of the previous periods are not considered in the budgeting process.

Budgets are then built around what is needed for the upcoming period, regardless of whether each budget is higher or lower than the previous one.

Zero-based budgeting can help lower costs by avoiding blanket increases or decreases to a prior period's budget.

The goal of zero-based budgeting is to reduce spending by looking at where costs can be cut.

ZBB is about looking for cost effective solutions to deliver the same or better results. AS such it frees up resources to be utilised in a different area/ expense.

ZBB can be applied to any type of expenditure- capital, operating, admin etc

## 2. How does this differ from traditional budgeting?

- a. Traditional budgeting calls for incremental increases over previous budgets, E.g. 2% increase in spending in travel expenses and this is included in the budget.

In ZBB, the previous travel expenses are not taken into consideration while budgeting. Instead, the teams are required to analyse costs and arrive at a justifiable travel expense budget for the budgeting period.

- b. Traditional budgeting analyses and justifies only new expenses which were not included in the previous budgets.

ZBB analyses both old and new expenses and aims at driving value by optimising costs.

### **3. Example of ZBB**

- a. If an organisation is starting a new project and requires human resources- In the case of traditional budgeting, the organisation will budget the cost to the company for hiring the number of resources

In ZBB, the organisation can attempt to understand the competencies of its existing employees to identify if any of them can be reallocated to the project. This will also require revisiting the existing projects to determine if there are surplus resources that can be reallocated.

- b. Travel expenses can be relooked at justified when the organisation decides that the field staff can for lesser number of days to the field and work remotely on the rest of the days
- c. Organisations can take a decision based on the cost benefit analysis of having a full fledged in house team vs outsourcing the work.

### **4. What are the advantages?**

- Its aligned to the requirements of the organisation
- Supports cost reduction
- Improves effectiveness and efficiency in functioning

### **5. Are there any challenges?**

- It is more time consuming to create than a traditional budget
- Requires in depth understanding of the needs of the organisation to justify the costs.