

Year 2 & Year 3 Forecast Adjustment Guide

Common Adjustments for a Three-Year Financial Forecast

Startup Financial Plan LLC | Reference Guide for Small Business Owners

Based on U.S. Bureau of Labor Statistics, Federal Reserve, SBA, and industry benchmarks — July 2026

Once Year 1 of your financial forecast is firmly established, the next step is to project Years 2 and 3. This guide provides a practical reference table of the most common line-item adjustments made when extending a base-year financial model forward. Each adjustment includes a suggested range, a conservative default, and a plain-language explanation of what drives the change. The goal is to give you a defensible, realistic set of assumptions — not a best-case scenario that no lender or investor will believe.

How to use this table: Start with the Conservative Default for each line item. If you have specific market data, a signed contract, or a strong business reason to use a different rate, override the default and document your reasoning. Lenders and investors will ask you to justify every assumption that is above the conservative range.

Section 1 — Revenue Adjustments

Revenue adjustments are the most visible and most scrutinized part of any multi-year forecast. Lenders and investors will compare your Year 2 and Year 3 growth rates against industry benchmarks and your own Year 1 performance. Use the ranges below as a starting point, and be prepared to explain any assumption above the conservative default.

Line Item	Year 2 Range	Year 2 Default	Year 3 Range	Year 3 Default	Driver / Notes
Sales revenue — unit volume growth	5% – 25%	10%	5% – 30%	15%	Startup businesses typically see faster growth in Year 2 as brand awareness builds. Use the lower end for slow-growth markets (food service, professional services) and the higher end for e-commerce or subscription models.
Sales pricing — average price increase	1% – 5%	2%	2% – 6%	3%	Aligns with general CPI inflation (2.9% core CPI, May 2026). Price increases above 5% require a specific business justification such as a premium product relaunch or a documented supply-cost pass-through.
New product / service line added	0% – 20% of Y1 revenue	0%	0% – 30% of Y1 revenue	0%	Only include if you have a concrete plan and timeline. Default is zero until the product is defined. If included, model it as a separate revenue line, not a percentage increase to existing lines.
Other income — grants, pitch competitions	0% – 100% of Y1 amount	0%	0%	0%	One-time income sources should not be projected forward unless you have a specific grant application in process. Default is zero for Years 2 and 3.
Seasonal revenue mix shift	No change to mix	No change	No change to mix	No change	Unless you have a specific reason to expect a shift in your revenue mix by product or season, keep the Year 1 mix constant and apply the volume and price adjustments uniformly across all product lines.

Section 2 — Cost of Goods Sold (COGS) Adjustments

COGS adjustments reflect changes in the cost of the products or services you sell. For product businesses, the primary driver is supplier cost inflation. For service businesses, COGS is often zero or minimal, and the primary cost driver is labor (covered in Section 3). Note that COGS should be modeled as a percentage of revenue or as a unit cost — not as a fixed dollar amount — so that it scales correctly with volume growth.

Line Item	Year 2 Range	Year 2 Default	Year 3 Range	Year 3 Default	Driver / Notes
Unit cost of goods — supplier cost	2% – 6%	3%	2% – 7%	3.5%	Tracks general goods inflation. Food and agricultural products

inflation					can be higher (USDA food price index: +3.1% year-over-year as of May 2026). Electronics and technology products can be lower or flat due to deflationary pricing trends.
COGS as a % of revenue — gross margin improvement	-1% to -3% of revenue	-1%	-1% to -4% of revenue	-1.5%	As volume increases, many businesses achieve modest gross margin improvement through bulk purchasing discounts and supplier negotiation. A 1–2 percentage point improvement in gross margin per year is realistic for a growing startup.
Inventory carrying cost — storage, shrinkage, spoilage	0% – 2% of inventory value	0.5%	0% – 2% of inventory value	0.5%	Relevant for product businesses. Perishable goods (food, cosmetics) carry higher shrinkage rates (1–3%). Durable goods (furniture, equipment) carry lower rates.
Beginning inventory adjustment — days on hand change	No change to days rule	No change	No change to days rule	No change	The days-on-hand rule used in Year 1 should remain constant unless you have a specific reason to change your inventory policy. Volume growth will automatically increase the dollar value of inventory required.

Section 3 — Labor and Payroll Adjustments

Labor is typically the largest operating expense for a startup. Multi-year labor adjustments have two components: rate increases for existing employees, and headcount additions as the business grows. Both should be modeled separately so the reader can see the cost of retention versus the cost of growth.

Line Item	Year 2 Range	Year 2 Default	Year 3 Range	Year 3 Default	Driver / Notes
W-2 employee wages — annual merit increase	2.5% – 5%	3.5%	2.5% – 5%	3.5%	U.S. employers budgeted an average 3.5% salary increase for 2026 (Payscale survey). Mercer reports 3.2% as the median for merit increases. Use 3–3.5% as a defensible default; use 5% only if you are in a high-competition labor market.
1099 contractor / sub-contractor rates	2% – 5%	3%	2% – 5%	3%	Contractor rates tend to track wage inflation but with more variability. Specialized trades (IT, legal, accounting) can increase 4–6% annually. General labor contractors typically increase 2–3%.
New headcount additions — W-2	0 – 2 FTEs	0	0 – 3 FTEs	1	Model new hires as a separate line item with a start month and full annual salary. Do not simply apply a percentage increase to the payroll total — that obscures the

					actual hiring plan. Default is zero until a specific hire is planned.
Payroll taxes and benefits load	No change to %	No change	No change to %	No change	The employer payroll tax rate (FICA, FUTA, SUTA) is set by law and does not change year to year for most small businesses. Benefits costs (health insurance) can increase 5–8% annually but are often not modeled separately at the startup stage. Keep the load percentage constant unless you have specific data.

Section 4 — Operating Expense Adjustments

Operating expenses include all the fixed and semi-variable costs of running the business that are not directly tied to producing a product or service. Many of these costs are contractual (rent, insurance, subscriptions) and escalate at predictable rates. Others are discretionary (marketing, travel) and should be tied to revenue growth rather than a fixed percentage.

Line Item	Year 2 Range	Year 2 Default	Year 3 Range	Year 3 Default	Driver / Notes
Rent / occupancy — commercial lease escalation	2% – 5%	3%	2% – 5%	3%	Most commercial leases include an annual escalation clause of 2–5%, often tied to CPI. Fixed-rate leases may have no increase for the term. Check your lease agreement first; if no clause exists, use 3% as a conservative estimate.
Marketing and promotion	5% – 20% of Y1 amount	10%	5% – 25% of Y1 amount	10%	Marketing spend typically grows faster than revenue in the early years as the business builds brand awareness. A common rule of thumb is to hold marketing at 5–10% of projected revenue. If Year 1 marketing was below that threshold, Year 2 may require a larger increase to reach the target ratio.
Office supplies and general admin	2% – 4%	3%	2% – 4%	3%	Tracks general CPI inflation. This is a low-dollar, low-risk line item for most startups. A flat 3% annual increase is appropriate unless headcount is growing significantly.
Insurance — business liability, property, workers comp	3% – 8%	5%	3% – 8%	5%	Business insurance premiums have increased 5–7% annually in recent years due to claims inflation and underwriting tightening. Workers compensation rates are set by state and class code and can vary significantly.
Legal fees	0% – 10%	0%	0% – 10%	0%	Legal fees are highly variable and event-driven. If you anticipate a

					specific legal event in Year 2 or 3 (contract drafting, IP filing, regulatory compliance), model it as a separate line item. Default is flat unless a specific need is known.
Accounting and tax support	0% – 5%	3%	0% – 5%	3%	Accounting fees typically increase modestly as the business grows and the complexity of the books increases. A 3% annual increase is a reasonable default.
Technology / software subscriptions	5% – 15%	8%	5% – 15%	8%	SaaS subscription costs have increased 8–12% annually in recent years. New tools added as the business grows should be modeled as separate line items, not as a percentage increase to the existing total.
Travel and entertainment	0% – 20%	5%	0% – 20%	5%	Highly discretionary. If Year 1 travel was minimal (startup phase), Year 2 may increase as the business begins attending trade shows or client meetings. Tie to a specific plan rather than a generic percentage if possible.
HR support and recruiting	0% – 25%	0%	0% – 25%	5%	Recruiting costs spike when new hires are planned. Model as a separate event cost (e.g., one month's salary as a recruiting fee) rather than a percentage of the existing HR support line.
Licenses and permits	0% – 5%	2%	0% – 5%	2%	Most business licenses and permits have fixed renewal fees that increase modestly with CPI. Check your specific license requirements for known fee schedules.

Section 5 — Non-Operating Expense Adjustments

Non-operating expenses — depreciation, amortization, and interest — are largely mechanical calculations that follow from the asset and debt schedules established in Year 1. They do not require a percentage adjustment in most cases; instead, they are recalculated based on the asset base and loan balances at the start of each year.

Line Item	Year 2 Treatment	Year 3 Treatment	Driver / Notes
Depreciation — existing fixed assets	Same annual amount as Year 1 (straight-line)	Same annual amount as Year 1 (straight-line)	Straight-line depreciation is constant each year over the useful life. No percentage adjustment needed. If new assets are purchased in Year 2, add their depreciation as a new line item.
Depreciation — new assets purchased in Year 2	Calculate from purchase month	Full year of depreciation	Model new asset purchases as a separate capital expenditure event. Calculate depreciation from the month of purchase using the same useful-life assumption as Year 1 assets.

Amortization — intangible assets	Same annual amount as Year 1	Same annual amount as Year 1	Amortization is straight-line over the useful life of the intangible (software, patents, startup costs). No adjustment needed unless new intangibles are acquired.
Interest expense — existing term loans	Recalculate from amortization schedule (lower than Year 1 as principal reduces)	Recalculate from amortization schedule	Interest expense declines each year as the loan principal is paid down. Use the amortization schedule from App 2 to pull the exact interest amount for each year. Do not apply a flat percentage.
Interest expense — new debt in Year 2 or 3	Calculate from loan start month	Full year of interest	If new loans are planned (equipment purchase, line of credit draw), model them as separate debt events with their own amortization schedule.
Line of credit — interest expense	Varies with draw amount	Varies with draw amount	Line of credit interest is based on the average outstanding balance. Model the expected draw amount and apply the APR. Default assumption: same average balance as Year 1 unless a specific draw is planned.

Section 6 — Balance Sheet Adjustments

Balance sheet adjustments in a multi-year forecast are primarily driven by the income statement results (net income adds to retained earnings) and any new capital events (new loans, new equity contributions, new asset purchases). The table below covers the most common balance sheet line items that require explicit adjustment in Years 2 and 3.

Line Item	Year 2 Treatment	Year 3 Treatment	Driver / Notes
Cash — ending balance	Calculated from cash flow statement	Calculated from cash flow statement	Cash is the result of all inflows and outflows. Do not set it manually — let it be the output of the cash flow model.
Inventory — ending balance	Recalculate using days-on-hand rule applied to Year 2 projected sales volume	Recalculate using days-on-hand rule applied to Year 3 projected sales volume	As sales volume grows, the required inventory balance grows proportionally. Apply the same days-on-hand assumption used in Year 1 to the Year 2 and 3 projected monthly sales volumes.
Accounts receivable (if accrual basis)	Recalculate as % of revenue based on Year 1 collection pattern	Recalculate as % of revenue	If you are on accrual basis, AR typically grows in proportion to revenue. Use the Year 1 days-sales-outstanding (DSO) ratio to project Year 2 and 3 AR.
Loans payable — current and long-term	Reduce by Year 2 principal payments per amortization schedule	Reduce by Year 3 principal payments per amortization schedule	Pull directly from the App 2 amortization schedule. The loan balance declines each year as principal is paid down.
Retained earnings	Year 1 retained earnings + Year 2 net income	Year 2 retained earnings + Year 3 net income	Retained earnings accumulate each year. A startup in its early years will typically show a negative retained earnings balance (accumulated deficit) until the business reaches sustained profitability.
Owner equity contributions — additional	Only if a specific new contribution is planned	Only if a specific new contribution is planned	Do not project additional equity contributions unless the owner has committed to them. Lenders will ask whether the owner is prepared to inject additional capital if the business underperforms.

Section 7 — Quick Reference: Conservative Defaults at a Glance

Use the table below as the starting point for your Year 2 and Year 3 assumptions. Override any default with a specific rate if you have market data or a business reason to support it, and document your reasoning in the forecast notes.

Category	Line Item	Year 2 Default	Year 3 Default
Revenue	Sales volume growth	+10%	+15%
Revenue	Sales pricing increase	+2%	+3%
Revenue	New product / service line	\$0	\$0
COGS	Unit cost inflation	+3%	+3.5%
COGS	Gross margin improvement	-1%	-1.5%
Labor	W-2 wage merit increase	+3.5%	+3.5%
Labor	1099 contractor rate increase	+3%	+3%
Labor	New W-2 headcount	0 FTEs	1 FTE
OpEx	Rent / occupancy	+3%	+3%
OpEx	Marketing and promotion	+10%	+10%
OpEx	Office supplies / general admin	+3%	+3%
OpEx	Insurance	+5%	+5%
OpEx	Legal fees	Flat	Flat
OpEx	Accounting and tax support	+3%	+3%
OpEx	Technology / software	+8%	+8%
OpEx	Travel and entertainment	+5%	+5%
OpEx	Licenses and permits	+2%	+2%
Non-OpEx	Depreciation — existing assets	Straight-line (same as Y1)	Straight-line (same as Y1)
Non-OpEx	Interest — existing loans	Per amortization schedule	Per amortization schedule
Balance Sheet	Inventory	Days-on-hand × Y2 volume	Days-on-hand × Y3 volume
Balance Sheet	Loans payable	Per amortization schedule	Per amortization schedule
Balance Sheet	Retained earnings	Y1 RE + Y2 net income	Y2 RE + Y3 net income

Important reminder: These defaults are starting points, not rules. The most credible three-year forecasts are built from the bottom up — specific hiring plans, specific price increase dates, specific marketing campaigns — not from generic percentage increases applied uniformly to every line. Use these defaults to fill gaps where you do not yet have specific data, and replace them with real numbers as your plan becomes more concrete.

Sources: U.S. Bureau of Labor Statistics CPI (May 2026); Payscale 2026 Compensation Survey; Mercer 2025 Compensation Planning Survey; USDA Food Price Outlook (June 2026); Federal Reserve Small Business Lending Survey Q4 2025; SBA Business Planning Guidelines.