Chapter 8

The Use of Budgets in Forecasting the Activity of the Firm

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ABSTRACT

In the current definition, the budget is a financial plan by means of which the shares of all relevant resources related to achieving an objective within a certain organisational subdivision are provided in the financial expression. The budget is the result of the budgeting activity that is characterised by: planning and coordinating, authority and responsibility, communication, control, etc. Any budget meets several functions and namely: prediction, control, providing the financial balance, etc. Budgeting the company’s activity involves preparing of budgets related to its functions, namely: the budget of production that includes the manufacturing budget, the budget related to machines and equipment, the budget related to the labour force, the budget of raw materials and consumables, the overall production budget, the commercial budget, meaning the seller’s budget, the budget of sales managers, the commercial manager’s budget, the commercial budget itself, the budget of the investments by emphasising the budget of the commercial and industrial investments, the budget of the research-development activity by emphasising the expenses related to this activity, the budget of treasury, meaning the budget of revenues, the budget of payments and correlation between them, etc. In the activity of the company’s manager, applying the management by budgets involves going through several stages: sizing the objectives in financial form, preparing the system of budgets at the company’s level by fields, organising the information system related to budgets, the control of budgetary system, etc.

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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 cannot 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 (Călin & Man, 2005).

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 process 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.
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