



BUGETING AND SHORT TERM **PLANNING**

Module Name: Management Accounting

Module code: LCBB5002

Lecture Name: Winifred Soribe

Student name: Svetlin Pavlov
Student Number: 1814104

Contents

Introduction	2
Types of Budgeting and Business Decision Making process	2
Budgeting Systems and Business Decision making.....	4
Conclusion	5
Reference	7

Introduction

In simple terms, budgeting is the process of projecting or predicting the details of future expenditure and income for a specified period in the context of all known factors (Huang, 2019). One of the important reasons why companies participate in detailed budgeting is to guide decision-making (Huang, 2019). Making the right decision is even more important when the rapidly changing conditions of our present business world are considered, for example, business conditions during the current Covid 19 pandemic. As such, the types of budgeting used must allow flexibility in decision making (Hint *et al.*, 2018). For instance, an IT company, Softconic, specializing in providing word processing software most of the time, might need to switch their focus to enhancing their collaborative software, C-Talk, during the pandemic, because there is more demand for C-talk than for word processing platforms. Using this scenario and other real-life examples, this essay will explore how budgeting helps business managers convert medium plans into short term plans to capitalize on short term opportunities. The essay will also compare the applicability of different budgeting styles in the above scenario.

Types of Budgeting and Business Decision Making process

There are many definitions and types of budgets. However, when the concept of planning and decision making is considered, two major themes emerge, static and flexible budgeting (Popesko *et al.*, 2017). Static budgeting involves incorporating forecasted values about the expected revenue and expenditure before the period in consideration even begins (Esakova *et al.*, 2020). A flexible budget on the other hand accounts for fluctuations in operational parameters and revenue when compiling budgets (Silvester, 2017). The major benefit of static budgeting is that it allows for stability in decision making as it remains unchanged even in the face of fluctuations (Esakova *et al.*, 2020). This makes it perfect for measuring overall financial progress made by a company across a period and for evaluating long term financial goals (Ross, 2020). But flexible Budgeting on the other hand allows the company to monitor the relevance of their decisions in the context of current flux in business changes (Silvester, 2017). Therefore when trying to maximize short term opportunities with a

massive impact on business operations like the Covid 19 pandemic, flexible budgeting offers more opportunities for adaptations.

When the situation of Softconic is considered, their fixed/static budget has predicted that 2.5 million new subscribers will be added which will generate a net profit of about £63 million. But their flexible budget prediction suggested that between 1 - 3 million subscribers will be added during the same period with varying levels of profits, ranging from £5 million to £80 million. To analyze, it can be said that the £63 million profit suggested by the static budget can be used as the benchmark to measure the overall performance of Softconic at the end of the fiscal year. However, this budgeting type will not apply to the current unpredictability in-market performance. This is because planning based on the expected £60 million profit leaves the company vulnerable to lowered demands that the market might generate. Therefore, it is advised that Softconic should utilize its flexible budget. This is because the flexibility allows easy absorption of the shock of demand instability that is the "new normal" in the current pandemic (Wnuk-Pel & Christauskas, 2018). For instance, lower demands for goods in the commodity market can make companies to hold less collaborative team meetings to address falling demands. This is because demands dropped not because of under-performance but because of the pandemic. Thus smaller management meetings might be made using C-Talk, to minimize costs and ensure profitability. This is make result in lower than expected demand for C-talk. On the other hand, a cure for Covid-19 might be found quickly, leading to the resumption of in-person meetings. This will force Softconic to revert to the word processing, hence undermining their previous shift in investment. All in all, flexible budgeting helps cover all these possible situations and many more because it allows the real-time monitoring of operational trends and revenue (Wnuk-Pel & Christauskas, 2018).

This flexible approach was adopted by Samsung. In April 2020, Samsung stated that it will focus on optimizing resource allocation during this pandemic period (Samsung, 2020). Specifically, the company stated that they will be engaging in flexible investments with no precise profit margin figure for the next quarter, due to the coronavirus pandemic (Samsung, 2020). This flexible decision making is reflective of a flexible budget plan that allows the restructuring of their resources across the board to minimize risk and absorb much of the pandemic's shock. Thus it can be seen that

flexible budgeting is what is most applicable during uncertain times like the current pandemic. Although there remains a place for static budgeting in post fiscal year performance evaluation

Budgeting Systems and Business Decision making

Budgeting systems are important in making decisions in an organization. However, whatever system is adopted, a realistic and clearly defined goal needs to be set (Brink *et al.*, 2018). Generally, there are three systems used to develop budgets. They include: imposed, negotiated, and participative systems of budgeting. In imposed budgeting, the higher-up executives determine the goals and financial targets of the company and the managers simply comply (Brink *et al.*, 2018). Negotiated budgeting on the other hand is a hybrid of the top-down approach of the imposed budgeting system and the bottom-up approach of the participative system (Daumoser *et al.*, 2018). Furthermore, participative budgeting is a bottom-up approach that allows the employees to recommend budgetary targets and plans to managers (Dorfuss, 2016). The managers then adapt and refine the suggestions with the executives (Dorfuss, 2016). In this situation, all the employees and departmental managers feel more in-tune with the budget's plan as they were involved in its development (Dorfuss, 2016). This is deeply contrasted with the top-down approach where employees might feel like the plans were forced on them and thus stimulating lesser engagement (Daumoser *et al.*, 2018). However, in times of crisis and financial turnarounds, imposed budgeting can be used to steady the ship and gain perspective across the board (Brink *et al.*, 2018).

In light of the current ravaging pandemic, participatory budgeting gives an edge to organizations by helping them stay ahead of the curve. In other words, a firm whose business planning incorporates input from every part of the organizational structure has a higher chance of recognizing the fluctuations that might greatly impact their outlook early (Al Hudithi, 2017). For example, inputs from the sales managers and representative might have earlier informed the management of Softconic in anticipating the changes in demand that the pandemic will initiate and the various ways it has begun to shape the demands, behaviors, and thoughts of their customers.

Likewise, the technical support teams would have earlier fashioned means of increasing and sustaining productivity beforehand. Al Hudithi, (2017) suggested that participative budgeting allows firms to be more proactive in their reactions to changes in the business world, as depicted in the scenarios explained above. For example, some staff members of Facebook have opined for more resources to be allocated to fighting hate speech and other harmful content on their platform (the New York Times, 2020). But the imposed budgeting system of the management determined that the level of resources apportioned is enough for now. Eventually, in light of the human rights equality movement that suddenly gripped the world in recent times, Facebook suffered a loss when some of their biggest customers complained about their practices and followed through by suspending their advertisement contracts (Kim and Fung, 2020). However, adopting a participatory approach could have enabled Facebook to proactively avoid this effect.

However, the pitfall of engaging in participative budgeting is that it allowing excessive inputs from all angles that can derail the planning and budgeting process (Antikainen *et al.*, 2017). This is because there might be contrasting inputs from the participating employees thus making the company lose focus. It can also make the business engage in excessive compromises that might water down their financial targets and lead to underperformances. Thus the onus rests on the managers to be able to balance the benefits of participative budgeting with its challenges.

Conclusion

The uncertainty of the current business landscape has forced businesses to be alert to the dangers of current times as well as being able to adapt and utilize short term opportunities. The essay demonstrated that flexible budgeting is better used to achieve this target than static budgeting. However, it was also shown that static budgeting should be used to evaluate long term goals and yearly financial performance. Additionally, it was shown that participative budgeting helps companies to be proactive about the dynamics of change in the business landscape, thus insulating them from devastating changes and preserving survival. All in all, it is clear

that the survival of all firms in modern times is dependent on making the right business decisions which are informed by choosing the right budgeting style and system.

Reference

1. Al Hudithi, F. A. S. 2017. *Social Capital and Participative Budgeting: A Process Thinking Perspective* (Doctoral dissertation, University of Hull). Available at: <https://pdfs.semanticscholar.org/9777/4d79a7f90a67cde30d288cc0e62cd4ca2991.pdf>
2. Antikainen, E., Sajasalo, P. and Auvinen, T. 2017. *Participative Strategy Work. Navigating Through Changing Times: Knowledge Work in Complex Environments*.
3. Brink, A. G., Coats, J. C. and Rankin, F. W. 2018. Who's the boss? The economic and behavioral implications of various characterizations of the superior in participative budgeting research. *Journal of Accounting Literature*, volume 41, 89-105.
4. Daumoser, C., Hirsch, B. and Sohn, M. 2018. Honesty in budgeting: a review of morality and control aspects in the budgetary slack literature. *Journal of Management Control*, Volume 29, Issue 2, 115-159.
5. Derfuss, K. 2016. Reconsidering the participative budgeting–performance relation: A meta-analysis regarding the impact of level of analysis, sample selection, measurement, and industry influences. *The British Accounting Review*, volume 48, issue 1, 17-37.
6. Esakova, E. E., Nalimova, Z. F. and Yakubenko, I. A. 2020. Improving the Relevance of the Budgeting System in the Transition to the Digital Economy Model. In *International Session of Factors of Regional Extensive Development (FRED-2019)*. Atlantis Press.
7. Hint, M. Ş., Popa, M. A., Trif, M. and Bădescu, M. 2018. New dimensions of managerial accounting and its influences in an unstable environment. *The Annals of the University of Oradea, Economic Sciences*. Volume 27, Issue 1, 181- 191
8. Huang, W. 2019. Developing a Better Planning, Budgeting, and Accounting System. In *Built on Value* (pp. 303-328). Palgrave Macmillan, Singapore.
9. Kim, A. and Fung, B. 2020. *Facebook boycott: View the list of companies pulling ads*. CNN, July 2. Available at: <https://edition.cnn.com/2020/06/28/business/facebook-ad-boycott-list/index.html>
10. Popesko, B., Novák, P., Dvorský, J. and Papadaki, Š. 2017. The maturity of a budgeting system and its influence on corporate performance. *Acta Polytechnica Hungarica*, Vol 14, issue 7, 91-104.
11. Ross, T. K. 2020. Budgeting for Results. *The Health Care Manager*, Volume 39, issue 1, 24-34.
12. Samsung, 2020. *Samsung Electronics Announces First Quarter Results 2020*. Available at: <https://news.samsung.com/global/samsung-electronics-announces-first-quarter-2020-results>
13. Silvester, K. J. 2017. Faith's Country Primitives: An Excel Project In Flexible Budgeting And Standard Cost Analysis. *Journal of Business Case Studies (JBCS)*, volume 13, issue 4, 85-98.
14. The New York Times. 2019. *Read the Letter Facebook Employees Sent to Mark Zuckerberg About Political Ads*. October, 28. The New York Times. Available at: <https://www.nytimes.com/2019/10/28/technology/facebook-mark-zuckerberg-letter.html?action=click&module=RelatedLinks&pgtype=Article>
15. Wnuk-Pel, T. and Christauskas, C. 2018. Analysis of Operational Budgeting Practices in Polish and Lithuanian Companies. *Transformations in Business & Economics*, Vol. 17 Issue 3, p102-124.