Chapter 12
Budgeting Technique of Strategic Management

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ABSTRACT

The industrial companies’ activities must take into account the existence of a balance between income and expenses. In this regard, the budget is the basic tool, and budgeting becomes a systemic economic practice in allocating the financial resources to achieve the objectives set forth by the company strategy. This chapter discusses budgeting as a technique of strategic management. In the companies’ activities of budgeting, the following may be used: general and partial budgets; budgets prepared by departments; budgets prepared by products, projects, and activities; fixed and flexible budgets; etc. Thus, to start with, the fundamentals of budgets are analysed, and afterwards, based on them, industrial companies’ budgets are elaborated. At the end of this chapter, the budgets thus elaborated are used as techniques of the industrial companies’ strategic management.

THE FUNDAMENTS OF BUDGETING

The Budgeting and the Budget of the Firm

The firm’s activity is recommended to develop in a permanent equilibrium between incomes and expenses. In the actual stage of transition of Romanian economy, the firms can not maintain this equilibrium because the expenses determined by the achievement of production overtake the level of the incomes obtained from the selling of production even when certain branches of activity are subsidized from the public budget.

In these conditions, finding the methods that allow the sizing and control of the equilibrium relation between expenses and incomes represents a problem with which the firm’s management confronts. From this point of view the budget can become an instrument of correlation and especially of turning to good account the relation between incomes and expenses.

Budgeting becomes a systematic economic practice that assumes the development of a pro-
cess of formal assignment of financial resources that aim at the achievement of some established objectives for the future periods.

Nowadays budget is a plan expressed in money through which the shares of the afferent resources for achieving an aim by a certain managerial subdivision are estimated in a financial expression.

Budgets are established on short run periods, on a year with a breakdown by quarters, months, weeks and even day as for each job.

When the firm's activities are varied, budgeting adapts to this situation through establishing some flexible budgets, elaborated on several levels of activity.

Budgeting resides in presenting in a scheduled form the data that make up the budget.

Budgeting is characterized by:

- Planning and coordination because budgeting works within the framework of a long term, overall objectives to produce detailed operational plans for different sectors and facets of the organization. This is expressed in the form of a Master Budget, which summarizes all the supporting budgets. The budget process forces managers to think of the relationship of their function or departments with others and how they contribute to the achievement of organizational objectives;

- Authority and responsibility, because budgeting makes it necessary to clarify the responsibilities of each manager who has a budget. The adoption of a budget authorizes the plans contained within it so that the management by exception can be practiced, meaning that a subordinate is given a clearly defined role with the authority to carry out the tasks assigned to him and when activities are not proceeding to plan, the variations are reopened to a higher level;

- Communication, because the budgetary process includes all levels of management. Accordingly it is an important avenue of communication between top and middle management regarding the firm's objectives and the practical problems of implementing these objectives and, when the budget is finalized, it communicates the agreed plans to all the stuff involved;

- Control, because this aspect of budgeting is the most well-known and is the aspect most frequently encountered by the ordinary stuff member. The process of comparing actual results with planned results and reporting on the variations, which is the principle of budgetary control sets a control framework which helps expenditure to be kept within agreed limits;

- Motivation, because the involvement of lower and middle management with the preparation of budgets and the establishment of clear targets against which performers can be judged have been found to be motivating factors.

Budgeting makes necessary the establishment of budgets that allow the presentation in figures of all forecasts on the activity of the firm.

In essence it arises the problem of creating some autonomic subsystems called cost centers that should focus on the optimization of the use of resources and obtaining profits.

The cost center is an identifiable function or part of the organization for which costs can be identified.

A profit center is an extension of this idea on a larger scale, where not only costs are identifiable but also profits.

The formal definition is that of a part of a business accountable for costs and revenues.

A budget center is defined as a section of an entity for which control may be exercised and budgets prepared.

Thus it will be apparent that a budget center may be a cost center, or group of cost centers or it may coincide with a profit center.

Because of its size it is likely that a typical profit center would consist of a number of budget centers.