RESOURCE GUIDE · HERMIT BUSINESS SOLUTIONS

Operational Variances vs Planning Variances

Why the same £2,500 overspend can mean two completely different problems ***and two completely different fixes.***

Why this matters

Every month end review throws up variances - the gap between what you planned to spend or earn and what actually happened. It's tempting to treat every adverse variance the same way i.e. find out who overspent and ask them to do better next time. That response only works if the problem sits with the people running the operation day to day. Sometimes the real problem is the plan itself, set months earlier on assumptions that never held up. Telling the two apart is the difference between fixing the right thing and quietly repeating the same mistake next quarter.

The core distinction

A planning variance is the part of a variance caused by the original budget or standard being unrealistic. It shows up when the assumptions behind the plan (a supplier price, a sales forecast, a project timeline) turn out to be wrong by the time that the work actually happens, often for reasons that nobody could reasonably have known in advance. This is a planning problem, not a performance problem; even a perfectly run operation would show this variance because the yardstick it's being measured against was wrong from the start.

An operational variance is what's left once you strip the planning error out. It's the genuine difference between what should have happened, given a fair and up to date standard, and what actually happened. This is the part that reflects real operational performance; efficiency, negotiation, scheduling and the day to day decisions that your team made. It's the part worth holding people accountable for.

How a total variance splits in two

To separate the two, you need a middle benchmark alongside the original plan and the actual result; a revised standard, built with the benefit of hindsight, that answers the question 'given what we now know, what should this have cost or achieved?' The gap between the original plan and this revised standard is the planning variance. The gap between the revised standard and what actually happened is the operational variance. Add the two together and you get back to the total variance that you started with, now split into a part that's about the plan and a part that's about the operation.

Not just a costing tool

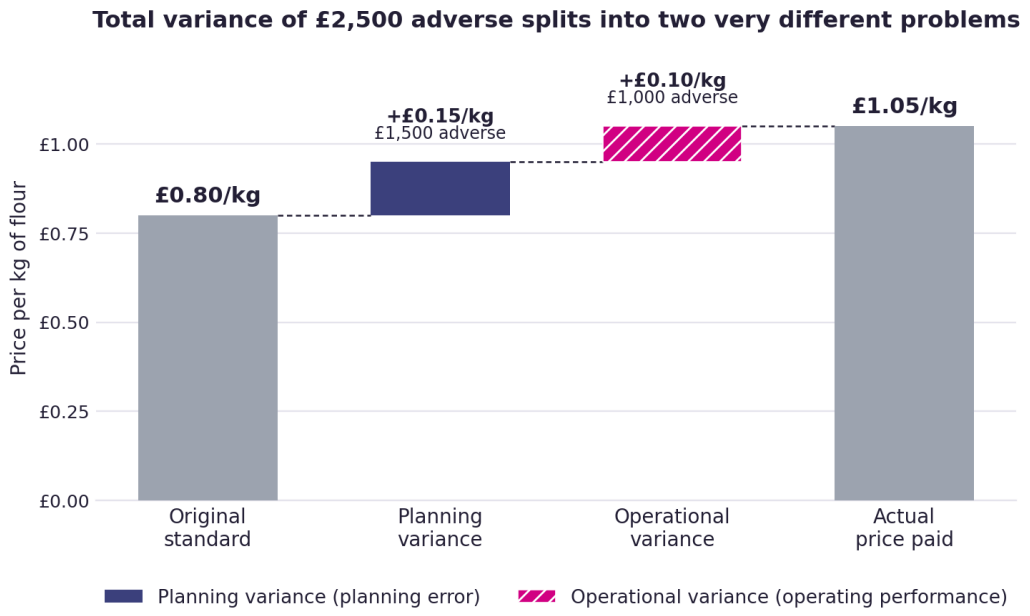
This framework didn't start out in bakeries. It comes from standard costing in management accounting but the logic travels well beyond material and labour costs. A project that runs three weeks over might be three weeks of the timeline itself being unrealistic (a planning variance), or three weeks lost due to poor coordination once work started (an operational variance). A sales target missed by 15% might reflect a target set on stale market data or a sales team that genuinely underperformed against a target that was perfectly fair. Whatever you're measuring, the same question applies - was the yardstick wrong or was the performance against a fair yardstick wrong?

Worked example: a bakery's flour bill

At the start of the year, the budget cost for flour was set at £0.80 per kg, based on the previous year's supplier price. Partway through the year, a poor wheat harvest pushed market prices up across the board, an event that nobody budgeting in January could have priced in. A fair, revised standard, reflecting that market shift, would have been £0.95 per kg. The bakery actually paid £1.05 per kg, having not shopped around once the market moved. Across 10,000kg purchased, here's how the £2,500 adverse total variance breaks down:

Stage	Price per kg	Variance from previous stage	What it tells you
Original budget (set at budget time)	£0.80	Starting point	The benchmark set months in advance, using last year's price
Revised budget (fair, with hindsight)	£0.95	Planning variance: £1,500 adverse	The wheat shortage was unforeseeable at budget time. This is a planning problem, not a buying problem
Actual price paid	£1.05	Operational variance: £1,000 adverse	The buyer didn't renegotiate or shop around once the market shifted. This is a genuine performance gap
Total variance		£2,500 adverse	Planning variance plus operational variance

The £2,500 overspend, visualised



Worked example: flour purchase, 10,000kg. The planning variance and the operational variance combine to the total adverse variance.

Operational vs planning variances, at a glance

Question	Planning variance	Operational variance
What causes it	The original budget, forecast or standard turns out to be unrealistic	Actual performance differs from a fair, up to date standard
Is it controllable day to day	No. It reflects the quality of the planning process, not day to day decisions	Yes. It reflects decisions and execution within the team's control
Who should own the fix	Whoever sets budgets, forecasts and standards, often finance or senior management	Whoever runs the operation day to day: buyers, project managers, department heads
Typical trigger	An unforeseeable market shift, a change in law, an unrealistic original forecast	A missed negotiation, an inefficiency, a scheduling slip, a quality issue
Typical fix	Revise the planning process itself: better forecasting, more frequent budget reviews, wider assumption testing	Coach or support the team, tighten processes, address the specific inefficiency

A second example: a website build that ran three weeks late

The same split works just as well for a timeline as it does for a cost. A client was quoted an 8 week build. Here's how the eventual 3 week delay breaks down once you separate the planning problem from the operational one:

Stage	Timeline	Variance from previous stage	What it tells you
Original plan (set at quote stage)	8 weeks	Starting point	The timeline quoted before work began
Revised plan (fair, with hindsight)	10 weeks	Planning variance: 2 weeks adverse	A third party payments system (like Stripe, Paypal) changed its requirements after the quote was given so the build took longer due to the extra work. This is a planning problem as the original scope was underestimated
Actual delivery	11 weeks	Operational variance: 1 week adverse	The developer was pulled onto another client's project for a week mid build. This is a genuine scheduling problem
Total variance		3 weeks adverse	Planning variance plus operational variance

Common causes of planning variances

- An out-of-date price list or supplier rate card used to set the original budget
- A sales forecast based on a market that shifted before the year even started
- A project timeline that never accounted for a known but unquantified risk
- An item cost that was set once and never revisited as conditions changed

Common causes of operational variances

- Buying from the wrong supplier or failing to renegotiate when prices move
- Inefficient use of materials, labour or machine time against a fair standard
- Poor scheduling or coordination that causes delays or rework
- Inconsistent quality control leading to waste or rework costs

Questions we're often asked

- Does this replace normal variance analysis? No, it's an extra step. Work out the total variance as you always would then use this split to decide where to focus your attention.
- Do I need to do this for every variance? No, just the larger or repeated ones. Small, routine variances rarely justify building a revised standard.
- What if I don't have a 'fair' revised standard to compare against? Use the best available evidence at the time: a spot market price, a competitor's rate, an industry benchmark. It doesn't need to be perfect, just more realistic than the original guess.
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KEY TAKEAWAY

A single 'adverse variance' on a report tells you something went wrong. It doesn't tell you whether the plan was wrong or the operation was wrong. Split the two out before you decide who needs a conversation and who needs a better forecast.

What to do next

- Before reacting to a variance, ask whether the original budget or standard was realistic given what's known now
- Build a revised, 'ex-post' standard for any variance that looks unusually large, then split the total into planning and operational components
- Route planning variances back to whoever owns the forecasting or budgeting process, not to the operational team
- Route operational variances to the team responsible, using the fair revised standard as the benchmark, not the original budget
- Get in touch if you'd like a hand building this split into your own management accounts