



## Role of budgeting process in achieving organizational goals as a strategic planning tool: a case at Harischandra Mills Plc

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### Abstract

Budgeting is the key element of strategic planning in corporate goal achievement as it guides and guides the organization to work out within restrictions and limitations. An excellent budget directs the organizational resources to reach a higher growth through achieving objectives in this most dynamic environment. However, it is rare to find researches conducted to investigate the contribution of budgeting process in goal achievement in manufacturing organizations and the study was conducted to examine the role of budgeting process in achieving organizational goals in reference of Harischandra Mills Plc using case study approach. The study purpose is to investigate the contribution of budgeting process as a strategic planning tool on company's corporate goal achievement. Data was collected for the study using depth interviews and discussions with the top and middle level managers and other relevant officers in the company, focusing the study model. Additionally Annual reports and budget reports were used. Collected data was analyzed specially using qualitative approach, and for further clarification and verification variance analysis, ratios and trend analysis were also used. The study results found that the company's budgeting process makes considerable positive influence on achieving organizational goals, though the company have not a properly designed strategic planning process. Further the findings suggested to pay special attention on strategic planning process, and integration of strategic planning and budgeting for better achievement of corporate goals.

*Keywords:* Budget process; Dynamic environment; Organizational goal; Strategic planning

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### Introduction

The business world today is more dynamic, challenging and competitive and the resource availability is also limited. The management needs to face these diverse challenges by the maximum utilization of their resources to achieve their goals and objectives properly. Naylor (1981) says that effective planning and control are crucial for achieving organizational goals and objectives. Effective planning ensures that goals are selected with care and effective controls ensure that the selected goals are implemented appropriately. Budgets perform an important role both in planning and control in achieving organizational goals. Budgeting has become an essential and inherent part in organizational planning, and planning process starts with the establishment of organizational goals and devising strategies for goal achievement (Anthony, 1965; Blumentritt, 2006). The process involves preparation of strategic planning, short term planning and converting them into annual budget. Buckley &

Mackenna (1972) says that the process of budgeting consists of planning, controlling, coordinating and motivating through money values, members of departments within an organization. According to Blumentritt (2006) and Naylor (1981) the top management of an organization decides the direction where the organization is trying to go in a certain period of time including vision, mission, corporate goals, long-term and short-term goals by their planning process. To achieve these goals and objectives, budgetary plans are developed and implemented. Hence budgeting process is a vital important tool which can be used properly in the organizational context to perform their activities. Blumentritt (2006) recognizes further the need for organizations to integrate strategic planning and budgeting for corporate goal achievement. However the selected Company treats strategic planning and budgeting as separate elements and prepares budgets specially to achieve short term goals making only short term planning. Therefore considering all above situations, it

is worthwhile to investigate the role of budgeting process in corporate goal achievement as a strategic planning tool with reference to a leading manufacturing company called Harischandra Mills Public Limited Company in Sri Lanka. The study investigates the research questions of does the budgeting process affect to the corporate goal achievement as a strategic planning tool. The main purpose of this study is to investigate and identify the contribution of budgeting process in corporate goal achievement.

### Materials and Methods

The research is conducted as a Case study and the primary data for the study was collected from interviews and discussions with top level and middle level managers and other relevant officers of Finance division focusing on all the variables of the study model including planning process, goal setting process, budgeting and goal implementing processes. The secondary data was collected reviewing documents, annual reports, budget reports, variance analysis reports of the company and relevant published books and articles etc. Data was analyzed specially using qualitative approach based on the study model developed by the researcher as depicted in Figure 1. The study compares and contrasts the actual

functioning of role of budgeting process which facilitates in achieving organizational goals as a strategic planning tool with the Study model, to clarify the way and the extent to which the budgeting process affect the company to achieve its corporate goals. Quantitative measures of variance analysis, ratios and trend analysis were also used for further clarifications and verifications.

The study model has been developed by reviewing literature by the researcher and the study model explains the role of budgeting process as a strategic planning tool in corporate goal achievement. Naylor (1981) explains that Budgeting is a part of the planning process and the annual budget for a company should not be formulated until after the strategic plan has been developed, and goals, objectives been determined. Blumentritt (2006) and Wilhelmi and Kleiner (1995) explain that in strategic planning, long term objectives are developed which are to be achieved within more than a year and to achieve them short term objectives are developed which are to be achieved within a year. In the short term planning, budgeting is developed as a strategic tool in implementing short term goals which ultimately affect the long term goals attainment (Anthony, 1965; Blumentritt, 2006). To measure the achievability of them, Variances analysis, Ratios and Trend analysis were used.

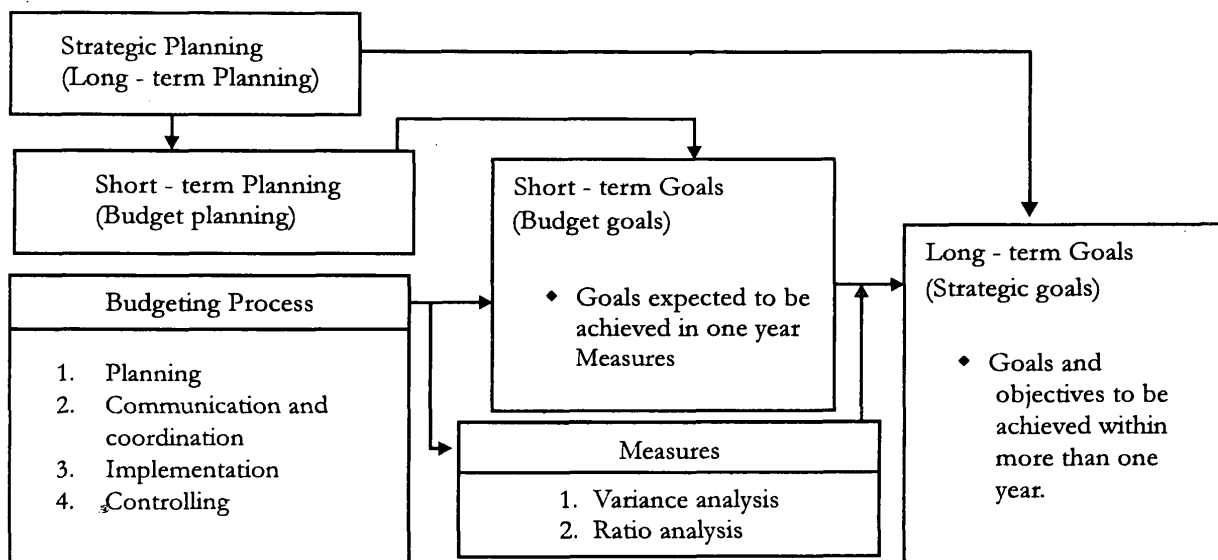


Figure 1. The Study Model

### Resultes and discussion

*Planning process of the company: Budgeting process as a strategic planning tool*

Naylor (1981) recognizes that Budgeting is a part of the Strategic planning process of an organization which is very crucial function. Lucey (1996) defines

Strategic planning as Formulating, Evaluating and Selecting of Strategies for the preparing of long-term plans of action to attain Objectives. According to the planning model of Drury (2004) both long term and short term planning should be done and budgeting process is established for implementing especially

short term goals in order to achieve long term goals of an organization. Budgets are prepared for achieving objectives and Ackoff (1981) defines objectives as desired outcomes of behavior which may be unattainable but must be approachable within a planning period. Blumentritt (2006) identified that the companies need to engage in strategic planning in gaining proper contribution from budgeting and large portion of companies are not doing that. HM Plc also does not engage in the strategic planning and does not have a vision. However company have a mission and pre-set corporate goals which are, Provide a fair return to share holders while safeguarding their investments, Provide maximum benefits to the employees and produce quality products using local raw materials. According to Blumentritt (2006) integration of budgeting and strategic planning is essential in achieving organizational goals from budgeting as a strategic planning tool by implementing short term planning. According to Lucey (1996) Short term planning or budgetary planning is the process of preparing detailed, Short-term plans for functional activities and departments of the organization thus converting the long-term corporate plans into action. However HM Plc develops only short term goals of maximizing sales and profit, and minimizing cost to be attained within a year in their short term planning process, though the short term planning process should be practiced as a part of strategic planning process. Hence company does not do long term planning to achieve long term goals and prepare budgets specially as a mean of achieving short run goals (Blumentritt, 2006).

*Budgeting process of the company: Role of the budgeting process*

A proper budgeting system is more than just a process of collecting and accumulating numbers and is a map that can guide an organization to implement its activities (Jehle, 1999). A budget is a plan of action. It is a document of formal planning and control and be a quantitative statement of goals and objectives expressed in monetary terms (Khan & Jain, 2000). HM Plc prepares budgets annually and monthly and preparation of monthly budgets is very important for the company as it produces seasonal products as kurakkan flour, gingerly roll, ulundu flour ...etc, because the production and other expenses to be incurred vary based on availability of Raw Materials, Production capacity and Sales Demand. Therefore preparing monthly budgets is highly effective for managing resources and to get the maximum benefits

by achieving Annual Goals (Drury, 2004) Considering the budgeting process of the company, it does not have both a well structured budget committee who is responsible for the budgeting process and a budget manual that have been developed to guide the budgeting process in preparing budgets, which are the fundamentals of budgeting process. Drury (2004) says that decision with regarding budgeting should be done by budget committee based on a budget manual. Company's budgeting process consists of planning, communication & coordination, implementation and control (Buckley & Mackenna, 1972). Considering the HM Plc, main role of decision making of budgeting process is done by the Managing director (MD). Based on all the collected data from sales persons of sales tertiary, production capacity, resource availability, costs of production and past financial information, MD determines the annual and monthly budgeted sales, profit and cost in the budget planning stage with the view of maximizing sales and profits, and minimizing cost in short run. MD prepares a rough budget and communicates the budget targets to the production department heads, since those Middle level managers are not participated in the budget planning and administration process. If there are any differences between budget targets and production capacity, those differences can be eliminated by it. In communicating and coordinating activities, budget serves as a vehicle through which the actions of different parts of the company can be brought together and reconciled in to a common plan (Drury, 2004). MD reconciles the rough budget if necessary and coordinates the activities so as to achieve budgeted targets and provides it to the Assistant Accountant through Chief Finance Officer to prepare detailed budgets. With rough budget given by the MD and collecting further required data from the sections of Production, Human Resources, Sales & Marketing and Accounting and Finance, Accountant prepares monthly and annual detailed functional and master budgets for each product, production department and company as a whole. The functional budgets prepared are Sales, Raw Material (RM) requirement, RM consumption, Direct Labor (DL), Variable Over Head (VOH), Fixed Over Head (FOH), Capital Expenditure and other expenses budgets such as Administrative Over Head (AOH) and Selling and Distribution Over Head Budget (SOH). In the preparation of budgets, Sales budget is prepared first with the data given by the MD. Before preparing RM, DL, VOH, FOH, AOH and SOH budgets,

Assistant Accountant prepares standard cost cards for each product by collecting cost data from relevant sections as the costs may be changing throughout the year, because company's products are seasonal and hence prices can be changed. It includes RM, DL, VOH, FOH, Gross profit and Net profit per unit, Sales and other expected target expenses as a whole for each product and section within the targets given by the MD. After preparing cost cards those figures are used to prepare the functional budgets and finally master budget is prepared aggregating functional budgets including Budgeted Income Statement, Balance Sheet and Cash Flow. After preparation of Budgets, they are implemented monthly taking required control actions. In the controlling, actual results are compared with budgeted & standard results (Actual quantities in to standard price) and identified the variances of goal achievements. If the goals are not achieved, control

actions are taken, evaluate performances & continue operations adjusting the coming budget. The main purpose of budgeting is the achievement of short term goals.

#### *Achievement of Short term Goals through Budgeting*

Because of following a properly designed budgeting process as explained above to have guidance and direction which is strictly developed to attain short term goals, HM Plc could be successful and it is shown by Table 1 and Figure 2 comparing Actual, - Budgeted and standard (Actual quantities in to standard price) figures of Sales, Profits and Costs over last 08 years. Studying the figures of Actual, Budgeted and Standard Sales, Profit and Cost in the Table 1, it can be seen that budget supports directly and positively to the attainment of short term goals of the company.

Table 1 Comparison of Actual, Budgeted and Standard Sales, Profit and Cost Rs. '000'.

Description/ Year	2001	2002	2003	2004	2005	2006	2007	2008
Actual sales	953010	916816	939817	850879	891549	1085878	1372860	2254144
Budgeted sales	1012653	905263	995014	1200563	875275	1395987	1558796	1758975
Standard Sales	986971	905007	975890	1105500	857580	1158901	1457896	1875604
Actual Profit	117899	107382	100825	113194	80000	194757	240000	233000
Budgeted profit	99758	103588	109256	105836	100126	175253	195869	205650
Standard Profit	95879	105780	998750	108970	958360	190575	235780	216530
Actual Cost	384314	405466	455811	486497	584245	682489	837333	1104532
Budgeted Cost	498675	456789	426987	607584	657584	809850	845604	897500
Standard Cost	452650	425890	405690	589600	558790	758360	905890	897505

Source: Annual Reports (2001-2008)

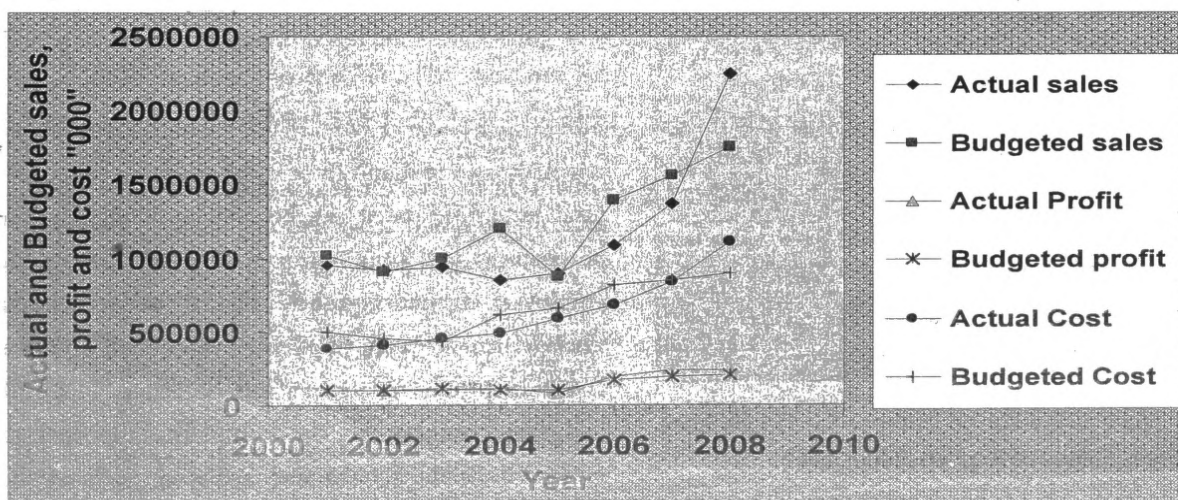


Figure 2. Trend analysis of Actual and Budgeted Sales, Profit and Cost Rs. '000'.

Source: Annual Reports (2001-2008)

*i. Maximize Sales*

An increase of company's actual sales can be seen looking at sales increasing trend in the Figure 2 along with the budgeted sales. It shows that budget provides a direction allowing immaterial fluctuations to maximize sales and hence actual sales have been increased gradually. Thus budget supports to achieve sales maximizing goal.

*ii. Maximize Profits*

Profits have been increased in line with budgeted amounts as per the profit increasing trend in Figure 2 and it shows that budget provides an ideal direction to increase and maintain expected level of profit regularly.

*iii. Minimize Costs*

Looking at the Company's cost flowing trend in the Figure 2, it has been increased over last eight years in line with the budgeted amounts. Though the cost has been increased, it has been increased in order to the budgeted amounts. Therefore in achieving the objective of minimizing cost objective, company is successful since the increase of cost is not a problem of budgeting and cost is similar to the budgeted (expected) amount.

Thus company is able to achieve short term goals with the support of budgets as it directs the company to face unseen future circumstances at best with what they have.

*Role of budgeting in Corporate Goal achievement as a Strategic Planning tool*

Since the company does not have strategic planning, it does not have integration of strategic planning and budgeting and proper long term goal setting process. However there are corporate objectives which support to achieve the mission. Hence researcher tested the achievability of corporate goals of increase returns to share holders and maximize benefits to employees through HM Plc's budgeting process. These objectives can be achieved by earning high profits, which is one of the short term goals and it is achieved through budgeting process as shown in Table 1 and Figure 2, and it affects to corporate goal attainment directly and further affects planning of expenses in budget to achieve these corporate goals.

*i. Increasing returns to share holders*

By earning higher profits and planning expected dividends to be paid using the budgeting process, company could provide following benefits to the shareholders and looking at the dividend percentages and the dividend distributing trend in the Table 2 and Figure 3, the achievement of this objective can be seen. However in 2008 it has been reduced because of a decision of the management. Generally dividend paid has been increased.

Table 2. Benefits provided to the Share holder

Year	2000	2001	2002	2003	2004	2005	2006	2007	2008
Dividend Rs. '000'	3839	5279	5276	5278	5759	9598	9598	19196	14,397
% of Value Added	4.04%	3.89%	3.67%	4.19%	4.29%	6.84%	5.27%	9.39%	5.48%

Source: Annual Reports (2000-2008)

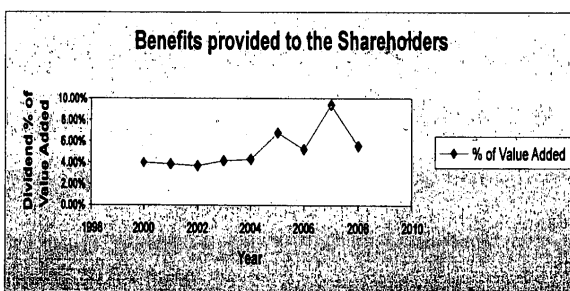


Figure 3. Trend analysis of benefits provided to the Share holder (Source: Annual Reports, 2000-2008)

*ii. Maximize benefits to the employees*

Considering this goal, company has given higher benefits to the employees including salaries, bonus, and

other fringe benefits allocated by the budget, and actual payment is more than 1/3 of company value added and total expenses, and it can be seen by looking at the percentages and trend of providing benefits to the employees as per Figure 4. Hence, budget directs management to plan, implement & control activities and earn profits to achieve this objective. Thus the budgeting process of the company supported to achieve both short term and corporate goals of the company, though there are some weaknesses in the company planning and budgeting process due to not having strategic planning process.

Table 3. Benefits provided to the employees

Year	2000	2001	2002	2003	2004	2005	2006	2007	2008
Employee paid									
Rs. '000'	44575	45406	54882	58821	64347	23092	30480	27720	122,790
% of value added	46.52%	33.4%	38.1%	46.0%	47.9%	53%	47.4%	51.7%	46.7%

Source: Annual Reports (2000-2008)

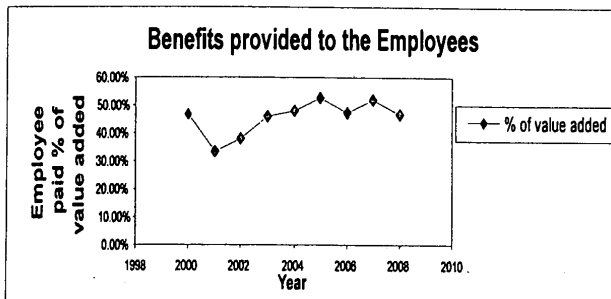


Figure 4. Benefits provided to the employees (Source: Annual Reports, 2000-2008)

### Conclusion

Company has no strategic planning and does only short term planning. However budget is prepared as an element of achieving short term goals of Maximize sales, profits and Minimize cost. However the researcher tries to understand the achievability of corporate goals by the Company's budgeting process. Hence, looking at the figures and analysis, the study concludes that the company's budgeting process makes considerable positive influence on achieving organizational goals, though the company does not have a properly designed strategic planning process. However the absence of strategic planning, long term objectives, and absence of integration of strategic planning & budgeting, and some weaknesses in budgeting process like centralized decision making, non budgetary participation and absence of guidance for budget preparation, make negative influence on goal achievement through budgeting, as a mean of the strategic planning as discussed Blumentritt (2006). However the positive influences of budgeting process in goal attainment over weights the negative impacts and therefore HM Plc's Budget supports to achieve organizational goals satisfactorily. Ultimately considering the HM Plc's whole role of budgeting

process as a tool of implementing strategic plans, researcher suggested to pay special attention on strategic planning process and integration of strategic planning and budgeting processes for better achievement of both short term and corporate goals.

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