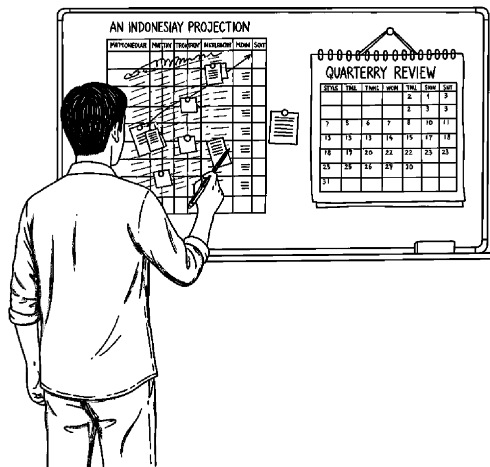
NICHE-SEARCH

WORKSHEET 5 OF 9

Three-Scenario Stress Test

Build base case, upside, and downside projections with explicit assumptions and measurable triggers. For use when a significant business decision — a new hire, a lease extension, a major purchase — depends on which scenario materialises.



Complementary worksheet for
Budget Forecasting Methods
by Ibrahim Anwar

SECTION 1

What This Is For

A budget with one scenario is a bet. It commits the business to one view of the future and leaves management with no prepared response when conditions differ from that view — which they always do, at some point. Three-scenario budgeting is not more complex than one-scenario; it is three sets of the same numbers with three explicitly different assumption sets. What makes it powerful is not the extra columns. It is the triggers: the pre-agreed conditions that tell management when to switch from base-case operations to downside response, or when to accelerate on an upside assumption.

This worksheet is for situations where a significant decision depends on which scenario materialises: adding a production line, signing a multi-year lease, taking on a major new hire, or committing to a capital expenditure above the normal threshold. Running the decision through three scenarios before committing to it answers the question most operators skip: can the business absorb the downside scenario, and what is the management response if that is the one that arrives?

SECTION 2

Benefits

What you get when you actually run this worksheet on a real situation:

- Prepares management responses before conditions change, so decisions made during a downside are deliberate rather than reactive.
- Forces explicit, defensible assumptions per scenario rather than one optimistic number dressed as a forecast.
- Reveals whether a capacity addition or major commitment is profitable only in the upside case — a risk that must be understood before, not after, the commitment is made.
- Produces the trigger definitions that allow operational managers to act without waiting for ad hoc direction when conditions shift.
- Generates the scenario documentation that institutional investors and underwriters treat as a management quality signal in due diligence.

SECTION 3

Framework To Use

— Assumption-First Scenario Build

Assumptions are written first. Numbers are calculated from assumptions. This makes each scenario defensible in one sentence rather than one column of hard-coded figures.

Three-Scenario Assumption Structure

Factor	Base Case	Downside Case	Upside Case
Revenue growth	Historical 3-yr average	Major customer -30% volume	New channel adds 20%
Gross margin	Consistent with current scale	Raw materials +15% above projection	In line with BI projection
CAPEX response	Execute as planned	Defer items A, B, C	Accelerate item D
Trigger condition	Base case is active assumption	Q1 revenue < 90% of target	Q1 revenue > 115% AND margin > 27%

SECTION 4

How To Use

Follow these steps in order. Each one builds on the previous.

1. Identify the five to seven factors that most influence this business's revenue and cost structure. Select the three most influential. These are the only factors that need to differ across scenarios.

2. Write the base case assumption for each factor in one concrete sentence. Not a percentage — a sentence that states the basis. 'Revenue growth in line with the three-year historical average of 12 percent' is a base case assumption. '15 percent growth' is not.

3. Write the downside case assumptions. The downside must be realistic and concrete — a condition that could happen within a normal business cycle. Not a disaster scenario. A downside assumption must be answerable: 'One customer representing 18 percent of revenue reduces volume by 30 percent.'

4. Write the upside case assumptions. The upside must be achievable if two or three identified conditions materialise. Not a best-case fantasy. State which conditions: 'Adding two distribution points in Q2 generates 20 percent volume growth in the first six months.'

5. Calculate the financial output for each scenario — operating profit, cash flow, working capital needs. Use formulas linked to the assumption cells. A model with hard-coded numbers in every cell cannot be audited when one assumption changes.

6. Define a trigger for each scenario shift. A trigger must meet three conditions: measurable (a specific number), time-bound (when the measurement is taken), and tied to a concrete pre-agreed action. 'If Q1 revenue falls below $X by [date]: freeze recruitment, defer CAPEX items A and B, reduce marketing budget by 30 percent.'

7. Communicate the triggers — not the full scenario document — to the managers who will execute the response. Each manager needs to know: the trigger relevant to their area and the steps they take when it is met.

8. Review the scenario assumptions quarterly, not annually. The downside case from December may look different from the downside case in April.

SECTION 5

Example Use

A distribution business with $5 million in annual revenue is considering adding a second warehouse location. The decision requires a 36-month lease at $8,500 per month. Management runs the three-scenario test before signing.

Base case assumptions: revenue grows 12 percent per year in line with the three-year average. The second location reaches 70 percent of the first location's volume by month 18. Lease cost is covered from month 8 onward.

Downside assumptions: one major customer (19 percent of revenue) reduces volume by 25 percent following a competitor's pricing move. The second location reaches only 45 percent of the first location's volume by month 18 due to slower market penetration. At these assumptions, the lease cost is not covered until month 22.

Downside cash flow check: at month 18 under downside conditions, cumulative lease payments total $153,000. Revenue shortfall from the reduced customer adds a further $85,500 gap. The business has $210,000 in operating cash reserves. The downside scenario is survivable, but leaves only $28,500 in reserve by month 18 — a narrow margin.

Trigger definition: if Q1 revenue at the new location falls below $180,000 (45 percent of the base case target for Q1), activate the downside response: freeze one planned hire for the new location; renegotiate payment terms with the two largest suppliers from net-30 to net-45 to preserve cash; defer the delivery vehicle purchase planned for month 6.

Decision: the board signs the lease with the trigger protocol documented and communicated. The operations manager at the new location receives a one-page document: 'If Q1 revenue at this location falls below $180,000 by [date], these three actions are already approved. You do not need to wait for a board meeting.'

SECTION 6

The Worksheet

Tear this out, copy it onto a fresh sheet, or fill it in directly.

Three-Scenario Stress Test

Build base case, upside, and downside projections with explicit assumptions and measurable triggers. For use when a significant business decision — a new hire, a lease extension, a major purchase — depends on which scenario materialises.

KEY ASSUMPTION	BASE CASE	UPSIDE CASE	DOWNSIDE CASE	TRIGGER FOR SCENARIO SHIFT

Reflection Prompts

After filling in the worksheet on the previous page, work through these.

1. For the downside scenario: if every assumption in the downside column materialised simultaneously, does the business remain cash-positive through the next six months? If not, identify which single cost reduction would restore cash-positive status — and pre-authorize that reduction now so the decision is not made under pressure.

2. Triggers must meet three conditions: measurable (a specific number, not 'conditions worsen'), time-bound (when the measurement is taken), and tied to a concrete pre-agreed action. Review each trigger row and confirm all three conditions are met.

3. For the upside scenario: which assumption is most likely to materialise, and what is the first operational decision that would need to be made within 30 days if it did? Write that decision in the margin so it is available when it becomes relevant.

SECTION 7

Tips and Traps

TIPS	TRAPS
• Build assumptions first, numbers second. If you build the numbers first and then write the assumptions to justify them, you have written aspirations with a scenario label attached. • The downside trigger must be pre-authorized before the scenario document is filed. A trigger that requires a board meeting to activate is not a trigger — it is a delay mechanism. • Write upside triggers too. A business with no protocol for capitalizing on conditions better than base case loses opportunity as surely as a business with no downside response loses time.	• Making the downside case only 5 percent below the base case. A downside that looks like a minor accounting variance is not a stress test — it is the base case with a different label. The downside must represent conditions that would require an active management response to survive. • Leaving the scenario document in the board's hands without communicating the triggers to operational managers. Managers who do not know a downside protocol exists will wait for direction when the trigger is met. By the time the direction arrives, the optimal response window has passed. • Mixing budget scenarios with stress tests. A downside scenario is a realistic condition within normal business variation. A stress test is an extreme condition to understand the business's breaking point. Both are useful. Neither should be confused for the other.

SECTION 8

Appendixes

Appendix A — Trigger Validation Checklist

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A valid trigger meets all three conditions. Check each before filing:

[ ] MEASURABLE — states a specific number, not a qualitative description.
    Valid:   "Q1 revenue below $375,000"
    Invalid: "if conditions worsen significantly"

[ ] TIME-BOUND — states when the measurement is taken.
    Valid:   "measured at end of Q1 (March 31)"
    Invalid: "when it becomes clear that Q1 is below target"

[ ] TIED TO CONCRETE ACTION — names specific steps, not a process.
    Valid:   "freeze two open roles; defer CAPEX items B and D;
              reduce marketing budget from $40,000 to $28,000 per month"
    Invalid: "convene management to discuss cost reduction options"

If any condition is not met, the trigger is a sentence in a document,
not a guide to action. Rewrite it before filing the scenario.
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WHERE THIS WORKSHEET COMES FROM

Budget Forecasting Methods

A Budget Never Revised Is Fiction That Gets Funded

by Ibrahim Anwar

This worksheet is one of nine in the *Budget Forecasting Methods* companion worksheet pack. The full pack is grouped into three categories: high-volume worksheets you can run weekly, niche-search worksheets for rare but high-value situations, and specific-case worksheets that walk you through a single concrete scenario.

Every framework, decision filter, and figure used in these worksheets is drawn from the chapters of the source book. The book sets the diagnosis, the worksheets give you the form to act on it.

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