**ASB/ABJ 4007 Finance for Managers**

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THE ROLE AND BEHAVIOURAL IMPLICATIONS OF BUDGETING

**Table of Contents**

[1. Introduction 2](#_heading=h.3rdcrjn)

[2. Concept and behavioural implications of budgeting 2](#_heading=h.26in1rg)

[2.1 Bugetary concept 2](#_heading=h.rrqjiy4hvoy4)

[2.2 Dysfunctional Behaviour 3](#_heading=h.1ksv4uv)

[2.3 Motivational Factors 3](#_heading=h.z337ya)

[3. Role of budgeting 4](#_heading=h.lnxbz9)

[3.1 Excessive pressure 4](#_heading=h.35nkun2)

[3.3 Budgetary Slack 4](#_heading=h.44sinio)

[3.4 Inter-departmental Conflicts 4](#_heading=h.2jxsxqh)

[5. Conclusion 5](#_heading=h.3j2qqm3)

[Reference 6](#_heading=h.1y810tw)

# 1. Introduction

This study centres around the concept of budgeting and its behavioural implications. Budgeting is a part of controlling the management system so that resources can be used efficiently for the maximum success of an organisation. Therefore, budgeting is an integral part of finance management and this study provides a precise understanding of budgeting concepts and the various types of budgets, which are in use presently. Furthermore, this study highlights the role and the behavioural implications of budgeting.

# 2. Concept and behavioural implications of budgeting

## 2.1 Bugetary concept

The budgetary system is at the centre of every organisation irrespective of organisational size and complexity. Budgeting is intricately related to the goals of a particular organisation and the need for resources, which are required for achieving those goals. As per the views of Aziz, and Shah(2021), the process of budgeting incorporates strategic goals and objectives setting and predicting costs, revenues, cash flows and other factors. By nature, budgeting is a quantitative analysis and the primary purpose of budgeting is to map out the use and sources of funds so that an organisation can achieve its objectives.



**Figure 1: Types of budgeting**

(Self-Created)

According to the approaches and development of final budgeting, budgeting can be classified under three heads, which are ***“imposed budget”***, ***“participative budget”*** and ***“negotiated budget”***. According to the comments of Pan *et al.* (2020), imposed budget implies that top management decides on budgets and the lower management team is only responsible for the execution of that budgetary plan and this type of budget is more convenient for an autocratic leadership style. On the other hand, a participative budget is convenient for a democratic style of leadership and in this type of budgeting, the lower team of management actively participates to develop a final budget. In negotiated budgets, both participative and imposed styles of budgeting are incorporated and the purpose of negotiated budgeting is to create an environment that supports a shared responsibility to prepare a final budget. In this context, it is important to note here that the leadership style, goals and objectives of an organisation determine which mode of budgeting needs to be adopted.

## 2.2 Dysfunctional Behaviour

When organisational goals and the individual goals of managers are in perfect alignment, that budget can promote positive behaviour. Conformity between organisational goals and individual goals in terms of budgetary expectation has been termed “goal congruence” (Klaorina and Suprasto, 2019). Therefore, participative managers feel happy and exhilarated when they sit for the budgeting-making process. Such congruent goals increase the performance and excellency of the managers. However, dysfunctional behaviour can occur in managers when their individual goals are not in conformity with the goals of their organisations. As per the views of Nehme *et al.* (2022), dysfunctional behaviour severely affects the performance of managers and at the same time, the productivity of the employees also gets adversely affected, therefore, budget goals must have realistic standards. Budgets, which are based on realistic standards, are beneficial for both organisations and managers.

## 2.3 Motivational Factors

The performance of managers and other employees can be enhanced by motivating them during final budgets. The major factor that motivates employees to perform better is achievable targets and goals (Kunnathuvalappil Hariharan, 2019). Unnecessary pressure creation significantly deteriorates employee performance and consequently, the objectives of organisations too remain unattained. Therefore, proper allocation of funds for required resources and cost prediction can motivate employees to enhance their performance. The unachievable standards and budgeted goals affect the performance of the employees, consequently, the organisational performance significantly hampers at the same time.

# 3. Role of budgeting

## 3.1 Excessive pressure

Budgets are set to coordinate every activity in an organisation and most often it can be seen that the final budget generates immense pressure and stress on managers and other employees working in an organisation. Therefore, according to the perspective of Bedford *et al.* (2022), budgets should not be set with achievable goals and expectations and at the same time not with excessively low expectations, an ideal budget needs to be moderate and based on realistic approaches. On the other hand, budgets with low expectations do not enhance the performance of the managers because they tend to think that they can easily meet the requirements of the budgets (Mauro *et al.* 2021). On the contrary budget with higher expectations or targets often observe to demotivate the employees and management of an organisation.

## 3.3 Budgetary Slack

Budgetary slack takes place when managers deliberately underestimate the revenues of their organisation and overestimate costs and demand more funds to execute activities, which can be executed with comparatively fewer funds (Daumoser *et al.* 2018). In this aspect, as per the views of Namazi and Rezaei (2023), this misprediction of cost and revenue and its difference with a realistic estimate is termed “budgetary slack”. Studies have found that the tendency of budgetary slack is prevalent in all organisations. It is because junior managers understand that senior managers are more likely to cut their budget proposals and therefore, they increase the cost projection while lowering the estimated revenue. However, on the contrary, Saarinen (2021) highlighted in a study that budgetary slack delivers a proper means to attain a cushion in a budget which focuses to enhance the potential of the actual performance level of an organisation compared to its set targets and motivate the employees.

## 3.4 Inter-departmental Conflicts

By nature a budgeting process is formal and highly technical, however, in reality, budgetary processes become extremely informal and a matter of bargaining. Informal bargaining processes during budgeting are quite common because managers of different departments tend to compete for resources. Such inter-departmental conflicts often lead to deviated goals, which are not in sync with organisational goals because at this stage managers fight for power and recognition and not for ways that can enable their organisation to achieve its goals (Arnold and Artz, 2019). According to the views made by Yu *et al.* (2022), budgeting provides an appropriate means through which inter-departmental conflicts could be avoided by establishing suitable budget goals and communication strategies.

# 5. Conclusion

Conclusively, it can be noted here that budgeting is essentially a complex and technical process. Appropriate budgeting requires accurate revenue and cost projection and proper identification of organisational objectives. However, the objectives or goals of an organisation need to be grounded on realistic standards, otherwise, irrational pressure is created for managers and other employees. Therefore, participative budgeting should be appreciated in an organisation and the individual objectives of managers should not be entirely dismissed.

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