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Financial Budgeting: A Key to A Sustainable Business and Organization

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ABSTARCT

Budgeting is a method of preparing and overseeing a financial and estimated document that estimates the income and expenses over a short or long period of time. Financial budgeting is a key to a sustainable business and organization. The politics of budgeting shows arriving at outcomes where some set goal are seen to be more important than others. Different types of budget which include incremental, activity-based, value proposition, and zero-based with each having its own advantages and disadvantages. The importance of budget being the sustainability of a business are resource availability, good reports on internal goal, prioritization of projects, financial opportunities and access to pivotal plans. Some of the advantages of the budgeting system are easy availability of working capital as the cash receipts and expenses budget ensures that sufficient working capital is available for efficient functioning. Effective coordination cannot be overemphasized as budgeting results in effective coordination between departments as goals of each department are interlinked with each other. It is therefore concluded that the failure to budget may result in conflicting and contradictory plans as well as in wasting corporate resources. Budget slack should be avoided or minimized. Budget slack is the underestimation of revenues.

Key words: Budget, Budgeting, Business and accounting

INTRODUCTION

Budgeting is a method of preparing and overseeing a financial and estimated document that estimates the income and expenses over a short or long period of time. For business executives, budgeting is the main skill for ensuring that organizations and teams have the resources to execute initiatives and reach goals (Cote, 2022). A concise budget consists of projected income and expenses for a given period. After expenses are subtracted from expected or proposed incomes, the balance money can be allocated to projects and initiatives, ensuring you're not planning to overspend. Budgets from previous years could be compared to the company's actual financial allocation and performance, giving an idea of how close predictions were to actual spent (Noble and Jones 2006)

The politics of budgeting shows arriving at outcomes where some set goal are seen to be more important than others. This might be that revenues achieved are, as a result of budgeting choices, directed to certain goals while other important issues receive less financial support and / or less support (Rubin, 2005). Humans never want to relishes the thought of losing out in a process of budgeting and virtually anybody who thinks that a goal is worthy of public funding would be pleased to discover that the majority of individuals making budgeting decisions think otherwise. The common result of the yearly budgeting is that it creates great fear or anxiety while it is going on, and the results of the budgeting often are that conflict is sewn for the next round of t allocations in each succeeding round (Page, 2004)

This paper seeks to address the importance of budgeting and budgeting methods in our business, x-rays the various types and their importance to our day to day business

TYPES OF BUDGETS AND BUDGETING METHODS

There are four common types of budgets that companies use: incremental, activity-based, value proposition, and zero-based with each having its own advantages and disadvantages

1. *Incremental budgeting*

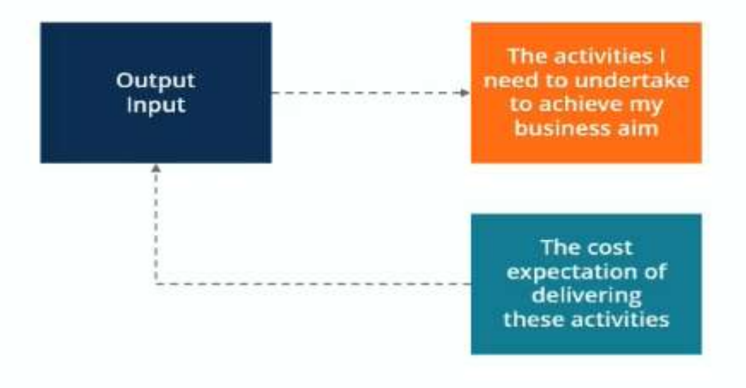
Incremental budgeting takes previous year's actual amount, adds and / or subtracts a percentage to obtain the present running budget. This is the most common type of budget since it is simple and easy to understand. Incremental budget is appropriate to use if the primary cost drivers do not change from year to year. However, there are some problems with using the method (Lee *et. al.,* 2012)

- It is likely to allow inefficiencies in the sense that if a manager knows that there is an opportunity to grow his budget by 10% every year, he would simply make use of the opportunity to obtain or achieve a bigger budget.

- It is likely to result in budgetary slack that is, if a manager overstate the size of the budget that the team needs, it would appear that the team is always under budget.
- It is may ignore external drivers of activities and performance as there could be a very high rate of inflation in certain input costs. Incremental budgeting seeks to ignore external forces and simply assumes the cost will grow by a particular percentage for a running business year.

2. Activity-based budgeting

Activity-based budgeting is a *top – to - down* type of budget that evaluate the amount of inputs needed to support a set target or outputs set by the organization (Smith and Thomas 2004)



3. Value proposition budgeting

Under this system, the budgeter considers why an amount included in the budget; if an item creates value for customers, staff, or other stakeholders; if the value of the item outweighs its cost? If not, then is there another reason why the cost is justified?

Value proposition budgeting is really a mindset about making sure that everything that is included in the budget delivers value for the business. Value proposition budgeting aims to avoid unnecessary expenditures – although it is not as precisely aimed at that goal as our final budgeting option, zero-based budgeting (Leach, 2003)

4. Zero-based budgeting

One of the most commonly used budgeting methods, zero-based budgeting begins by assuming that all department budgets are zero and must be rebuilt from zero point. Accounting managers must justify every single expense as expenses are okay single handedly and automatically. This type of budgeting is very tight, which is aimed at avoiding any and all expenses that are not essential to the business successful operation. This is a bottom – to - up budgeting that is very effective in taking a business to a higher ground (Lee *et. al.*, 2012)

The zero-based method is good to use where there is need for urgent replacement such that in a situation where a business is undergoing financial restructuring and market turn-down that requires it to reduce its budget automatically. Zero-based budgeting is best suited for addressing discretionary costs rather than essential operating costs. Nevertheless, it could be time-consuming as many business agencies use this approach occasionally (Noble and Jones, 2006)

IMPORTANCE OF BUDGETING

Budgeting involves number crunching, attention to detail, and making informed decisions about allocation of funds

1. It ensures resource availability

One of the primary functions of budget is for an organization that has enough resources to meet its goals. By planning financially in advance, helps to determine which teams and initiatives require more resources and areas where you can cut back on.

2. It Can Help Set and Report on Internal Goals

Budget for an upcoming year is not just o allocate money for spending; but to determine how much revenue would be needed to reach the business goals.

One can use budget to set business wide and team monetary goals that align with them. This is especially needed when using activity-based budget, but it is beneficial no matter what type you use.

Financial goals should be attainable enough that you count on them to inform the rest of your budget allocations.

One can also use budgeting to update workers on progress and revisit the next years goals; Tracking progress, or lack thereof, allows you to align your workers and plan for growth in the following year.

3. It helps to prioritize project

A byproduct of the budget process is that it requires prioritizing projects and initiatives. When prioritizing, consider the potential profit investment for each project, how each aligns with your company's values, and the extent they could impact broader financial goals.

4. It Lead to Financing Opportunities

If you work at a startup or are considering seeking outside investors, it is important to have documented budget information. When deciding whether to fund a business company, investors highly value its current, past, and predicted financial performance.

Providing documents for previous periods with budgeted and actual spend can show your ability to handle a company's finances, allocate funds, and pivot when appropriate. Some investors may ask for your current budget to see your predicted performance and priorities based on it.

5. It Provides a Pivotal Plan

A budget is a financial roadmap for the upcoming period; if all goes according to plan, it shows how much should be earned and spent on specific items. Yet, the business world is anything but predictable. Circumstances outside your control can impact your revenue or cause priorities to change at a moment's notice. A budget gives one a plan; maintaining an agile mindset enables you to pivot that plan and help lead the organization through turbulent times.

ADVANTAGES OF BUDGETING AND BUDGET CONTROL

Budgeting eliminates uncertainty as it provides a planned approach to every activity. Result of team effort and various brains since it is a collective effort by the top management; it is made by several heads keeping in mind organization objectives. It provides optimum use of capital resources. There is easy availability of working capital as the cash receipts and expenses budget ensures that sufficient working capital is available for efficient functioning. Effective coordination cannot be overemphasized as budgeting results in effective coordination between departments as goals of each department are interlinked with each other .Responsibility can be pinpointed as it can pinpoints a person on whom a responsibility can be fixed. Spotlight on deviations can be seen and areas of improvement can be identified to take suitable corrective action. The Budgeting system provides a benchmark for actual performance and shows the path to achieve the standard. Meeting budgets can be a good incentive for employees who get rewards and recognition on achieving targeted budgets (Tyagi, 2017)

DISADVANTAGES OF BUDGETING

Budgets are estimates hence can never be accurate as Inflation and rapidly changing business environment tend to distort budget data. Effective planning, implementation is crucial as i cannot guide as to what action should be taken and proper system of supervision and control is essential otherwise the budget will be ineffective. Budgeting can face the danger of inflexibility and everyone may think that without adherence to it, they will be called inefficient. Sometimes budgets may be misused by bosses to find faults in employees and restrict performance rather than improve it and the initiative and creativity of an employee may be hampered if budget is the only yardstick. Budgeting is a time consuming process and involves expenses and its goals may lead people to supersede organization goals. The Success of budgeting depends on the motivation of people involved and it should be a gradual and cooperative exercise. Budgeting being just a pathway and does not guarantee successful implementation, it helps arrive at important management decisions however if used in isolation may lead to harmful consequences for the business (Tyagi, 2017)

CONCLUSION

A budget should be based on norms and standards. The budget should be coordinated, integrated, organized, systematic, clear, and comprehensive to accomplish optimal results. The budget preparation, review, and evaluation process must be facilitated. An orderly budgeting process will result in less cost, less man -hours, and minimization of conflict and turmoil. It will require less revision at a later date. The budget process must consider input -output relationships. The budget aids in anticipating problems before they become critical. Short-term budgets should be used for businesses subject to rapid change. A budget is a tool for planning and for "what-if" analysis. It aids in identifying the best course of action.

As it is in the computer world—garbage in, garbage out—so it is with budgeting. If forecasts are inaccurate so will be the projections, resulting in bad management decisions to the detriment of the firm. A manager must be cautious when analyzing past experience. Unforeseen circumstances such as economic downturns and future innovations have direct inputs on current operations. A manager deviating from a budget target must explain why and, of course, is on the defensive. Without proper justification for missing targets, the manager may be dismissed.

The failure to budget may result in conflicting and contradictory plans as well as in wasting corporate resources. Budget slack should be avoided or minimized. Budget slack is the underestimation of revenues.

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