BUDGETING, FORECASTING AND FINANCIAL PLANNING AS A STRATEGIC TOOL IN THE EASTERN CAPE’S MANUFACTURING INDUSTRY

by

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DECLARATION

This dissertation is an original piece of work, which is made available for photocopying and for inter-library loan. This dissertation has not been previously submitted for assessment to another university for another qualification.

Signed at Port Elizabeth on 04 March 2013

____________________
Signature
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CHAPTER 1
INTRODUCTION AND BACKGROUND

1.1 INTRODUCTION

One of the key challenges facing companies today is the ability to plan for
the future and to predict operating performance. An effective, timeous and
accurate budgeting, forecasting and financial planning process offers
organisations an opportunity to prepare for and be in a position to succeed in
a rapidly changing business environment. Companies that can update plans
and forecasts quickly are in a better position to take advantage of
opportunities and respond to threats (Stretch, 2009: 90).

Budgeting, forecasting and variance analysis are management accounting
tools that can help organisations gain a more in depth understanding of the
industry in which they operate. Over time, the understanding is refined and
these tools can ultimately add value to the organisations’ strategic decision-
making process.

Achieving true value through the financial planning process is dependent on
a number of factors, namely:

• understanding of the industry-specific challenges and opportunities
• corporate culture of the organisation regarding planning and budgeting
• the organisations ability to quickly change the scope of its
  assumptions as the business environment changes
• time and costs involved in the process
• integration of all the functional areas of the organisation in the
  planning process

Organisations need to carefully consider the economic environment as well
as take cognisance of the various internal and external factors which may
have an impact on its operations. According to Botten (2008: 42)
organisations should maintain a weather-eye on its environment, watching
out for emerging opportunities and threats. Each industry has its own set of challenges and opportunities that organisations have to take into account in their strategic planning. Therefore, budgeting and forecasting have to consider these general and industry-specific opportunities and threats.

An organisation's attitude toward planning is important, buy-in from the whole organisation must be obtained in order for the process to add value and to be effective. Stretch (2009: 89) argues that many managers are burdened with planning systems developed years ago in a relatively static, easy to understand, industrial age. This kind of organisational scenario at a managerial level could lead to negativity and a lack of buy-in to the planning process. Other reasons for criticism and lack of buy-in are highlighted by Collier & Agyei-Ampomah (2007: 39 - 40) as follows, budgets;

- are time-consuming and expensive
- provide poor value to users
- are too rigid and prevent fast response
- can lead to unethical behaviour

In an environment where timely and accurate information is invaluable to making strategic decisions, an organisation's ability to change or update the original plan quickly is crucial. The use of flexible budgets or rolling forecasts has given organisations this opportunity. A flexible budget or forecast is a much better basis for investigating variances, especially when key drivers such as planned volumes differ from the original plan (Collier & Agyei-Ampomah, 2007: 41).

Shortened budgeting and planning cycles are also integral to the success of the financial planning process. According to PricewaterhouseCoopers (2011: 9), the consequence of lengthy planning and budgeting cycles often mean that the final budget falls out of step with quickly evolving business conditions. Shortened planning cycles also mean there are less costs involved in the process.

The role of the finance department is to provide a financial evaluation of agreed-upon sales volumes, macro-economic and internal assumptions.
Although finance drives the budgeting process, it has to originate at a strategic level through the company’s mission statement, key corporate objectives and goals. Financial planning must be an integrated process involving all the functional areas of the organisation.

PricewaterhouseCoopers (2011: 3) states the importance of linking sales and operational planning activities with the financial planning process. Ogilvie (2008: 28-35) argues that financial analysis requires an understanding of the products, services and operating characteristics of the entity. This reiterates the need for finance to be closely involved with the various functional areas of the organisation throughout the planning process. Improving the finance department’s understanding of the business will ultimately improve the quality and accuracy of the financial evaluation.

1.2 BACKGROUND TO THE PROBLEM

For many years, organisations have viewed budgeting and forecasting as mandatory and time consuming. The traditional budgeting and forecasting processes are still the cornerstones of the corporate financial planning process. In South Africa today, companies still budget once a year, and use this budget as the benchmark for judging monthly performance (Stretch, 2009: 90).

Each year, the various operational areas within the company provide input to finance in order to compile a budget. These inputs are used together with certain assumptions and the financial impact thereof presented as the finance department’s evaluation. Once all parties agree, a formal budget is approved and filed away. However, as key drivers such as the macro-economic and socio political environment, pricing, inflation and volumes change, the approved budget becomes useless as a measurement tool for evaluating the organisations performance. Stretch (2009: 89) argues that today’s rapidly changing economy has rendered these old, time-consuming, costly, slow and unresponsive processes obsolete. Organisations may still have the traditional budgeting process but should also do monthly rolling
forecasts to modify the original plan as circumstances change; this modified plan would be a much better basis for performance management.

Even if the organisation moves toward the flexible or rolling forecast approach, there are still a number of factors that hinder the quality of the budgeting and forecasting processes. As a result, planned data is not being used to its full potential. This information should add value to an organisation’s strategic decision-making process.

Considering the limitations of the traditional budgeting and forecasting processes and also the various factors that influence the quality of these processes, organisations need to have a strong focus on budget and forecast accuracy. Forecasts are not always accurate – they are essentially about predicting the future with incomplete information (Department of Treasury, 2008: 2). According to Ernst & Young (2011: 2) budget and forecast results may not focus on accurate or timely information, thus offering little predictive value which limits the organisation’s ability to respond confidently to changing market conditions and increases the possibility of poor strategic decision-making.

Accurate financial planning data provides the following:

- gives finance a good base with which to compare actual accounting data
- actual versus budget/forecast analysis provides finance and top management with necessary information for improving strategic decision-making

PricewaterhouseCoopers (2011: 3) argues that forecasting accuracy is at the top of the improvement agenda; companies that formally measure and report on forecast accuracy have achieved a higher level of precision. In a discussion regarding the importance of forecast accuracy, Morlidge (2012: 1) mentions that if organisations do not measure the quality of their forecast and budgeting process and, most importantly, act upon it, they have no guarantee that the budget or forecast can be relied upon. Forecasting
without understanding any deviations from the actual to forecast offers no real value to an organisation.

A very effective method of understanding the deviations to a forecast or budget is thorough variance analysis. Variance analysis can be defined as the evaluation of performance by means of variances, whose timely reporting should maximise the opportunity for managerial action (CIMA, 2008a: 3). This process gives organisation’s an opportunity to learn from the inaccuracies in their assumptions and take cognisance of any anomalies affecting the business that are outside the general scope of its assumptions. Many organisations do not evaluate actual results versus budget / forecast, this hinders the quality of the assumptions and forecasting going forward.

Lack of a formal process, namely; budget or forecast cycle plan, stunts the finance department in terms of the timeous and accurate presentation of financial data for decision-making. According to Ernst & Young (2011: 4), the following potential benefits are derived from a formal planning, budgeting and forecasting process:

- enhanced performance management capabilities
- increased visibility into and across operations
- more objective and data driven decision-making
- increased responsiveness to external factors

The purpose of this study is to highlight current organisational paradigms regarding budgeting, forecasting and financial planning and to assess whether organisations add value to their decision-making through budgeting, forecasting and financial planning.

The researcher aims to investigate the limitations of the traditional budgeting and forecasting processes as well as the various factors influencing the quality of financial planning data for strategic decision-making.
1.3 PROBLEM STATEMENT

As mentioned in the background to the problem, organisations view the traditional budgeting and forecasting processes as mandatory, time consuming and provides little or no value to the organisation. This kind of attitude towards planning leads to a lack of buy-in from the various functional areas. It is for this reason, and various others, that organisations are not using the information generated through these processes to its full potential.

The main problem is to assess whether organisations are using their budgeting, forecasting and financial planning as a strategic tool in the overall decision-making process.

1.3.1 Sub-problems

- the limitations of the traditional budgeting and forecasting processes
- the factors influencing the quality of budget and forecast accuracy
- time consuming and costly budgeting and planning cycles
- lack of organisational ‘buy-in’ to the budgeting and forecasting process
- the role of the finance department in a value-adding financial planning process

1.4 RESEARCH OBJECTIVES

1.4.1 Primary objective

The primary objective of the study is to assess whether organisations are using their budgeting, forecasting and financial planning information as a strategic tool in the decision-making process. The research aims to investigate the various factors that hinder the success of the finance department in delivering a quality financial plan, budget or forecast to top management and the rest of the organisation.
1.4.2 Secondary objectives

To achieve the primary objective, the following secondary objectives will be pursued:

- to investigate current organisational paradigms towards budgeting, forecasting and financial planning
- to explore the various factors influencing budget and forecast accuracy and quality
- to explore the role of the finance department in a value-adding budgeting, forecasting and financial planning process
- to determine the role of financial planning information in the strategic decision-making of firms

1.4.3 Research design objectives

The following research design objectives will be pursued in this study:

- to conduct a literature review on existing, available and current information regarding budgeting, forecasting and financial planning
- based on the literature review, to construct a questionnaire which will be used to collect the primary data needed to address the research objectives
- to finalise the questionnaire and seek ethics clearance for the questionnaire from the NMMU Ethics Committee
- to execute the data collection procedure by mailing the questionnaire to a selected sample of organisations in the Eastern Cape’s manufacturing sector
- to analyse and interpret the data and make conclusions
1.5 RESEARCH METHODOLOGY

Research methodology, also known as the research paradigm, is the way one thinks about research, how one collects and analyses the data and the way in which one writes the dissertation. Two types of research have been identified; namely, qualitative and quantitative research.

Qualitative research is concerned with qualities and non-numerical characteristics while quantitative research is all about data that is collected in a numerical format. Phenomenological research tends to produce qualitative data and positivistic research tends to produce quantitative data (Collis & Hussey, 2003).

The main advantage of a quantitative approach to data collection is the ease and speed with which the data can be collected. In this research it is possible to use large samples while in a qualitative study the sample size may be small. For example, a case study may consist of one respondent. A qualitative data collection method can be time consuming and costly, although it can be argued that qualitative data provides a more real basis for interpretation and analysis.

The research project will follow a mixed research approach which is a combination of qualitative and quantitative approaches. Chapter 4 of this study will deal with research design and methodology.
1.5.1 Sampling

Convenience sampling will be used to select a sample of senior finance staff members of organisations in the Eastern Cape’s manufacturing industry. A structured questionnaire will be distributed electronically to selected respondents. The design of the questionnaire and the types of questions are covered in Chapter 4. Follow-ups will be done to ensure a good response rate.

1.5.2 Measuring instrument

A self-constructed scale will be used to measure organisational attitude toward the financial planning process. Certain questions will be linked by way of a 7 point scale ranging from strongly disagree to strongly agree. Certain questions will be open-ended to encourage the free flowing of views and opinions. For the purpose of this study, the researcher is the measuring instrument.

1.6 DEFINITION OF KEY CONCEPTS

1.6.1 Strategic planning

It is a systematic planning process of the organisation, including its mission, vision for the future, operating values, needs, goals, prioritized actions and strategies, action and monitoring plans (Foundation for Community Association Research, 2001: 2).
1.6.2 Forecasting accuracy

Forecasting accuracy is a useful measure that helps finance managers assess the quality of the process (Papenfuss, 2012a: 1).

1.6.3 Variance analysis

Variance analysis involves comparing actual performance against plan, investigating the causes of the variance and taking corrective action to ensure that targets are achieved (Collier & Agyei-Ampomah, 2007: 40).

1.6.4 Macro-economic environment

The macro-economic environment will include trends in gross domestic product (GDP), inflation, employment, spending, and monetary and fiscal policy. The macro-economic environment is closely linked to the general business cycle, as opposed to the performance of an individual business sector (Investopedia ULC, 2012: 1).

1.6.5 Corporate culture

An organisation’s culture is made up of its collective history, beliefs and experiences. Organisations act based on the beliefs upon which they were founded and the nature of the people who work there. Every organisation has a unique culture (Rothwell, 2012: 265).
1.7 DELIMITATION OF THE RESEARCH

The delimitation of the study will assist the researcher in making the research topic more manageable. The study has therefore been limited to companies in the Eastern Cape’s manufacturing industry. By delimiting the study the implication is not that research on the same topic is not needed in other sectors, but that the same principles can be applied universally.

1.8 RESEARCHER’S QUALIFICATIONS

The researcher has the following academic and industry background:


1.9 OUTLINE OF THE STUDY

The study will be divided into 6 Chapters.

- Chapter 1: Deals with introduction and overview of the study, the problem statement that necessitates the need for the research and encapsulates the main objective of the research.

- Chapter 2: Represents an in-depth literature review and discussion regarding the limitations of the traditional budgeting process and the various factors influencing the quality of financial planning information. This chapter will highlight the shortcomings of organisations that do not add real value to strategic decision-making through inaccurate and/or unreliable financial projections.

- Chapter 3: This chapter deals with the value-adding budgeting, forecasting and financial planning process. The role of the finance
function in a value-adding financial planning process is explored. Financial planning must be corporate policy within the organisation, not just something done by finance for finance.

- Chapter 4: Will cover the selection of the sample, structure of the questionnaire and extent of the responses.

- Chapter 5: The biographical information of respondents and empirical findings of the research study are presented and discussed.

- Chapter 6: Presents a final summary, conclusions and recommendations for future research.
## CHAPTER 2

**LIMITATIONS OF TRADITIONAL BUDGETING AND FACTORS INFLUENCING THE QUALITY OF BUDGETING, FORECASTING AND FINANCIAL PLANNING**

### 2.1. INTRODUCTION

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CHAPTER 2
LIMITATIONS OF TRADITIONAL BUDGETING AND FACTORS INFLUENCING THE QUALITY OF BUDGETING, FORECASTING AND FINANCIAL PLANNING

2.1 INTRODUCTION

This chapter will focus mainly on the limitations of the traditional budgeting and forecasting processes as well as the various factors that influence the quality of the budgeting, forecasting and financial planning processes.

The researcher will compare and contrast various definitions of budgeting, forecasting and planning. A review of related literature regarding the limitations of the traditional budgeting process will be looked at with a focus on the following key elements:

- budgeting and forecasting – cost control versus value creation
- lack of departmental collaboration
- lengthy, inflexible and laborious planning cycles
- behavioural implications of budgeting

There are certain elements of budgeting, forecasting and financial planning that are crucial to the success of these processes. Focusing on these elements and continuously trying to improve upon them will fine-tune the organisations ability to update plans quicker, place more reliance on financial information and add value to strategic decision-making.

The advantages of a value-adding budgeting, forecasting and financial planning process will be investigated.
2.1.1 Definition of budgeting

According to IBM (2009: 3) budgeting is planning distributed to individual areas of responsibility in a business. As a result, many more people are involved and work at a much greater level of detail. Jackson, Sawyers and Jenkins (2009: 326) argue that budgets are plans dealing with the acquisition and use of resources over a specified time period. There are various definitions for budgeting, the common purpose however, is control. Budgets provide a control mechanism through both the feed forward and feedback loops. In feed forward terms, budgets can be reviewed in advance to ensure that they are consistent with organisational goals and strategy. Using feedback, variations between budget and actual performance can be investigated and monitored and corrective action taken for future time periods (Collier & Agyei-Asampah, 2007: 39).

2.1.2 Definition of forecasting

Forecasting is essentially a re-casting of the budget, in summarized form, to reflect changing market conditions, strategic plan alterations, error corrections and revised assumptions in the original approved budget. Companies typically re-forecast monthly or on an ad hoc or event basis in this unpredictable economy, with the process executed by a handful of finance personnel (IBM, 2009: 3).

According to Barrett and Hope (2006: 28), a common approach to forecasting is geared at fiscal year-end and is aimed at helping managers ‘keep on track’. This is often known as “3+9”, “6+6” and “9+3”, the second number representing the months remaining until the fiscal year end. In its simplest form, IBM (2009: 8) argue that a forecast is a revision of the budget that reflects changing business conditions, reassessment of key budget assumptions or perhaps a significant review of the strategic plan. The increasing use of forecasts has meant that budgets have become more forward-looking and better linked to strategic planning (CIMA, 2004: 3).
2.1.3 Definition of planning

IBM (2009: 3) states that planning is a strategic prediction of business performance at a summary level. Usually, planning is the province of a few savvy senior managers charged with making sure the company responds to changing market conditions and opportunities, balancing assets with opportunities. Accordingly, the process can be fairly frequent and must be completed quickly. According to Jackson, Sawyers and Jenkins (2009: 326) planning is the cornerstone of good management and requires the development of objectives and goals for the organisation as well as the actual preparation of budgets.

The key aspects of planning, budgeting and forecasting are summarised in Table 2.1.

**TABLE 2.1: Key aspects of planning, budgeting and forecasting**

<table>
<thead>
<tr>
<th></th>
<th>Centralised or Decentralised</th>
<th>Level of detail</th>
<th>Frequency</th>
<th>Speed</th>
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</thead>
<tbody>
<tr>
<td>Planning</td>
<td>Centralised</td>
<td>Summary</td>
<td>Often</td>
<td>Quick</td>
</tr>
<tr>
<td>Budgeting</td>
<td>Decentralised</td>
<td>Highly detailed</td>
<td>Annual</td>
<td>Slow</td>
</tr>
<tr>
<td>Forecasting</td>
<td>Centralised</td>
<td>Mostly light detail</td>
<td>Monthly or ad hoc</td>
<td>Quick</td>
</tr>
</tbody>
</table>

(Source: IBM 2009: 4)

2.2 LIMITATIONS OF THE TRADITIONAL BUDGETING PROCESS

The traditional budgeting process is still very much the cornerstone of the corporate financial planning process. IBM (2009: 9) cites the following reasons why budgets are still valuable to an organisation:

- helps develop an understanding of business drivers and constraints
- substantiates information for external use
- identifies mismatches and exceptional changes
• supports the strategic plan

Despite the above mentioned reasons, the traditional budgeting and forecasting processes have been under scrutiny in recent years. According to Collier and Agyei-Ampomah (2007: 40) budgeting disempowers the front line, discourages information sharing and slows an organisation’s response to market conditions. Barrett and Hope (2006: 28) argue that the annual budget takes too long and in many instances adds little value. Traditional budgeting evolved at a time of stable trading environments, however, today’s markets are increasingly unstable and the pace of change is rapid. In contrast to the reasons cited above, IBM (2009: 2) mentions the following reasons why the traditional budgeting process can add little or no value to the organisation:

• we spend more time creating a budget than analysing it
• after the budget is approved, no one looks at it again
• budget holders dislike the tedious and lengthy process
• budget holders attribute adverse variances to the finance department and favourable variances to their own performance and managerial skill

According to KPMG (2010: 3) in traditional budgeting, companies set targets with checkpoints throughout to aid alignment across the organisation. They then forecast performance every quarter, typically through the end of the fiscal year. Annual plans are static, strongly determine where investments would go and often serve as benchmarks for executive performance measurement and compensation. This static approach does not hold in today’s uncertain times.

A few of the criticisms of the traditional budgeting process cited by CIMA (2004: 7) are as follows:

• budgets constrain responsiveness and flexibility are often a barrier to change
• budgets add little value, especially given the time required to prepare them
• budgets encourage gaming and perverse behaviours
- budget are developed and updated too infrequently
- budgets are based on unsupported assumptions and guesswork
- budgets make people feel undervalued

### 2.2.1 Cost control versus value creation

One of the key limiting factors of the traditional budgeting and forecasting processes is the purpose for which the budget was prepared in the first place. Jackson, Sawyers and Jenkins (2009: 326) highlight two purposes for which budgets are typically prepared:

- the use of budgets for cost control and performance evaluation
- the use of budgets in strategic planning and operating activities

Many organisations still prepare an annual budget for the first reason, to control costs and evaluate performance. John and Ngoasong (2008: 8) argue that this kind of planning encourages internal politics, gaming behaviour and a short-termist culture that focuses on achieving the budget figure or target. According to CIMA (2004: 3) budgeting in this manner can stifle the entrepreneurial, risk-taking culture that can be responsible for value creation. When rewards and incentives are offered for achieving targets, managers may become reluctant to present an unbiased picture. This unbiased picture will therefore add little or no value as an informational tool in the strategic decision-making process. Jackson, Sawyers and Jenkins (2009: 328) state that this kind of behaviour is unethical and is not beneficial to the company as a whole. Organisations can reduce incentives for this type of behaviour by holding managers accountable and punishing unethical behaviour with strong sanctions.

Organisations may continue to use the annual budget and monthly re-forecasts as a tool for cost control and performance measurement. However, Barrett and Hope (2006: 29) mention that this process must not be seen by senior managers as just a tool for questioning and reassessing performance targets. Leading organisations use budgeting and forecasting to support strategy reviews rather than simply check where they are against
the actual plan. According to CIMA (2004: 3), if implemented correctly, budgeting and forecasting can inform strategy implementation, risk management, resource allocation and are generally regarded as an integral part of running a business.

### 2.2.2 Lack of departmental collaboration

A lack of cross-functional collaboration and the mind-set that the budget ‘belongs’ to finance is also one of the limiting factors of the traditional budgeting and forecasting processes.

In most organisations, the finance department ‘owns’ and administers the budgeting process. Accountants are therefore first in the line of fire for its perceived shortcomings and are charged with making the necessary changes (CIMA, 2004: 2). Akintoye (2008: 11) argues that the finance department are often seen as traffic cops rather than strategic partners. Budgetary planning then becomes a mere exercise; consequently, the quality of information for budgetary planning and control is seriously compromised. This kind of organisational paradigm regarding the budgeting and forecasting process can have serious implications as to whether the process itself adds value to strategic decision-making.

Departmental managers provide assumptions such as sales volumes, inflation and other key drivers to finance to use in the budgeting and forecasting process. According to Adaptive Planning (2005: 1) because finance does much of the work themselves, line managers see little benefit and are dragged through the process. There is a lack of buy-in from the various functional areas and the finance department’s plan loses credibility.

The role of finance and importance of cross departmental collaboration is dealt with in greater detail in chapter 3.
2.2.3 Lengthy, inflexible and laborious planning cycles

The traditional budgeting and forecasting process is time consuming, inflexible and costly. According to Deloitte Consulting LLP (2010b: 9) the greatest threat to effective financial stewardship is a long, resource-consuming planning cycle. Too many decisions are made without meaningful perspective and direction.

PricewaterhouseCoopers (2011: 9) states that organisations spend a great deal of time and effort on consolidating, summarising, communicating, explaining and reviewing information for financial planning. This argument is supported by IBM (2009: 6) who mention that weeks and months are spent struggling with the mechanics of the process, chasing submissions, checking for incomplete or invalid data and trying to track and control versions. Another concern raised by IBM (2009: 6) is that the finance department, even with enterprise resource planning software, is still doing too much manual work to fine-tune the budget thus adding to the inefficiency of the process. According to Adaptive Planning (2005: 6) many organisations have an inefficient and inflexible budgeting and planning process. This time-consuming distribution and consolidation processes guarantees that the budget data is irrelevant before it is even shared.

John and Ngoasong (2008: 36) state that with less time spent on the mechanics of budgeting, there is more time to devote to analysing the implications of the plan. Organisations are able to do more ‘what-if’ thinking to look into alternative approaches and consider responses to changes in the plan. Results of a research study conducted by PricewaterhouseCoopers (2011: 11) suggest that most of the time is spent on reviewing the budget and securing approvals.

In view of the above-mentioned arguments, it is clear that more time is spent preparing the budget or forecast than analysing it. Analysing data from the budgeting and forecasting process is only valuable to the organisation if the data is relevant, timely and accurate.
2.2.4 Behavioural implications of budgeting

When budgets are used for both planning and control purposes, conflicts invariably arise. If managers are evaluated and compensated according to whether they ‘meet the budget’, they may have incentives to pad the budget, thus making targets easier to reach (Jackson, Sawyers & Jenkins, 2009: 328).

According to Collier and Agyei-Ampomah (2007: 49) the practise of reducing budgets where they have not been spent has led to managers spending their budget allocations at year end, whether the expenditure is needed or not to avoid budget cuts in the following year. Collier and Agyei-Ampomah (2007: 50) go on to mention that the manipulation of data or its presentation to show performance in the best possible light is one of the dysfunctional behaviours of budgeting, these include:

- smoothing: shifting revenue or expenses from one accounting period to another
- biasing: selection of a message that the recipient wants to hear
- focusing: emphasising on certain positive aspects rather than on other negative ones

Another example of dysfunctional behaviour as a result of traditional budgeting is ‘gaming’. Jackson, Sawyers and Jenkins (2009: 328) makes the following example of ‘gaming’ behaviour, if a manager knows that he or she will receive a bonus if sales in the department exceed the budget, they may attempt to set the sales budget at an unrealistically low level.

This dysfunctional behaviour in traditional budgeting has a serious impact on the financial information being used to drive decision-making.
2.3 FACTORS INFLUENCING THE QUALITY OF BUDGETING, FORECASTING AND FINANCIAL PLANNING PROCESSES

Organisations that have moved away from the traditional 'annual' budgeting process and embraced a planning cycle that focuses on a budget with more frequent re-forecasting still face the challenge of ensuring the quality of information generated through the budgeting, forecasting and financial planning process. This information is useful for analysing trends, developing meaningful business insights and ultimately adding value to strategic decision-making.

According to KPMG (2010: 3) the key to reliable planning and forecasting is the ability to draw together culture, process and internal and external data into balanced and cohesive framework enabled by technology. Reliable planning and forecasting can have an incredible long-term impact on the business, helping to improve the ability to identify new opportunities and manage potential risks.

Deloitte Consulting LLP (2010b: 4) states that a value-adding budgeting, forecasting and financial planning process provides the organisation with the following:

- aligns everyone to the same goals
- provides both short-term and long-term targets
- sets a framework with which to evaluate investment opportunities
- guides the definition of key performance indicators (KPI’s)

As illustrated in figure 2.1, when it's done right, the planning, budgeting and forecasting process begins with the enterprise strategy (3-5 years) which drives decision-making about investments, capital allocation and resource deployments. Executives and business stakeholders are fully engaged in the process and drive initiatives to obtain funding. These initiatives drive high-level financial plans (18-24 months) which set targets for operating plans (12-18 months). Lessons learned from variance analysis drives re-forecasting which in turn feeds back to the strategic plan. Figure 2.1 also indicates that
the organisations strategic plan should guide the key performance indicators used to measure performance.

**Figure 2.1 Planning, budgeting and forecasting as a value-adding process**

![Diagram](image)

(Source: Deloitte Consulting LLP 2010b: 4)

Leading organisations are changing their mind-set about the budgeting, forecasting and financial planning process. KPMG (2010: 4) cites the term ‘results-based budgeting’ and argue that it can help integrate the strategic planning and financial planning processes by linking the achievement of performance or specific measurable outcomes to the allocation of resources and shifting the mind-set of the organisation. Figure 2.2 illustrates how results-based budgeting can add value to strategic decision-making. The
strategic plan should drive the annual budget, once the framework has been provided through the annual budget the organisation should re-forecast the budget. Actual results and comparing these results to budget and forecast will influence the strategic plan.

**Figure 2.2  Results-based budgeting**

(Source: KPMG 2010: 4)

According to Jackson, Sawyers and Jenkins (2009: 328), a budgeting process that is clearly guided by a strategic plan makes managers more focused on important aspects of the budget and less worried about irrelevant details.

As illustrated in both figures 2.1 and 2.2, the starting point for the budgeting, forecasting and financial planning process is careful consideration of the organisations strategic plan.
2.3.1 Corporate culture towards planning

According to CIMA (2004: 4) organisational culture is by far the biggest influence on how formal systems and processes operate in practice. Fostering the right culture, whatever that may be in the context of individual companies, was recognised as one of the most important factors in the success of the budgeting and forecasting process.

It is critical that a company’s culture embraces and rewards planning. Excellent business management requires excellent financial management, which in turn requires a company-wide commitment to excellence in budgeting, forecasting and reporting (Adaptive Planning, 2005: 2).

Many organisations regard the budgeting, forecasting and financial planning processes with a mixture of suspicion and frustration. Planning is viewed as a time-consuming waste of resources and the organisation is practically dragged through the process each year. Adaptive Planning (2005: 2) argues that senior managers are engaged in strategic planning, with finance running the budgeting show and departmental managers viewing the annual process as an unwelcomed chore. Another issue raised by IBM (2009: 5) is that senior managers are concerned that the budget bears little relation to their carefully prepared strategic plans.

A study of related literature indicates two key ways to improve organisational culture toward planning:

- According to CIMA (2004: 5) pay and reward structures have the biggest influence on people’s motivation. However, it is noted that offering remuneration for target achievement can lead to dysfunctional behaviour. In summary, you may get people motivated but there is still a potential risk to the quality and integrity of financial information.
- Adaptive Planning (2005: 3) argue that leading organisations have a top-down and bottom-up approach to planning. Senior managers provide initial guidance, a top-down perspective on strategic goals. Next, departmental managers build a plan from the bottom-up
showing how they intend to meet those goals. This process will often require frequent iterations for the top-down and bottom-up approaches to meet. The result is a plan that:

- is supported by departmental managers because they helped create it
- is supported by senior managers because it is aligned with their strategic goals
- is supported by finance because they added value to a productive, collaborative effort rather than demanding participation in an exercise with little added value

2.3.2 Plausibility of assumptions

The use of assumptions is a vital element of budgeting, forecasting and financial planning and has a direct impact on the quality of information generated as a result of these processes.

According to Steven-Jennings (2009: 13) the key assumptions used in the plan must be tested thoroughly by researching the industry, speaking to colleagues and competitors and getting objective opinions. In a related publication, KPMG (2010: 1) mention that the key to an effective budgeting and forecasting process is to validate all possible assumptions and factors so that executive management can weigh the validity of each and determine which to include and which to omit. Evaluating actual outcomes to what was planned is a very effective means of testing the assumptions used in the plan. Barrett and Hope (2006: 30) argue that management should carry our ‘post-mortems’ on their budgets and forecasts. The purpose is not to attribute blame but learn if forecast accuracy is improving and how they can improve it even further. These ‘post-mortems’ can also help significantly improve or change the scope of assumptions.

Papenfuss (2012b: 1) mentions that the development, testing and discussion of forecast assumptions are now a critical part of the planning process.
Figure 2.3 illustrates where the development, testing and discussion of assumptions would fit into the financial planning process.

**Figure 2.3  The development, testing and discussion of assumptions**

A longer range outlook in the budget or forecast process offers organisations the opportunity to test the plausibility of their assumptions. Organisations, operating in an international environment, which are affected by factors such as currency differences have to make significant assumptions in terms of the strength or weakness of their trading currency. Inflation and a deteriorating trading currency are often recovered through product pricing and marketing. Jackson, Sawyers and Jenkins (2009: 348) state that predicting inflation rates and prices in countries with unstable economies adds a great deal of complexity and uncertainty to the budgeting process.

A longer range outlook, beyond the end of the budget fiscal year, could indicate to organisations the various flaws in their assumptions. There is no rule of thumb with regard to the range of this extended outlook, according
Barrett and Hope (2006: 30) it should certainly be longer than the end of the budgeted financial year. To some extent it depends on how long it takes to make key decisions about operations, capacity and capital spending.

2.3.3 A focus on improving forecast accuracy

The quality of financial information from the budgeting and forecasting process is largely dependent on the organisation’s attitude towards budget and forecast accuracy. The need for improved value and accuracy from budgeting, forecasting and financial planning led to a thorough research study conducted by PricewaterhouseCoopers in 2011. This study focused not only on the current challenges but also on the practices organisations are deploying to improve the financial budgeting and forecasting processes (PricewaterhouseCoopers, 2011: 2).

According to PricewaterhouseCoopers (2011: 3) a key finding of this study is that increasing forecasting accuracy is at the top of the improvement agenda. Companies continue to struggle with the shared ownership between business and finance of the financial plan and the overall financial conservatism built into the planning process. Companies that formally measure and report on forecast accuracy have achieved a higher level of precision. KPMG (2010: 7) states that a forecast is comprised not only of financial measures, but also key drivers of the business that affect current and future financial performance. The deeper the understanding of the relative impacts of each driver, the more accurate the forecast and the ability to make informed decisions.

In contrast to the views held above, Papenfuss (2010: 1) cites the following reasons why forecast accuracy is not worth measuring:

- forecast accuracy cannot be influenced. The markets follow a random path and it can therefore not be expected to achieve accurate forecasts
• forecast accuracy is a dangerous thing to measure and manage. People can start influencing the accuracy by managing their numbers according to expectations
• the quality of forecast accuracy is hard to define. If you beat your own forecast by performing really well. Is that good or bad?

Barrett and Hope (2006: 29) argued for less of a focus on accuracy. Budgeting and forecasting is only necessary because organisations cannot react instantly to changing events. That's why fast reaction is more important than accurate prediction.

According to PricewaterhouseCoopers (2011: 22), three of the leading causes of variances between forecast and actual performance are:

• uncertainty in the external business environment
• difficulty in accessing and incorporating external information (namely, macro-economic indicators, industry reports, competitive intelligence) when forecasting
• confusion between forecasts and targets / pressure to match forecast to targets

Of the three points mentioned, points two and three are internal influences and can be addressed by changing an organisation’s culture toward planning. The first point could be the most difficult to manage when trying to improve forecast accuracy. PricewaterhouseCoopers (2011: 24) engaged with leading finance executives in the above mentioned research study and observed that external sources of data including macro-economic indicators, industry reports and competitive benchmarks can provide a useful perspective on internal performance projections. These external sources of data often contradict internal thinking and create questions which can be value adding.

Achieving forecast accuracy improves the quality of financial information and increases the credibility of the finance department’s financial evaluation. Organisations must however shift the focus from control and accuracy to how effectively they use this information as a tool for strategic decision-making.
2.3.4 Frequency and level of detail

Organisations face the challenge of choosing the ideal frequency and level of detail for their budgeting, forecasting and financial planning. According to KPMG (2010: 7) rolling forecasts, revised monthly, quarterly, or at least annually are key to understanding the company’s current financial situation and also its future. The market, competitors and economy change constantly and at ever-increasing rates. Organisations are reacting by forecasting more frequently and reducing the amount of detail in each forecast. Barrett and Hope (2006: 30) state that the frequency of updating forecasts would depend on the industry. However, if an organisation has got forecasting down to a slick process that takes up little time and involves little cost, more frequent re-forecasting will give better early warnings of emerging trends and enable organisations to be more responsive.

A focus on material content in budgeting will free managers from unnecessary detail, enabling them to produce better plans. While supporting detail can provide audit trail and insight to manager’s thinking, more detail does not necessarily make for a better plan. Managing material content means that a company pays attention to whatever has a real and significant impact on expenses, revenues, capital or cash flows (Adaptive Planning, 2005: 6). Barrett and Hope (2006: 30) argue that is makes more sense to focus on the key drivers of revenue and costs and build a dynamic budgeting model that incorporates these non-financial drivers.

According to PricewaterhouseCoopers (2011: 15-16) obtaining the right level of detail for an organisation means that that a company has to understand and focus on the real drivers of the business that significantly impact their financial statements and spend less time managing the detail that has little impact on decision-making. Developing the balanced level of detail in a company’s planning environment translates into the following benefits:

- avoids giving the perception of false accuracy
- allows financial planners and managers to focus on the most important accounts and their drivers
enables finance teams to perform scenario analysis and turn around ‘what-if’ challenges in a timelier manner

In light of the views held above, it is clear that the frequency and level of detail in budgeting, forecasting and financial planning has a major impact on the quality of information used in the strategic decision-making process.

2.3.5 Technology

The technology used by organisations in the budgeting, forecasting and financial planning processes is a very important factor in whether these processes add value to strategic decision-making.

CIMA (2004: 4) state that new technology has helped organisations move away from a culture characterised by functional divisions and ‘silo’ mentality. Departments and managers using off-line spreadsheets can end up disconnected from other parts of the organisation that would impact on their planning.

Research conducted by PricewaterhouseCoopers (2011: 9) indicates that 27% of the organisations surveyed still rely on spreadsheets and manual processes for their budgeting, forecasting and financial planning. Whilst spreadsheets are flexible and relatively quick to update, IBM (2009: 14) cite the following reasons why they are inadequate in managing a budgeting process of any significant size or sophistication. Spreadsheets are:

- two-dimensional
- hard to maintain
- don’t integrate well with other systems
- difficult to share
- often hard to understand

For the reasons cited above, and many others, organisations are moving away from manual processes and spreadsheets in their financial planning. Jackson, Sawyers and Jenkins (2009: 327) indicate that more and more
companies are using enterprise resource planning systems as a key budgeting and planning tool. These systems link data from across all areas of the business and ensure that the same assumptions are used throughout the organisation; this also speeds up the budgeting process significantly. CIMA (2004: 4) argue that speed and accuracy means that the organisation has more time to focus on activities which really add value rather than on collecting data and ensuring its integrity.

The use of enterprise resource planning systems, as opposed to manual spreadsheets, for financial planning has added significant value to strategic decision-making. IBM (2009: 6) indicates that by re-evaluating the use of spreadsheets and investing in a planning application that best fits their needs, organisations have the following benefits:

- consolidates budgets in real time, automatically
- enables powerful driver-based modelling and scenario analysis
- creates a single version of all financial plans, forecasts and reports
- scales and expands to the needs of the business

2.4 CONCLUSION

This chapter explored the various limitations of the traditional budgeting process. It is evident that budgeting, with all the limitations identified, is still used by many organisations as a framework for further financial planning and analysis that supports decision-making.

More and more organisations are developing their financial planning systems and moving away from the traditional annual budgeting process. The value-adding budgeting, forecasting and financial planning process was briefly discussed and also the key factors that organisations must consider to ensure that quality is achieved and value is added to strategic decision-making.
# CHAPTER 3

**THE VALUE-ADDING BUDGETING, FORECASTING AND FINANCIAL PLANNING PROCESS**

### 3.1. INTRODUCTION

### 3.2. THE VALUE-ADDING BUDGETING, FORECASTING AND FINANCIAL PLANNING PROCESS

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### 3.4. THE LINK BETWEEN FINANCIAL PLANNING INFORMATION AND STRATEGIC DECISION-MAKING

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### 3.5. CONCLUSION

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CHAPTER 3
THE VALUE-ADDING BUDGETING, FORECASTING AND FINANCIAL PLANNING PROCESS

3.1 INTRODUCTION

In this chapter, the researcher will look at the value-adding budgeting, forecasting and financial planning process in greater detail. In light of the limitations of the traditional budgeting process, a value-adding budgeting, forecasting and financial planning process is essential for an organisation's strategic success.

The researcher will explore the important role of the finance department in a value-adding budgeting, forecasting and financial planning process as well as exploring the following elements:

- the administrative aspect of the process
- cross departmental discussion forums and meetings
- financial analysis
- process improvement

Lastly, this chapter will investigate the link between financial planning information and strategic decision-making.

3.2 THE VALUE-ADDING BUDGETING, FORECASTING AND FINANCIAL PLANNING PROCESS

According to PricewaterhouseCoopers (2007: 3) it is no longer sufficient to just measure past performance. Budgeting and forecasting have become a core competency for organisations to effectively plan, manage and execute strategy. KPMG (2010: 2) argue that budgeting and forecasting is an essential component of their effort to create and sustain value in the business.
The need for a value-adding budgeting, forecasting and financial planning process is becoming more and more evident in today’s complex and rapidly changing business environment. The accuracy and timeliness of the information generated through these processes have serious implications for strategic decision-making.

Figure 3.1 illustrates the four typical phases of the planning, budgeting and forecasting process. The starting point for the financial planning process is the strategic plan and the budget or forecast must be prepared with strategic goals in mind. Once a formal budget is approved it must be able to accommodate change through re-forecasting. Lastly, performance measurement is vital to understanding why budgets or forecasts have not been met and also to gain insight into future budgeting and forecasting.

**Figure 3.1 Four phases of the planning, budgeting and forecasting process**

(Source: KPMG 2009: 2)
3.2.1 Importance of the strategic plan

According to Ilesanmi (2011: 134) a strategic plan refers to the formulation of a unified, comprehensive and integrated plan aimed at relating the strategic advantages of the firm to the challenges of the environment. Its overall purpose is to assess the future implications of current decisions, to develop a framework for adjusting operations to changes in the wider business environment and to link and control the various elements of complex organisations.

A value-adding budgeting, forecasting and financial planning process should be driven by the organisation's strategic plan. According to Deloitte Consulting LLC (2010a: 4) when organisations do not have a clear business strategy, it is difficult to make budgeting and forecasting decisions.

An effective strategic plan translates the business strategy into a simple story about the organisation's future. This story is clear when people in the organisation understand what leadership has chosen to do, and not to do. This clarity is the foundation for a planning, budgeting and forecasting process that works.

3.2.2 Develop an annual budget based on the strategic plan

CIMA (2008b: 5) states that the main purposes of budgeting as it relates to planning and control and supporting the achievement of strategic plans are as follows:

- translating the long-term plan into an annual work programme
- co-ordinating the various departments of the organisation to ensure they work in harmony. A budget requires managers to consider the relationship between their operations and those of other departments. Otherwise, managers might make decisions in their own interests, rather than the organisation's best interests
• communicating plans to those who will be held accountable. Each department or individual should understand what role they play in helping the organisation achieve its plans.

One of the limitations of the traditional budgeting process is that financial plans are disconnected from the organisation’s overall strategic plans. According to IBM (2009: 5) senior managers are concerned that the annual budget bears little relation to their carefully prepared strategic plans.

IBM (2009: 11) further states that an organisation’s budget should closely reflect its strategic plan. The budget acts as a ‘sanity check’ for the strategic plan and as a means of building management commitment to high-level, long-term goals. Deloitte Consulting LLP (2010b: 4) argues that the prerequisite for value in the planning, budgeting, and forecasting process is the strategic plan. There is little chance of achieving ambitious objectives if the corresponding financial results are not incorporated into the financial and operating plans across the business units.

Management needs to ensure that financial planning targets are closely linked with organisational strategy and value drivers. Without strong linkage, the budget and reporting process becomes a financial exercise and is not used as an effective management tool to drive decision-making (PricewaterhouseCoopers, 2007: 40).

The strategic plan is the basis for value-adding budgeting, forecasting, and financial planning and the results of these processes help examine and validate the strategic plan.

3.2.3 Re-forecasting the annual budget

Preparing the annual budget is simply not enough in today’s volatile and rapidly changing business environment. Barrett and Hope (2006: 28) maintain that for this reason many organisations have adapted their budgeting process and are looking at other performance management
methodologies such as re-forecasting. There are two basic approaches to re-forecasting the budget:

- the first approach is geared at fiscal year-end and often referred to as “3+9”, the second number representing the number of forecast months left until financial year-end. This approach was briefly mentioned in chapter two

- secondly, rolling forecasts are being used to manage businesses more effectively making planning a continual process. The following example is made by Barrett and Hope (2006: 29), if the organisation was just approaching the end of the quarter one of the fiscal year. The management team gets the actuals for that quarter and starts to review the next four quarters ahead. Three of these quarters are already part of the original plan or budget but a further quarter needs to be added (quarter one of the following fiscal year). By definition, the fiscal year-end is always on a 12-18 month rolling forecast

According to KPMG (2010: 3) more companies are realising the limitations of the static annual plan and the shortcomings of limited horizon forecasting geared at fiscal year-end. To correct this, they are implementing rolling forecasts that consider a range of potential scenarios.

PricewaterhouseCoopers (2007: 27) mention that employing rolling forecasts enables the organisation to react quickly to market conditions and alter long range plans accordingly without worrying about artificial end points, like the end of a fiscal period.

With re-forecasting and rolling forecasts, organisations have the opportunity to change certain key assumptions in line with current and emerging market trends. A value-adding budgeting, forecasting and financial planning process is therefore dependant on the annual budget being able to accommodate change.
3.2.4 Performance measurement

According to Deloitte Consulting LLP (2010b: 4) too many companies put tremendous effort in the planning, budgeting and forecasting process, only to have much of that work wasted by not having the right information available to make sure they stay on track. The most fundamental planning, budgeting and forecasting value adding capability is the measurement of actuals against plan.

Grigore, Bagu and Radu (2009: 278) argue that the performance measurement process collects, processes, and distributes data to allow an effective execution of the other sub-processes. This information is presented in the form of key performance indicators (KPI’s) and these KPI’s must be guided by the strategic plan. Reviewing actual performance against planned targets ensures that timely preventative and corrective action is taken to keep the organisation on track.

Botten (2008: 416) cites the following reasons why organisations should measure performance:

- check position. Allows management to understand how well the business is performing at present
- communicate position. This ensures that stakeholders are aware of how the business is performing
- confirm priorities. Setting targets for particular aspects of the business so that management can focus on these targets
- compel progress. If the goals of the business are not being reached, performance measurement would highlight where action is needed forcing management to act

The quality of budget and forecast information and timing of these reviews against the plan are crucial. Shortcomings of organisational performance measurement are cited by Grigore et al (2009: 279) as poor quality of budgets and targets and bad timing of performance reviews.
Deloitte & Touche LLP (2009: 6) mention the following symptoms of ineffective performance measurement systems:

- reporting and analysis efforts fail to highlight potential issues in a timely manner
- inability of existing technology to effectively manage and analyse performance management data

This aspect of the budgeting and forecasting process is where the most value can be added to strategic decision-making. Reviewing actual performance against plan is very important, not to point out the inefficiencies in the plan and allocate blame but rather to learn from the variances and ultimately have them influence the organisations strategic direction. According to Barrett and Hope (2006: 29) these reviews should focus on strategy and improving initiatives rather than the numbers. They should help answer questions such as have we got the right products? Are we focused on the right markets? Have we got the right value proposition?

3.3 THE ROLE OF THE FINANCE DEPARTMENT

Budgeting, forecasting and financial planning, when it’s done right, can be a valuable tool in the strategic decision-making process. It helps improve the organisations ability to identify new opportunities and manage potential risks.

According to KPMG (2010: 3) leadership for this process rests with the finance role within the organisation. Finance should promote wider cultural change by putting budgeting and forecasting at the centre of strategic decision-making and engaging with leaders and stakeholders within the organisation to ensure that plans focus on the things that really matter.

PricewaterhouseCoopers (2007: 39) states that the finance department is in a unique position to drive change and realign organisational behaviours that are impacted by the financial planning process. Finance must collaborate to translate organisational strategies into financial targets as well as link operational activities with financial targets. Thomson (2007: 22) mentions
that management accountants and the finance function have the opportunity to influence operations, value creation and business performance by being involved in the organisations multi-year strategic plans, budgets and forecasts.

Lack of cross departmental collaboration in the financial planning process is a key limitation of traditional budgeting. PricewaterhouseCoopers (2007: 40) further states that optimal financial budgeting and forecasting processes require a strong degree of interaction between finance, operations and business unit managers. Finance must use periodic budgeting and forecasting processes to better understand the business and make planning activities part of the corporate culture by driving the collaboration between departments.

Jackson, Sawyers & Jenkins (2009: 33) suggest that management accountants in many organisations today focus on analysing information and creating knowledge from it rather than collecting and processing it. They have become decision-support specialists who see their role as facilitator of management decision-making. In table 3.1, Thompson (2007: 22) outlines the results of a job analysis conducted by the Institute of Certified Management Accountants (ICMA) in March 2006. It lists strategic planning as number 1 and budget preparation as number 5 under most important knowledge and skills a management account should possess.
TABLE 3.1: Knowledge and skills management accountants need to possess

(Source: Thomson 2007: 22)

Management accountants and the finance function have a key role in the planning activities of the organisation. In table 3.2, Thomson (2007: 25) further outlines key planning activities and the role of the management accountant.

<table>
<thead>
<tr>
<th>Strategic Planning</th>
<th>87%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Organisation Management</td>
<td>83%</td>
</tr>
<tr>
<td>Decision Analysis</td>
<td>78%</td>
</tr>
<tr>
<td>Financial Statement Analysis</td>
<td>75%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Budget Preparation</th>
<th>75%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Information Management</td>
<td>74%</td>
</tr>
<tr>
<td>Performance Measurement</td>
<td>71%</td>
</tr>
<tr>
<td>Cost Management</td>
<td>71%</td>
</tr>
<tr>
<td>Internal Controls</td>
<td>70%</td>
</tr>
<tr>
<td>Business Process</td>
<td>66%</td>
</tr>
<tr>
<td>Investment Decisions</td>
<td>64%</td>
</tr>
<tr>
<td>Business Economics</td>
<td>63%</td>
</tr>
<tr>
<td>External Reporting</td>
<td>63%</td>
</tr>
<tr>
<td>Strategic Marketing</td>
<td>58%</td>
</tr>
<tr>
<td>Global Business</td>
<td>57%</td>
</tr>
<tr>
<td>Quantitative Methods</td>
<td>56%</td>
</tr>
<tr>
<td>Corporate Finance</td>
<td>53%</td>
</tr>
<tr>
<td>Operational Paradigms</td>
<td>51%</td>
</tr>
</tbody>
</table>
### TABLE 3.2: Key planning activities and management accountants

<table>
<thead>
<tr>
<th>KEY PLANNING ACTIVITY</th>
<th>ROLE OF THE MANAGEMENT ACCOUNTANT: FINANCE FUNCTION</th>
<th>SUGGESTED FREQUENCY</th>
</tr>
</thead>
<tbody>
<tr>
<td>Setting/Validating the vision and mission</td>
<td>Contributing to feedback sessions to set or validate the vision and mission</td>
<td>Every three years</td>
</tr>
<tr>
<td>Environmental scan / Business landscape</td>
<td>Research and synthesize intelligence on key environmental factors, including regulatory environment and competitors</td>
<td>Every three to six months</td>
</tr>
<tr>
<td>Product and Market Priorities</td>
<td>Identify key market segments, inventory current products and service set, and determine the priority products and markets for resource allocation, market launches, etc.</td>
<td>Every six to 12 months</td>
</tr>
<tr>
<td>Strategic Change Portfolio</td>
<td>Work with cross-functional teams to create and update strategic initiatives that overlay the multiyear baseline view to achieve strategic goals</td>
<td>Every six to 12 months</td>
</tr>
<tr>
<td>Determine measures of success:</td>
<td>Key role for the management accountant in terms of determining goals, key financial and non-financial measures (e.g., used of balanced scorecard and strategy maps), long-run forecasting of key measures, budget expense detail for first year of plan, etc.</td>
<td>12 months (budget/plan cycle) supplemented by periodic in-year outlook updates.</td>
</tr>
<tr>
<td>Develop, deploy and sustain a continuous improvement process</td>
<td>Work closely with cross-functional teams to support or lead continuous improvement efforts for one of the organisations most critical business processes: strategic planning, budgeting and forecasting</td>
<td>Ongoing</td>
</tr>
</tbody>
</table>

(Source: Thomson 2007: 25)

### 3.3.1 Financial planning meetings and discussion forums

As previously discussed, the finance department is responsible for preparing the annual budget and periodically re-forecasting that budget. This process is dependent on input from all functional arrears within the organisation, using the manufacturing industry as an example; the input would look as follows:

- projected sales volumes and product pricing will be provided by marketing
- a production plan prepared by the production department
- based on the production plan, a projected direct labour cost
- a projection of material handling and transportation costs supplied by logistics
- a projection of material cost inflation, purchasing negotiates this with suppliers
- the treasury function should provide input regarding the macro-economic environment for example, assumptions regarding gross domestic product, prime interest rates, consumer price inflation

These inputs, among others, are provided to finance to prepare a financial evaluation for top management. Meetings are held with the various functional areas to discuss these inputs before using them in the financial plan. According to Bester (2012) one of the critical success factors of the budgeting, forecasting and financial planning process is the administration of meetings to discuss and approve inputs. Finance is directly responsible for the success and usefulness of these discussions and they must include the following:

- detailed agenda
- minutes of meetings
- follow-up discussions on unresolved issues
- each department must present and validate their inputs

Bester (2012) further states that there should be constant dialogue between finance and the other functional areas of the organisation during the budgeting process. Formal meetings are not necessary to agree and change inputs, discussion forums via email or telephone are also useful as long as there is documented consensus regarding issues discussed. These discussion forums, in smaller groups, can help reduce planning cycle times drastically.
3.3.2 Financial Analysis

Farrel and Geere (2012: 1) state that there are many opportunities for the finance function to use analytics or financial analysis, which is the practice of using data to enhance business performance by making more effective decisions and actively incorporating insights gained from this data into business processes.

3.3.2.1 Driver-based forecasting

Enhanced forecasts can improve decision-making. Decisions regarding whether to target customers and growth, improve financial asset management or simply re-directing business strategy, knowing what is going to happen next and planning the business response is critical (Farrel & Geere, 2012: 1).

3.3.2.2 Financial reporting

Finance functions typically need to simplify, streamline and industrialise the process in order to be able to move onto value-adding financial analysis (Farrel & Geere, 2012: 2).

3.3.2.3 Treasury

According to Farrel and Geere (2012: 3) the treasury function can use analysis to enhance financial risk management to adapt to or exploit market volatility. Key areas include:

- funding risks: sensitivity analysis
- hedging: forecasting, management and monitoring of net exposure to foreign currencies
- cash flow: customer profitability analysis
### 3.3.3 Process improvement

In figure 3.2, Deliotte & Touche LLP (2009: 11) illustrate the following ways the finance function in leading organisations are improving their planning process.

**Figure 3.2: Best practices to improve planning processes and enhance their value**

- **Key performance indicators (KPIs)**
  - Identification of the most significant measures of business performance
  - **Key benefit:** better alignment between strategy and execution

- **Rolling forecasts**
  - Expansion of forecast horizon beyond current fiscal year
  - **Key benefit:** better insight into market conditions and expected performance

- **Driver-based planning**
  - Planning models based on major internal and external factors that influence performance
  - **Key benefit:** more accurate plans and better insight into performance drivers

- **Capital Allocation**
  - Focusing capital spend on projects or initiatives that drive value
  - **Key benefit:** better return on investment for key initiatives

- **Scenario Analysis**
  - Using various assumptions to gauge bottom line impact, ‘what-if’ analysis
  - **Benefit:** better decision making that includes consideration for all business scenarios

(Source: Deliotte & Touche LLP 2009: 11)

The finance department is tasked with the challenge of continuously improving the budgeting, forecasting and financial planning process. Two key ways in which the finance department can add value to strategic decision-making is through the following:
3.3.3.1 Driver-based planning

Budgets and forecasts should be based on the key drivers that affect financial performance. The finance function is responsible for sharing these key drivers with the rest of the organisation, not just to present the financial evaluation as the result of the shared input by all contributors in the process. Understanding the key drivers of financial performance improves the quality of budgeting and forecasting information which improves decision-making (Farrel & Geere, 2012; KPMG, 2010).

3.3.3.2 Scenario analysis

KMPG (2010: 2) suggests that the finance department should focus on a range of alternative situations and assess the financial impact of each alternative. According to Castellina and Hatch (2011: 21) certain factors have huge implications on plans meaning they must be considered to make informed budgets and forecasts. Leading organisations are 44 per cent more likely than all others to know the effect of events going into their planning. Castellina and Hatch (2011: 14) further state that plans become more informed because they take into account, and can anticipate the impact of potential events.

3.4 THE LINK BETWEEN FINANCIAL PLANNING INFORMATION AND STRATEGIC DECISION-MAKING

According to Castellina and Hatch (2011: 18), to make more attainable and strategic business decisions, managers need accurate, relevant and timely information. They need to be able to determine how to accelerate or build on success, as well as how and when to correct course. Olszak (2010: 2) states that the ability of an organisation to take advantage of available information is a critical component for its success.
PricewaterhouseCoopers (2007: 43) argue that budgeting, forecasting and financial planning processes can play a major role in an organisation’s strategic direction by becoming a tool to rapidly assess and adapt to a changing market place. Organisations that take advantage of these processes will:

- use budgeting, forecasting and financial planning as a tool to integrate strategic planning and day-to-day operations
- reduce the planning cycle times and improve forecast accuracy by standardising data collection and consolidation
- shift the focus of the budgeting and forecasting processes from data collection and reporting to target-setting, financial analysis and ongoing measurement
- break organisational ‘silo’s by using the budgeting and forecasting function as a way of increasing collaboration between finance and operations
- increase the organisation’s understanding of creating value through the budgeting and forecasting process and supporting it with a performance measurement and management function

KPMG (2010: 3) states that top executives recognise that without a reliable planning process at the heart of their performance management process, management information will be mired with detail about the past and they are likely to miss key opportunities and inadvertently overlook risks.

### 3.4.1 Support from information systems

In recent years, technology has become a major contributing factor in the value-adding budgeting, forecasting and financial planning process. Management’s responsibility for making informed strategic decisions is dependent on the accuracy, integrity and timeliness of information at their disposal.
Collier and Agyei-Ampomah (2007: 217-218) cite the following information systems which assist top management in the strategic decision-making process:

3.4.1.1 **Management information systems (MIS)**

Management information systems provide managers with information for decision-making and control. Data are drawn from transaction processing systems and produced as reports. It is quite common for information to be extracted from standard reports and transferred to spreadsheets for manipulation and analysis by managers.

3.4.1.2 **Enterprise resource planning systems (ERPS)**

Enterprise resource planning systems help to integrate data flow and access to information over the whole range of a company’s activities. Enterprise Resource Planning Systems typically capture transaction data for accounting purposes, operational data, customer and supplier data which are then made available through data warehouses against which custom-designed reports can be produced.

3.4.1.3 **Strategic enterprise management (SEM)**

Strategic enterprise management is an information system providing the support needed for the strategic management process. It is based on data stored in a data warehouse which is then used by a range of analytical tools. It can be an important driver of organisational performance as it enables faster and better decision-making.
3.4.1.4 Decision support systems (DSS)

Decision support systems contain data analysis models that provide the ability for managers to simulate or ask “What if?” questions so that different options can be considered and information can be obtained to aid in decision-making.

3.4.1.5 Executive information systems

Executive information systems are used for decision support, which incorporates access to summarised data, often in graphical form, to enable senior managers to evaluate information about the organisation and its environment. It uses a ‘drill down’ facility to move from aggregated data down to a more specific and detailed level.

3.4.2 Business intelligence (BI)

According to Olszak (2010: 2) information technology (IT) organisations have, in recent years, begun to focus on turning financial information into business intelligence (BI). This gives decision-makers insight into every area of data stored across the enterprise. The strategic value of BI has led to it becoming a key concentration for today’s IT organisations.

Olszack (2010: 3) suggests that BI implementations no longer provide the competitive advantage they used to, there are two reasons for this:

- BI has become pervasive, organisations cannot gain competitive advantage by doing what everyone else is doing
- BI is focused on providing users with insight into stored data, it does not deliver the tools to make operational changes
3.4.3 Business performance management (BPM)

Olszak (2010: 3) further states that organisations are taking the next step, transforming BI into business performance management (BPM). BPM provides a critical foundation for organisations to manage their businesses and empower individuals to make the right decisions to maximise profitability. BPM links BI to business strategies and processes via business metrics.

Figure 3.3 illustrates the strategic value of financial information in the business performance management model.

Figure 3.3: Business performance management (BPM) model

There are four steps that constitute the closed-loop process created by BPM. Within the framework of each step an organisation has got different techniques and technologies at its disposal. At the first step its mission is defined, key objectives it wants to achieve and a means of measuring these objectives. The next step is the creation of plans and allocation of resources; this is the typical annual budget and target setting. The third step involves monitoring and analysis of carried out plans and the last step refers to improvement of the process.
BPM connects business strategy with planning, budgeting, forecasting and efficiency management.

3.5 CONCLUSION

This chapter dealt with the value-adding budgeting, forecasting and financial planning process in greater detail. A study of related literature confirmed the significance of budgeting and forecasting in strategic decision-making as well as the fundamental aspects of a value-adding financial planning process.

The researcher explored the important role of management accountants and the finance function in a value-adding budgeting, forecasting and financial planning process. It is evident that the finance function has an integral part to play in the organisation gaining strategic insight from financial planning information through financial analysis, reporting, administration and continuously improving the financial planning process.

Lastly, the researcher investigated the link between financial planning information and strategic decision-making. Budgeting, forecasting and financial planning information has to be relevant, timely and accurate in order for it to add value to the user of the information. Organisations have invested significantly in technologies that support the decision-making process; these technologies make financial planning information more accessible and timely for top management.
CHAPTER 4

RESEARCH DESIGN AND METHODOLOGY

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4.3. RESEARCH APPROACH
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CHAPTER 4

RESEARCH DESIGN AND METHODOLOGY

4.1 INTRODUCTION

The aim of this chapter is to present an overview of the various research methods in general and to indicate the specific methodology used for this research study. The main problem identified in chapter one was to assess whether organisations add value to their strategic decision-making through budgeting, forecasting and financial planning. In order to solve the main problem, the following sub-problems should be addressed:

- the limitations of the traditional budgeting and forecasting processes
- the factors influencing the quality of budget and forecast accuracy
- the role of the finance department in a value-adding financial planning process
- the role of financial planning information in the strategic decision-making process

The questionnaire design, selection of the sample, administration of the questionnaire, as well as an account of the actual response rate are covered in this chapter.

4.2 RESEARCH DESIGN

4.2.1 The concept of research

Welman, Kruger and Mitchell (2005: 2) define research as a process that involves obtaining scientific knowledge by means of various objective methods and procedures. The term objective indicates that these methods and procedures do not rely on personal feelings or opinions. Welman, Kruger and Mitchell (2005: 3) further states that research is a process of using scientific methods to expand knowledge in a particular field of study.
Pellissier (2007: 6) describes research as a systematic investigation to established facts.

Leedy and Ormrod (2005:2) point out that the following characteristics are typical of research:

- research starts with a question or problem
- research needs a clear goal
- research divides the main problem into smaller sub-problems
- research is directed by the research problem, questions, or hypothesis
- research accepts certain vital assumptions
- research requires the collection and interpretation of data in order to resolve the problem that initiated the research
- research follows a cycle comprising of logical steps

4.2.2 The concept of research design

Welman, Kruger and Mitchell (2005: 52) states that research is conducted to investigate a research hypothesis or research question, data is collected from the participants or objects of the enquiry in order to solve the problem concerned. A crucial element in research is the research design. Research design is the plan according to which research participants are obtained and how data is collected from them. According to Zikmund (2003: 65) research design is the master plan specifying the methods and procedures for collecting and analysing the needed information.

Zikmund (2003: 65) indicates four basic research design techniques available for data collection:

- Surveys;
- Experiments;
- Secondary data studies;
- Observation.
Zikmund (2003: 66) further states that the objective of the research methods, the available data sources, the urgency of the decision and the cost of obtaining the data will determine which technique is chosen.

4.3 RESEARCH APPROACH

4.3.1 Qualitative approach

According to Johnson and Christensen (2008: 34) qualitative research relies primarily on the collection of qualitative (non-numerical data such as words and pictures) data.

Welman, Kruger and Mitchell (2005: 188) refer to it as an array of techniques which seek to describe, decode, translate, and otherwise come to terms with the meaning of naturally occurring phenomena. Welman, Kruger and Mitchell (2005: 193) further outline the use of five data collection methods used by qualitative research, namely:

4.3.1.1 Case study research

The term case study pertains to the fact that a limited number of units of analysis (often only one) are studied intensively. The units of analysis include individuals, groups and institutions. The term case study does not refer to a specific technique that is applied but rather directed towards understanding the uniqueness of a particular case in all its complexities.

4.3.1.2 Participant observation

According to Welman, Kruger and Mitchell (2005: 194) participant observation requires the researcher, for an extensive period of time, to take part in, and report on, the daily experiences of the members of a group, community or organisation, or the people involved in a process or event. In
participant observation the aim is not to observe the experiences of the individuals involved as detached outsiders but rather experience them first-hand as insiders.

4.3.1.3 Unstructured, in-depth interviews

Welman, Kruger and Mitchell (2005: 198) mention that in unstructured interviews an attempt is made to understand how individuals experience their life-world and how they make sense of what is happening to them. The interviewer simply suggests the general theme of the discussion and poses further questions as these come up in the spontaneous development of the interaction between interviewer and research participant.

4.3.1.4 Focus groups

Focus groups consist of a small number of individuals or interviewees that are drawn together for the purpose of expressing their opinions on a specific set of open questions. The aim of using such focus groups is to gather information that can perhaps not be collected easily by means of individual interviews.

4.3.1.5 Participatory research

According to Welman, Kruger and Mitchell (2005: 205) participatory research involves the integration of elements such as social investigation, educational work and action in an interrelated process. In participatory research the roles of the researcher and participant are as follows:

- the participants are actively involved in the planning and implantation of the research outcomes and are thus empowered
- the researcher is dependent on the participation of research group or individuals
4.3.2 Quantitative approach

Welman, Kruger and Mitchell (2005: 8) state that quantitative research emphasises the measurement and analysis of casual relationships between variables. The purpose of quantitative research is to evaluate objective data consisting of numbers. Johnson and Christensen (2008:33) refer to quantitative research as “research that relies primarily on the collection of quantitative (numerical) data.”

Welman, Kruger and Mitchell (2005: 78) outline the use of three quantitative research approaches:

4.3.2.1 Experimental research

All types of experimental research involve some sort of intervention. In other words, the participants (units of analysis) are exposed to something to which they would not have been subjected to otherwise. In the hypothesis we express the influence that the independent variable is expected to have on the dependant variable and it is this influence that is measured in the experiment.

4.3.2.2 Quasi-experimental research

According to Welman, Kruger and Mitchell (2005: 88) quasi-experimental research differs from true experimental research in that the researcher cannot randomly assign subjects to different groups. It presents a second best alternative to eliminating known nuisance variables as far as possible, and the corresponding rival hypothesis on logical grounds.
4.3.2.3 Non-experimental research

Welman, Kruger and Mitchell (2005: 92) state that in this type of research one or more variables, apart from the independent variable in question, could be the actual source of observed variation in the independent variable(s). It is therefore accepted that conclusions about casual relationships may be made with greater confidence by means of true experimental research.

4.3.3 Mixed research

Johnson and Christensen (2008: 34) refer to mixed research as research that includes the mixing of quantitative and qualitative methods or other paradigm characteristics. The research questions and the situational and practical issues facing the researcher will determine the appropriate mixture of the two approaches.

Johnson and Christensen (2008: 35) argue that the use of only quantitative research or qualitative research is seen to be limiting and incomplete for many research questions. Johnson and Christensen (2008: 51) further state that by following a mixed research approach, the quality of the research improves and the researcher is less likely to make an error due to the different strengths and weaknesses of the research methods.

4.4 APPROPRIATE RESEARCH APPROACH

The researcher has chosen to use a combination of qualitative and quantitative approaches. In order to fully answer the main research question raised at the beginning of this study, Dichotomous, open-ended and close-ended questions have been included in the survey.
4.5 SAMPLE SELECTION

As indicated in chapter 1, this research study has been restricted to companies with operations in the Eastern Cape’s manufacturing industry. The population consists of the following companies:

- Volkswagen of South Africa (Pty) Ltd
- General Motors South Africa
- REHAU Polymer (Pty) Ltd
- Aspen Pharmacare
- Shatterprufe (Pty) Ltd
- Goodyear South Africa
- SJM Flex SA (Pty) Ltd
- Eberspaecher South Africa (Pty) Ltd
- Corning SA (Pty) Ltd
- BASF (Pty) Ltd
- Shaefller South Africa (Pty) Ltd

4.6 STRUCTURE OF THE QUESTIONNAIRE

The nature of this research topic dictated the use of a questionnaire survey as the primary research tool. Questionnaires are very structured data collection techniques in which respondents are asked the same set of questions. The questionnaire was developed from the literature review in chapter 2 and chapter 3.

The questionnaire (Annexure A) is divided into two sections. Section A contains four questions designed to obtain particular biographic information about the respondents such as their age, job titles, experience and qualifications. Section B consists of questions which were designed to research both general and specific aspects of budgeting, forecasting and financial planning.

The following types of questions were used in the questionnaire:
• Dichotomous questions. The respondents are offered a choice between two options only, for example “Yes” or “No”
• Scaled-response questions. The five point Likert-scale, ranging from strongly agree to strongly disagree, was used to determine respondents’ level of agreement on a given subject. It included a middle point reflecting the neutral responses
• Open-ended questions. Respondents are allowed to answer in their own words and freely express themselves. The number of these questions were kept to a minimum as it was felt that respondents react better to the first two types of questions as less time is spent completing the questionnaire

4.7 ADMINISTERING THE QUESTIONNAIRE

The researcher established contact with an individual in the finance department of each of the 11 companies either telephonically or via email. These individuals were made aware of the research project and asked to discuss it with the person(s) in their company responsible for budgeting and planning. Once these individuals indicated their willingness to participate in the survey a cover letter and questionnaire was emailed to them on 20 August 2012. The cover letter provided the respondents with a brief background and purpose of the research project. Further, respondents were requested to return the completed questionnaire by 21 September 2012.

4.8 EXTENT OF RESPONSES

Responses were sought from companies operating in the Eastern Cape manufacturing sector. As previously stated, the researcher set out to make contact with a finance representative at each of the companies in the population to sensitise these companies to the survey and also obtain a tentative agreement of their willingness to participate in the survey.
This initial contact and discussion secured a high response rate with 10 of the 11 companies completing the questionnaire on or before the due date. The respondents printed the questionnaire emailed to them, completing and returning it to the researcher via email. Whilst this is a relatively high response rate for the study it should be taken into account that the population (11 companies) is small and ideally a 100% response rate would be conclusive regarding the industry.

However, the population consists of two of the seven motor vehicle manufacturers in South Africa as well as a few of their main component suppliers with operations in the Eastern Cape. To gain further perspective in the study, two of the companies in the population had operations outside of the automotive sector. Consequently, the researcher is of the view that the results obtained from the study do present a fair reflection of the industry.

4.9 CONCLUSION

This chapter outlined the purpose of research in general and described the difference between qualitative and quantitative research. The research strategy found most suitable for this project was a mixed research approach, which is a combination of qualitative and quantitative methods. The design of the questionnaire, selection of the sample and extent of responses was also discussed in this chapter. Chapter 5 will address the empirical findings of the study.
CHAPTER 5

EMPIRICAL FINDINGS AND PRESENTATION OF RESULTS

5.1. INTRODUCTION

5.2. BIOGRAPHICAL DETAILS OF RESPONDENTS
   5.2.1. Current age in years
   5.2.2. Job titles
   5.2.3. Number of years business experience
   5.2.4. Highest academic qualification/professional association

5.3. ACHIEVEMENT OF THE RESPECTIVE STUDY OBJECTIVES
   5.3.1. Primary objective: Assess whether organisations add value to strategic decision-making through their budgeting, forecasting and financial planning
   5.3.2. Sub-objective 1: To investigate current organisational paradigms towards budgeting, forecasting and financial planning
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CHAPTER 5
EMPIRICAL FINDINGS AND PRESENTATION OF RESULTS

5.1 INTRODUCTION

The aim of this chapter is to present an overview of the biographical details of the respondents and the empirical findings of the respective research objectives. A survey was conducted to assess whether organisations in the Eastern Cape’s manufacturing industry use budgeting, forecasting and financial planning as a strategic tool in the decision-making process. Tables and figures are used to present the empirical findings of the study which are based on summaries of the questionnaire responses.

5.2 BIOGRAPHICAL DETAILS OF RESPONDENTS

Section A of the questionnaire consisted of four questions designed to obtain certain biographical information of the respondents such as age, job title, number of years’ experience in the finance function and academic background.

5.2.1 Current age in years

Figure 5.1 shows the distribution of respondents according to their current age in years. A high percentage (70%) of the respondents are between the ages of 30 and 40 years old whilst 20% are between the ages of 40 and 50 years. The remainder of respondents are between the ages of 20 to 30 years.
5.2.2 Job titles

Figure 5.2 shows the distribution of respondents according to their job titles or positions held in the company. Out of a total of 10 respondents, 50% indicated that they were management accountants. Financial managers comprises of 30%, financial controller and treasurer shared 10% of the population.
5.2.3 Number of years business experience in the finance function

Figure 5.3 shows the distribution of respondents according to the number of year’s business experience, specifically in the finance function. The majority of respondents (60%) have between 10 and 20 years’ experience in the finance function.

Figure 5.3: Years of business experience in the finance function

5.2.4 Highest academic qualification/professional association

Figure 5.4 shows the distribution of respondents according to the academic qualifications or professional association they hold. Of those respondents, 40% have achieved a Bachelor’s Degree whilst 30% are professional Chartered Accountants CA(SA). National Diplomas are held by 20% of the respondents with the remaining 10% achieving National Higher Diplomas.
5.3 ACHIEVEMENT OF THE RESPECTIVE STUDY OBJECTIVES

The questionnaire contained specific questions that were posed to the respondents in order to get their responses with regards to budgeting, forecasting and financial planning. These questions were aimed at addressing the study’s main and sub-objectives as stated in Chapter 1. Further, the empirical findings for each objective are also discussed in this section.

5.3.1 Primary objective: Assess whether organisations add value to strategic decision-making through their budgeting, forecasting and financial planning

To address this objective, the following questions were included in the questionnaire:

- Q2.1 Does your company prepare an annual budget?
- Q2.2 How long does your company take to complete and approve the annual budget?
Q2.3 Which areas/departments are involved in the annual budgeting process?

Q2.4 Are there any other areas/departments in your organisation that are involved in the annual budgeting process?

Q2.5 Does your company re-forecast or update the annual budget, based on latest actuals and updated assumptions?

Q2.6 If yes, how often is your annual budget updated/re-forecasted?

Q2.7 Do you regard this update/re-forecast of the budget to be useful to your organisation?

The responses to these questions are discussed below.

Q2.1. Does your company prepare an annual budget?

All respondents indicated that their companies do prepare an annual budget.

Q2.2. How long does your company take to complete and approve the annual budget?

Figure 5.5 shows the distribution of respondents according to how long it takes their companies to complete and approve the annual budget. The majority of respondents (70%) indicated that it takes their organisations between 2 and 4 months to complete and approve the annual budget whilst the remaining 30% take between 4 and 6 months to do the same.
Figure 5.5: Distribution of respondents according to how long it takes to complete and approve the annual budget

Q2.3. Which areas/departments are involved in the annual budgeting process?

A vital element of the value-adding budgeting, forecasting and financial planning process is cross-departmental collaboration. In order to determine which departments are involved the financial planning process, respondents were requested to indicate from a list of departments provided, which departments are involved in the organisations budgeting and forecasting process. Figure 5.6 shows the areas/departments that are involved in the budgeting, forecasting and financial planning process.
Ten respondents completed the questionnaire for this study. As depicted in Figure 5.6, all ten respondents indicated that marketing and finance/accounting are involved in the budgeting process. Nine respondents indicated that production/manufacturing and purchasing departments are involved in the process. Seven respondents indicated that logistics is involved in budgeting with the product design/development department showing the least involvement in the process.

**Q2.4. Are there any other areas/departments in your organisation that are involved in the annual budgeting process?**

Respondents were asked to indicate whether there are any additional areas/departments, not included in Figure 5.6, involved in their budgeting and forecasting process. Four additional areas/departments were mentioned by the respondents, namely:

- human resources
- information technology (IT)
- quality
- project management
Q2.5. Does your company re-forecast or update the annual budget, based on latest actuals and updated assumptions?

All respondents indicated that once the annual budget is approved, a re-forecast or update of the budget is performed based on latest actuals or updated assumptions. It is important to note that the majority of respondents indicated that even though a forecast or update was performed, the approved annual budget remained fixed throughout the year in terms of its use in performance measurement. This re-forecast or update of the budget is performed to add value to financial planning and give better insight into changing markets conditions.

Q2.6. If yes, how often is your annual budget updated/re-forecasted?

Figure 5.7 shows the distribution of respondents according to how often their annual budget is re-forecasted or updated. The responses were fairly evenly spread between monthly and quarterly with 40% of the respondents indicating a monthly re-forecast whilst 50% indicated these forecasts were performed on a quarterly basis. 10% of the respondents indicated that this was only done bi-annually and a special footnote was added to indicate that it was also performed on a 'need-to' basis depending on major impacting events.
Q2.7. Do you regard this update/re-forecast of the budget to be useful to your organisation?

All respondents answered positively to this question indicating that the update/re-forecast of the annual approved budget using latest actuals and updated assumptions is useful to their organisation.

5.3.2 Sub-objective 1: To investigate current organisational paradigms towards budgeting, forecasting and financial planning

The purpose of this sub-objective was to gain insight into current organisational paradigms with regard to budgeting, forecasting and financial planning. The literature review in chapters two and three revealed certain limitations or drawbacks to the traditional budgeting approach as well as the advantages of updating/re-forecasting the annual budget. The following questions were included in the questionnaire to address this sub-objective:

- Q2.8 The following factors are considered to be limitations of the traditional budgeting approach. Indicate your level of agreement on these factors
Q2.10 In your opinion, are there any other limitations/drawbacks of the budgeting process in general?

Q2.9 The following statements relate to updating/re-forecasting the annual budget. Indicate your level of agreement on these statements.

Feedback from respondents is discussed below.

**Q2.8. Indicate level of agreement on factors considered to be limitations/drawbacks of traditional budgeting approach**

To assist in addressing sub-objective 1 of this study, respondents were asked to indicate their level of agreement with factors perceived to be limitations/drawbacks of the traditional budgeting approach identified from the literature review.

Table 5.1 reflects the responses given by the respondents for question Q2.8.

**Table 5.1: Summary of responses (expressed in %) with regard to limitations/drawbacks of the traditional budgeting approach.**

<table>
<thead>
<tr>
<th></th>
<th>Strongly disagree</th>
<th>Disagree</th>
<th>Neutral</th>
<th>Agree</th>
<th>Strongly Agree</th>
</tr>
</thead>
<tbody>
<tr>
<td>a</td>
<td>10,0</td>
<td>30,0</td>
<td>0,0</td>
<td>50,0</td>
<td>10,0</td>
</tr>
<tr>
<td>b</td>
<td>10,0</td>
<td>30,0</td>
<td>10,0</td>
<td>20,0</td>
<td>30,0</td>
</tr>
<tr>
<td>c</td>
<td>10,0</td>
<td>40,0</td>
<td>10,0</td>
<td>20,0</td>
<td>20,0</td>
</tr>
<tr>
<td>d</td>
<td>10,0</td>
<td>50,0</td>
<td>20,0</td>
<td>20,0</td>
<td>0,0</td>
</tr>
<tr>
<td>e</td>
<td>0,0</td>
<td>50,0</td>
<td>20,0</td>
<td>20,0</td>
<td>10,0</td>
</tr>
<tr>
<td>f</td>
<td>0,0</td>
<td>50,0</td>
<td>40,0</td>
<td>10,0</td>
<td>0,0</td>
</tr>
</tbody>
</table>
An analysis of responses indicates that ‘length of budgeting/planning cycles’ and ‘more time is spent creating, than analysing the budget’ are the two items which respondents consider to be the main limitations of the traditional budgeting approach. These items scored agreement rates of 60% and 50% respectively. ‘Lack of cross-departmental collaboration’ scored moderately achieving an agreement rate of 40%.

The rest of the items (items d to f in Table 5.1) scored low, achieving an average agreement rate of only 20%. This would suggest that the respondents do not consider these items to be significant limitations or drawbacks of the traditional budgeting approach.

Q2.10. In your opinion, are there any other limitations/drawbacks of the budgeting process in general?

Respondents were requested to indicate whether there are any other limitations or drawbacks of the traditional budgeting approach, not listed in Table 5.1. Question 2.10 was open-ended thus allowing respondent’s to answer freely and in their own views. Below is a summary of the responses obtained:

- lack of involvement from directors and top management
- budgets are viewed as a finance process, therefore no ownership by other departments
- budgets are prepared too far in advance, volumes and exchange rates will change
- budget profit before interest and taxes (PBIT) agreed before the budget is complete
- budgets can be unrealistic when trying to achieve pre-determined targets

Q2.9. Indicate level of agreement on statements relating to updating/re-forecasting the annual budget
Respondents were requested to indicate their level of agreement with statements relating to the update/re-forecast of the annual budget. Table 5.2 reflects the responses given to question Q2.9.

Table 5.2: Summary of responses (expressed in %) in respect of updating/re-forecasting the annual budget

<table>
<thead>
<tr>
<th></th>
<th>Strongly disagree</th>
<th>Disagree</th>
<th>Neutral</th>
<th>Agree</th>
<th>Strongly Agree</th>
</tr>
</thead>
<tbody>
<tr>
<td>a</td>
<td>It is crucial in today’s rapidly changing business environment</td>
<td>0,0</td>
<td>10,0</td>
<td>0,0</td>
<td>40,0</td>
</tr>
<tr>
<td>b</td>
<td>Enables your organisation to react quickly to market conditions and alter long range financial plans</td>
<td>0,0</td>
<td>10,0</td>
<td>0,0</td>
<td>50,0</td>
</tr>
<tr>
<td>c</td>
<td>Enhances the value of financial planning information used for strategic decision-making</td>
<td>0,0</td>
<td>10,0</td>
<td>0,0</td>
<td>60,0</td>
</tr>
<tr>
<td>d</td>
<td>Planning tools/systems should be flexible enough to update the annual budget</td>
<td>0,0</td>
<td>0,0</td>
<td>10,0</td>
<td>60,0</td>
</tr>
<tr>
<td>e</td>
<td>Updating/re-forecasting the budget adds little value in the financial planning process</td>
<td>20,0</td>
<td>70,0</td>
<td>0,0</td>
<td>10,0</td>
</tr>
</tbody>
</table>

An analysis of responses indicates that respondents agreed with the majority of statements (items a to d in Table 5.2). These items scored very high achieving an average agreement rate of 90%. This would suggest that respondents feel that updating or re-forecasting the annual budget is an integral part of the budgeting, forecasting and financial planning process. Item e in Table 5.2 scored only a 10% agreement rate with 1 respondent feeling that this update or re-forecast add little value in the financial planning process.
5.3.3 **Sub-objective 2: To explore the various factors influencing budget and forecast accuracy and quality**

A literature review was conducted in chapter two and chapter three where certain factors were identified as important to maintaining budget and forecast accuracy and quality. The purpose of this sub-objective is to explore whether the organisations participating in the study firstly, agreed with these factors and secondly, whether their planning processes took cognisance of them. To address this sub-objective, the following questions were included in the questionnaire:

- **Q2.13** The following are considered to be factors that influence budget and forecast accuracy and quality. Indicate your level of agreement on these factors.
- **Q2.14** Are there any other factors (not listed in Q2.13) which you regard as relevant in maintaining budget and forecast accuracy and quality?
- **Q2.11** Does your company validate and test the plausibility of major assumptions used in the budget or forecast?
- **Q2.12** When preparing the budget or forecast, what is your company’s planning horizon? How far out does the budget or forecast extend?
- **Q2.15** Does your company make use of a special software application for financial planning and analysis?

Feedback from respondents is discussed below.

**Q2.13. Indicate level of agreement on factors that influence budget and forecast accuracy and quality**

Respondents were requested to indicate their level of agreement on factors that influence budget and forecast accuracy and quality. Table 5.3 reflects the responses given for question Q2.13.
### Table 5.3: Summary of responses (expressed in %) in respect of factors influencing budget and forecast accuracy and quality

<table>
<thead>
<tr>
<th></th>
<th>Strongly disagree</th>
<th>Disagree</th>
<th>Neutral</th>
<th>Agree</th>
<th>Strongly Agree</th>
</tr>
</thead>
<tbody>
<tr>
<td>a</td>
<td>The organisation's attitude/culture towards planning</td>
<td>0.0</td>
<td>0.0</td>
<td>20.0</td>
<td>60.0</td>
</tr>
<tr>
<td>b</td>
<td>Validation and testing of assumptions</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>90.0</td>
</tr>
<tr>
<td>c</td>
<td>A focus on improving forecast accuracy</td>
<td>0.0</td>
<td>10.0</td>
<td>0.0</td>
<td>70.0</td>
</tr>
<tr>
<td>d</td>
<td>Uncertainty in the external business environment</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>50.0</td>
</tr>
<tr>
<td>e</td>
<td>Frequency and level of detail</td>
<td>0.0</td>
<td>10.0</td>
<td>0.0</td>
<td>80.0</td>
</tr>
<tr>
<td>f</td>
<td>Systems and technologies used for planning and analysis</td>
<td>0.0</td>
<td>0.0</td>
<td>10.0</td>
<td>70.0</td>
</tr>
</tbody>
</table>

An analysis of the responses indicates that all the factors listed in Table 5.3 are considered relevant in maintaining budget and forecast accuracy and quality. Two items, namely, validation and testing of assumptions and uncertainty in the external business environment scored 100% agreement rates. Items c, e and f in Table 5.3 scored 90% agreement rates.

**Q2.14. Are there any other factors (not listed in Table 5.3) which you regard as relevant in maintaining budget and forecast accuracy and quality?**

Respondents were requested to indicate if there are any other factors, not listed in Table 5.3, which they regard as relevant in maintaining budget and forecast accuracy and quality. A summary of the responses obtained follows:

- the quality of figures on which the budget is based is crucial. Information must be complete, plausible and understood
• the budget or forecast should take into account changes in manufacturing processes and new technologies
• depending on the size of the company, there should be a specialist focus on improving the forecasting process

Q2.11. Does your company validate and test the plausibility of major assumptions used in the budget or forecast?

All respondents indicated that their companies validate and test the plausibility of major assumptions.

The researcher felt that going deeper into how they tested the assumptions would have been an interesting question but was ultimately outside the scope of the study.

Q2.12. When preparing the budget or forecast, what is your company’s planning horizon? How far out does the budget or forecast extend?

Figure 5.8 shows the distribution of respondents according to how far out their budget and forecast planning horizons extend. Of the ten respondents, 50% indicated that their budgets and forecasts were geared for the next 12 months, 30% indicated the next 18 months and the remainder (20%) > 25 months.

Two of the respondents who indicated that their planning horizon was for the next 12 months also indicated their financial planning process begins with a 5 years medium term plan. Once this 5 year financial evaluation is approved, the first year of this plan is refined and then becomes the annual budget. Therefore, although the budget is for the next 12 months there is a longer range outlook in place to test the plausibility of the plan.
Q2.15. Does your company make use of a special software application for financial planning and analysis?

Respondents were requested to indicate whether their organisations made use of a special software application for financial planning and analysis. Figure 5.9 illustrates the distribution of respondents according to whether they make use of a special software application or not. The majority (60%) of respondents indicated that they did make use of a special software application for their planning and analysis with the remainder indicating otherwise.
An additional question (Q2.16), specifically for the 40% of respondents who answered negatively in Q2.15, was included in the questionnaire to gain insight into the alternatives that these companies employ for financial planning and analysis.

Figure 5.10 shows the distribution of the four respondents, who answered ‘No’ to question Q2.15, according to how they responded to questions asked regarding their non-adoption of financial planning software tools. An analysis of the responses indicates that all four respondents (100%) indicated that their budgets and forecast are prepared in Microsoft Excel. Two of the four respondents (50%) indicated that their organisations have a fairly simple business model that allows for planning and analysis outside of a planning software application and also that they are satisfied with their organisations current planning tools. Three respondents (75%) indicated that their organisation has considered investing in financial planning software.
5.3.4 Sub-objective 3: To explore the role of the finance department in a value-adding budgeting, forecasting and financial planning process

The goal of this sub-objective was to explore the important role of the finance department in a value-adding budgeting, forecasting and financial planning process. The following questions were included in the questionnaire:

- Q2.17 Does your finance department measure budget and forecast accuracy through variance analysis?
- Q2.18 Please indicate the value that variance analysis has in your budgeting and forecasting process?
- Q2.19 When preparing the budget or forecast, does your finance department formally engage with other functional areas to discuss and agree inputs?
- Q2.20 Please indicate how budget assumption inputs are obtained and agreed?
• Q2.21 The following are ways in which the finance department can enhance their financial planning process. Indicate your level of agreement.

Feedback from respondents is discussed below.

Q2.17. Does your finance department measure budget and forecast accuracy through variance analysis?

Respondents were asked to indicate whether their finance department measured accuracy through variance analysis. Three methods were given to respondents, namely:

- budget versus actual
- budget versus forecast
- actual versus forecast

Respondents were requested to indicate yes or no to each of these methods of variance analysis. Figure 5.11 shows the distribution of respondents according to how they answered in question Q2.17. All ten respondents indicated that their finance department did perform budget versus actual variance analysis. Budget versus forecast analysis is performed by eight of the ten companies in the study whilst actual versus forecast is performed by nine. An analysis of the responses indicates that some or other form of variance analysis is performed by the finance department of each company in the sample.
Q2.18. Please indicate the value that variance analysis has in your budgeting and forecasting process? Indicate level of agreement with statements regarding measuring budget and forecast accuracy.

A follow-up question to Q2.17 was posed to the respondents to ascertain the perceived benefits that variance analysis offers in a value-adding budgeting, forecasting and financial planning process. Table 5.4 reflects the responses given to question Q2.18.
Table 5.4: Summary of responses (expressed in %) in respect of the value variance analysis has in the budgeting and forecasting process

<table>
<thead>
<tr>
<th></th>
<th>Strongly disagree</th>
<th>Disagree</th>
<th>Neutral</th>
<th>Agree</th>
<th>Strongly Agree</th>
</tr>
</thead>
<tbody>
<tr>
<td>a</td>
<td>Helps improve the value and credibility of your company’s budgets and forecasts</td>
<td>0,0</td>
<td>0,0</td>
<td>0,0</td>
<td>70,0</td>
</tr>
<tr>
<td>b</td>
<td>Gives your organisation insight into potential risks and opportunities</td>
<td>0,0</td>
<td>0,0</td>
<td>0,0</td>
<td>70,0</td>
</tr>
<tr>
<td>c</td>
<td>Helps keep your organisation on track in achieving its objectives and targets</td>
<td>0,0</td>
<td>0,0</td>
<td>0,0</td>
<td>70,0</td>
</tr>
</tbody>
</table>

An analysis of the responses obtained indicates that all respondents agree that the finance department’s measurement of budget and forecast accuracy through variance analysis has a major role in a value-adding budgeting, forecasting and financial planning process. All items (item a to b in Table 5.4) achieved an agreement rate of 100% with 70% of the respondents agreeing and 30% strongly agreeing.

**Q2.19. When preparing the budget or forecast, does your finance department formally engage with other functional areas to discuss and agree inputs?**

Respondents were requested to indicate whether or not there was a formal process in place and whether the finance department engaged with the other functional areas to discuss and agree budget and forecast inputs. Figure 5.12 shows the distribution of respondents according to whether or not their finance department engages with other function areas to discuss and agree inputs. The majority of respondents (90%) indicated that their finance department formally engages with other function areas during the budgeting and forecasting processes. In chapter three, the important role of the finance department...
department was discussed and a key element of success in a value-adding budgeting, forecasting and financial planning process is the ability of finance to foster cross-departmental collaboration during the financial planning process.

**Figure 5.12:** Distribution of respondents according to whether or not finance department formally engages with other functional areas

| Obtaining budget and forecast inputs |  
|-------------------------------------|----------------------------------|
| Formally engages with other functional areas | 90%                             |
| Does not formally engage with other functional areas | 10%                             |

Q2.20. Please indicate how budget assumption inputs are obtained and agreed?

Respondents were asked to indicate yes or no to a series of questions and statements relating to obtaining and agreeing on budget assumptions and inputs. Table 5.5 reflects the responses given to question Q2.20 and shows the distribution of respondents according to how budget and forecast assumptions and inputs are obtained and agreed.
Table 5.5: Summary of responses (expressed in %) in respect of how budget and forecast assumptions and inputs are obtained and agreed

<table>
<thead>
<tr>
<th></th>
<th>Yes</th>
<th>No</th>
</tr>
</thead>
<tbody>
<tr>
<td>a</td>
<td>Budget and forecast inputs are provided to your finance department without discussion and agreement</td>
<td>10,0</td>
</tr>
<tr>
<td>b</td>
<td>Cross-departmental teams meet regularly during the budget and forecast process to review and approve planning results</td>
<td>90,0</td>
</tr>
<tr>
<td>c</td>
<td>Cross-departmental meetings are considered timely and non-value adding in your planning process</td>
<td>10,0</td>
</tr>
<tr>
<td>d</td>
<td>Do you feel that formalising your financial planning process would improve the value derived from it?</td>
<td>70,0</td>
</tr>
<tr>
<td>e</td>
<td>As a member of your finance department, do you feel there is a lack of ‘buy-in’ from the other functional areas in terms of your financial planning process</td>
<td>40,0</td>
</tr>
</tbody>
</table>

10% of the respondents indicated that inputs and assumptions are not provided to the finance department without first discussing and agreeing on them whilst 90% indicated that cross-departmental teams meet regularly to review and approve planning results. These meetings are considered value-adding to the financial planning process by 90% of the respondents and 70% feel that further formalising the process will improve the value derived from it. Of the 10 respondents, 40% indicated a lack of ‘buy-in’ from the other functional areas in the planning process.
Q2.21. The following are ways in which the finance department can enhance their financial planning process. Indicate your level of agreement.

Respondents were requested to indicate their level of agreement with statements relating to ways in which the finance department can enhance their financial planning process. Table 5.6 reflects the responses given to question Q2.21.

Table 5.6: Summary of responses (expressed in %) regarding ways in which finance departments can enhance their financial planning process

<table>
<thead>
<tr>
<th>Item</th>
<th>Description</th>
<th>Strongly disagree</th>
<th>Disagree</th>
<th>Neutral</th>
<th>Agree</th>
<th>Strongly Agree</th>
</tr>
</thead>
<tbody>
<tr>
<td>a</td>
<td>The use of key performance indicators (KPI’s) to measure what is really important to the organisation</td>
<td>0,0</td>
<td>0,0</td>
<td>0,0</td>
<td>60,0</td>
<td>40,0</td>
</tr>
<tr>
<td>b</td>
<td>Rolling forecast – expanding forecasts beyond the current financial year</td>
<td>0,0</td>
<td>0,0</td>
<td>0,0</td>
<td>60,0</td>
<td>40,0</td>
</tr>
<tr>
<td>c</td>
<td>Budgets and forecasts based on internal and external factors that impact on performance</td>
<td>0,0</td>
<td>0,0</td>
<td>20,0</td>
<td>60,0</td>
<td>20,0</td>
</tr>
<tr>
<td>d</td>
<td>Scenario analysis – doing ‘what if’ analysis on a range of alternative possible outcomes</td>
<td>0,0</td>
<td>0,0</td>
<td>0,0</td>
<td>70,0</td>
<td>30,0</td>
</tr>
<tr>
<td>e</td>
<td>Formalising the budgeting and forecasting process</td>
<td>0,0</td>
<td>0,0</td>
<td>0,0</td>
<td>80,0</td>
<td>20,0</td>
</tr>
</tbody>
</table>

An analysis of responses indicates that the respondents consider all the items listed in Table 5.6 to be ways in which the finance department can enhance their financial planning process. The majority of items (item a, b, d and e in Table 5.6) scored a 100% agreement rates. Item c scored an agreement rate of 80%.
5.3.5 Sub-objective 4: To determine the role of financial planning information in the strategic decision-making of firms.

The goal of this sub-objective was to determine the role that financial planning information has in the strategy of organisations. To achieve this, the following questions were included in the questionnaire:

- Q2.22 The following statements relate to the use of financial planning information in organisational decision-making. Indicate your level of agreement
- Q2.23 How has budget, forecast and financial planning information (including analysis) affected decision-making in your organisation?

Feedback from respondents is discussed below.

Q2.22. The following statements relate to the use of financial planning information in organisational decision-making. Indicate your level of agreement.

Respondents were requested to indicate their level of agreement with statements relating to the use of financial planning information in organisational decision-making. Table 5.7 reflects the responses given to question Q2.22.
Table 5.7: Summary of responses (expressed in %) regarding the use of financial planning information in organisational decision-making

<table>
<thead>
<tr>
<th></th>
<th>Strongly disagree</th>
<th>Disagree</th>
<th>Neutral</th>
<th>Agree</th>
<th>Strongly Agree</th>
</tr>
</thead>
<tbody>
<tr>
<td>a</td>
<td>Financial planning information must be timely, accurate and relevant for it to be useful</td>
<td>0,0</td>
<td>0,0</td>
<td>0,0</td>
<td>40,0</td>
</tr>
<tr>
<td>b</td>
<td>A long range financial outlook can help validate and often change an organisation’s strategic direction</td>
<td>10,0</td>
<td>0,0</td>
<td>10,0</td>
<td>60,0</td>
</tr>
<tr>
<td>c</td>
<td>Value-adding financial planning information is crucial in the decision-making process</td>
<td>0,0</td>
<td>0,0</td>
<td>0,0</td>
<td>70,0</td>
</tr>
<tr>
<td>d</td>
<td>Financial planning systems/tools must be able to accommodate rapid changes</td>
<td>0,0</td>
<td>0,0</td>
<td>10,0</td>
<td>30,0</td>
</tr>
</tbody>
</table>

An analysis of the responses indicates that the majority of respondents agree with all items listed in Table 5.7. Items a and c achieved agreement rates of 100%. One respondent strongly disagreed with item b and included a footnote stating “it should be the other way around”. The researcher suspects this to mean that a firm’s strategic direction should validate and change the long range financial outlook.

**Q2.23.** How has budget, forecast and financial planning information (including analysis) affected decision-making in your organisation?

Question Q2.23 explores how budget, forecast and financial planning information affects decision-making in the organisations. The respondents listed the following example of how financial planning information has affected their organisation’s decision-making:

- improves the timing of corrective actions required to steer against negative profit developments
• assists with major investment and forward cover (exchange rate hedging) decisions
• provides direction and targets for performance management
• assists in determining the optimal efficiency for the organisation when resources such as funding, people and equipment are limited
• manpower planning
• forecasts can identify specific risks that were not evident when preparing the budget
• identify risks on working capital management (liquidity)
• keeps the organisation competitive in a global market – competitor threat
• assists in determining optimal volume and mix on range of product offerings

5.4 CONCLUSION

This chapter presented an overview of the biographical details of the respondents as well as the empirical findings of the study. The results were presented in descriptive terms as well as in graphic and tabular forms. The main conclusions to emerge from this chapter are:

• completed questionnaires were received from 10 of the 11 companies in the sample
• the questionnaires were completed by experience practitioners. The majority of respondents (60%) have between 10 and 20 years’ business experience in the finance function
• all respondents have achieved a tertiary qualification
• all respondents indicated that their companies prepare an annual budget
• all respondents indicated that once an annual budget is approved, a re-forecast of the budget is performed
• ‘length of budgeting/planning cycles’ and ‘more time is spent creating than analysing the budget’ are considered the major drawbacks of the traditional budgeting approach
• the majority of respondents (90%) consider the update or re-forecast of the annual budget to be value-adding in the financial planning process
• all respondents indicated that their companies validate and test the plausibility of budget and forecast assumptions
• 60% of the respondents make use of special software applications for their financial planning and analysis
• the finance department at each of the companies in the sample have an integral role in their financial planning process through variance analysis, formally engaging with other functional areas and preparing quality budgets and forecasts
• the firms use financial planning information to drive major strategic decisions
CHAPTER 6

SUMMARY AND CONCLUSIONS

6.1. INTRODUCTION

6.2. SIGNIFICANT FINDINGS IN RESPECT OF THE RESEARCH OBJECTIVES

6.2.1. Findings: Research objective 1

6.2.2. Findings: Research objective 2

6.2.3. Findings: Research objective 3

6.2.4. Findings: Research objective 4

6.2.5. Findings: Research objective 5

6.3. AREAS FOR FUTURE RESEARCH
CHAPTER 6
SUMMARY AND CONCLUSIONS

6.1 INTRODUCTION

As stated in chapter 1, one of the key challenges facing organisations today is the ability to plan for the future and predict operating performance. An effective, timeous and accurate budgeting, forecasting and financial planning process offers organisations an opportunity to prepare for and be in a position to succeed in a rapidly changing business environment.

Against the knowledge of the importance of timely, accurate and complete financial planning information, the main purpose of this research has been to establish whether organisations add value to strategic decision-making through their budgeting, forecasting and financial planning information. In support of the main research purpose, the study focused on achieving the following sub-objectives:

- to investigate current organisational paradigms towards budgeting, forecasting and financial planning
- to explore the various factors influencing budget and forecast accuracy and quality
- to explore the role of the finance department in a value-adding budgeting, forecasting and financial planning process
- to determine the role of financial planning information in the strategic decision-making of firms

The objectives of the study were achieved by performing an in-depth study on budgeting, forecasting and financial planning as presented in the literature.

The empirical survey entailed self-administered questionnaires being sent to companies in the Eastern Cape’s manufacturing sector. In the rest of this
chapter, the significant empirical findings that emerged from the study will be summarised. After this, areas for future research are considered.

6.2 SIGNIFICANT FINDINGS IN RESPECT OF THE RESEARCH OBJECTIVES

The findings of the empirical surveys and the interpretation thereof cannot supply answers on all aspects relating to budgeting, forecasting and financial planning. However, it is the belief that the findings of this study do provide valuable insight and understanding regarding budgeting, forecasting and financial planning as a strategic tool in the decision-making process.

6.2.1 Findings: Research objective 1

In Chapter’s 2 and 3, the value-adding budgeting, forecasting and financial planning process was discussed. Here, important factors were identified as crucial to the process in order for it to add value to an organisation.

From the research conducted, the findings can conclude that all companies in the sample prepare an annual budget. Figure 5.5 page 70 indicates that the majority (70%) of respondents complete and approve the budget in two to four months. The finance department is supported by the other functional areas in preparing the annual budget. Once the annual budget is approved, all respondents indicated that a re-forecast of the budget is performed using latest actuals and updated assumptions.

Reducing the length of budgeting cycles, frequent re-forecasting of the annual budget and cross-departmental collaboration ensures that the financial information generated through the budgeting and forecasting process adds value to the decision-making of the organisation.
6.2.2 Findings: Research objective 2

Respondents regard the following items as the main limitations/drawbacks of the traditional budgeting approach:

- length of budgeting and planning cycles
- more time is spent creating than analysing the budget
- lack of involvement from directors and top management
- budgets can be unrealistic when trying to achieve pre-determined targets

The majority of respondents feel that an update or re-forecast of the annual budget is crucial in a rapidly changing business environment and must be supported by planning systems and tools that can accommodate these changes. This re-forecast enables their organisations to react quicker to market conditions and enhances the value of financial planning information. This is evident from the agreement rates of respondents to a list of statements in Table 5.2 page 76 regarding the update or re-forecast of the annual budget with 53% agreeing and 38% strongly agreeing.

6.2.3 Findings: Research objective 3

Respondents strongly agreed with the list of factors regarded as important in maintaining budget and forecast accuracy and quality, and further provided additional factors which they considered relevant. Two such factors, which the researcher considered significant, are as follows:

- budgets and forecasts should take into account changes in manufacturing processes and new technologies
- depending on the size of the organisation, there should be a specialist focus on improving the budgeting and forecasting processes

There is a long term financial planning outlook in place and the majority of respondents (60%) indicated that they made use of a special software
application for their financial planning and analysis (Figure 5.9 page 81), with
the remainder indicating that the use of Microsoft excel was sufficient for their
organisation’s planning and analysis.

6.2.4 Findings: Research objective 4

The finance departments of the organisations participating in the study play a
significant role in whether budgeting, forecasting and financial planning adds
value.

All respondents indicated that the finance department measures budget and
forecast accuracy through variance analysis and this is perceived as a value-
adding element of the process. The finance department engages with other
departments during the budgeting and forecasting process through cross-
departmental meetings to discuss and agree inputs as well as review and
approve planning results.

Lastly, from the literature review, Table 5.6 page 88 presented a list of ways
in which finance departments can enhance their financial planning process to
which the respondents agreed (66%) and strongly agreed (30%).

6.2.5 Findings: Research objective 5

Budgeting, forecasting and financial planning information plays a significant
role in the strategic decision-making of organisations. Decisions regarding
major capital investments, forward cover contracts (exchange rate hedging),
manpower planning, product strategy and liquidity planning. Respondents
indicated that financial planning information provides direction and targets for
performance management and keeps the organisation competitive in a global
market. Lastly, respondents agreed (50%) and strongly agreed (43%) with a
list of statements in Table 5.7 page 90 regarding the use of financial planning
information in organisational decision-making.
Chapter 1, par 1.7 page 12 outlined the delimitation of the study. To make the research project more manageable, it was focused locally on the Eastern Cape’s manufacturing sector. Based on the current research objectives, future research may therefore include:

An empirical survey on a national basis can be performed. This will significantly increase the sample size and the increase in the sample size will highlight and strengthen the significance of the current research objectives. Thereafter a comparison can be made between the local survey and the national survey for possible differences which may exist.

Secondly, research can be undertaken in service industries to assess whether budgeting, forecasting and financial planning is used as a strategic tool in decision-making. This research will enable a comparison to be made between manufacturing and service industries.
REFERENCE LIST


KPMG, 2010. Forecasting for sustainability, Budgeting for better performance, Trends in forecasting – The science behind the crystal ball. Finance function insights, 1(5), 2-7


