BUDGETING AND ITS IMPACT ON FINANCIAL PERFORMANCE: THE CASE OF NON-BANK FINANCIAL INSTITUTIONS IN GHANA

Samuel Pimpong
University of Professional Studies, Accra (UPSA)
Ghana

Henrietta Laryea
Ghana

ABSTRACT

Budgeting plays a significant role in the performance of businesses. In view of the fact that most firms want to improve performance, various systems and structures are put in place to ensure that a firm grows profitably. Budgets thus provide useful information for superiors to evaluate firm performance and inform financial allocation strategies across various components of a firm. This study assessed the impact of budgeting on firms' performance of non-bank financial institutions in Ghana. The study adopted a quantitative research strategy. Primary data was collected by use of questionnaires in order to ascertain the relevance of budgets as a financial management tool among non-bank financial institutions. The study applied the step-wise method to generate the models. Moreover, regression analysis was used to measure the degree and extent of the relationship between budgeting and firm performance. The findings of the study revealed that, budget coordination has a statistically significant moderate positive relationship on firm performance.

Keywords: Budgeting, financial performance, non-bank financial institutions.

INTRODUCTION

The subject of financial performance has received significant attention from scholars in the various areas of business and strategic management. It has also been the primary concern of business practitioners in all types of organizations since financial performance has implications on an organization's health and ultimately its survival (Onduso, 2013). Financial performance refers to the degree to which financial objectives are being or has been accomplished. Extensive literature regarding the firm's objectives, places much emphasis on the maximisation of shareholder's wealth. Managers are thus concerned about maximising shareholder's wealth as it connotes future prospects, reflects steady growth, and provides a risk shield. In order to achieve this, Naser and Mokhtar (2004), argue that high performance reflects management effectiveness and efficiency in making use of company's resources. According to (Lazaridis, 2006) the greatest dilemma in financial management is to achieve desired trade-off between liquidity, solvency and profitability, while seeking to maximise shareholder wealth.

A budget on the other hand is a plan for the accomplishment of programmes related to the following; objectives and goals, a definite time period, an estimate of resources required, an estimate of resources available, compared with one or more past periods and showing future requirements (Smith and Lynch, 2004). The budgeting process therefore puts an organisation's activities in a coherent manner that results in the general welfare of the organisation.

In many developing countries such as Ghana, one of the growing sectors of the economy is the financial services sector. Bawumia and Owusu-Danso (2008) concluded that Financial sector stability is a priority and Ghana's financial soundness indicators have all improved in recent years. The banking sector has experienced rapid growth, as a result of credit expansion, changes in regulation, significant technological advances in the sector and more forceful risk management policies by banks. It is for this reason that the Government of Ghana has shown strong commitment to financial sector development. This is evident with Cabinet's approval of the Financial Sector Strategic Plan (FINSSP) in 2003, which aims at broadening and deepening the financial sector. The second phase of the Financial Sector Strategic Plan II (FINSSP II 2011-2015), approved in 2010 and launched in June 2011, aims at developing the financing base of banking institutions, improving quality services through increased competition and removing barriers to accessing finance and introducing innovative financial instruments. Non-bank financial institutions form part of this financial service industry and play a critical role in ensuring that the overall objective is achieved.

The effect of budgeting on firms' performance has been studied in various countries across the world. However, not much research has been covered in this area on Non-bank financial institutions in Ghana. Whereas Kenis (1979) supported the argument that budgeting is positively and significantly associated with performance, Milani (1975) found that there is a weak positive association between budget and performance. With reference to the ambiguities arising in previous studies as well as the absence of extensive research in this area of study in Ghana, this research seeks to find out the effect of budgeting on financial performance of Non-Bank Financial Institutions in Ghana. As at June 2015, the total number of Non-Bank Financial Institutions (NBFI's) in Ghana was sixty three (63).

LITERATURE REVIEW

Theoretical literature review

Goal setting theory (Locke and Latham 1990,2002) was developed inductively within industrial organization psychology over a 25 year period based on same 400 laboratory and field studies. Goal setting is effective on any task where the person has control over his or her performance. The question was: How do you get goal commitment? Their initial belief was: through participation. Participation in decision making was a popular topic of study following World War II. Locke (1968) predicted that participation would enhance goal commitment. This main effect of participation in decision making on performance was completely mediated by self- efficacy and task strategy. In 1997, Locke, Alavi, and Wagner reviewed all the reviews and controversies regarding participation in decision making. They concluded that participation in decision making is more fruitfully conceived as a method of information exchange or information sharing rather than as a method of gaining goal commitment. Hollenbeck, Williams, and Klein (1989) developed a useful measure of goal commitment, which they have subsequently refined. They and others found that goal commitment was most important when goals are difficult. This suggests that commitment acts in two different ways: as a moderator when there is a range of goal difficulty, and as a main effect when goal level is held constant at a high level.

In discovering goal mechanism, Locke and Latham documented the directive effect of goals by showing that when feedback is given for multiple performance dimensions, performance only improves on those dimensions for which goals are set (Locke and Bryan, 1969). The effort dimension was validated implicitly by showing that people with hard goals work harder, and later others did study involving direct ratings of effort. La Porte and Nath (1976) and Latham and Locke (1975) showed that goals affect persistence. Direction, intensity and persistence, of course, are the three aspects of motivated action. Each of these mechanisms is easily verifiable by introspection. Knowledge is another goal mechanism, Locke and Latham (1990) rest on the premise that goal-directedness is an essential attribute of human action and that conscious self- regulation of action, though volitional is the norm. Locke, et al, 1989 differentiated the effects of goal difficulty from those of goal specificity by showing that specificity alone affected performance variance whereas difficulty affected performance level. They concluded that all goal effects are mediated by task knowledge. Motivation without cognition is useless. Conversely, cognition without motivation is also useless because the individual will have no desire to act on what is known. A budget is a way of setting an organization at goals for a specific period of time. The prime axiom of goals lead to higher performance than when people strive to simply "do their best" (Locke and Latham 1990) the performance benefits of challenging specific goals have been demonstrated in hundreds of laboratory and field studies (Locke and Latham 1990, 2002). Budgets should therefore be set to a standard that is quite challenging for employees to achieve, obtaining a high standard set goal creates a sense of efficiency and this will bring about yearn to achieve more.

Empirical literature review

Wijewardena and De Zoysa (2001) perceive that the impact of budget planning and budgetary control on performance may vary from firm to firm depending on the extent of its use. The greater extent of the formal budgeting process should have a positive impact on the performance of SMEs. In their study, performance is measured by two financial indicators: sales growth and return on investment. Data was collected from two thousand manufacturing SMEs in Australia. The results show a positive and significant relationship between budgeting planning and sales growth, and between budgetary control and sales growth. However, no significant difference was found between budget planning and return on investment (ROI), nor between budgetary control and return on investment. To explain the insignificant relationships between budget planning and ROI, as well as budgetary control and ROI, they explain that, although firms with a greater extent of planning or control report higher rates of growth in sales, "these revenues are not bringing about higher profits because of internal inefficiencies."

In his study on "the participative budgeting process and its impact on employees' performance", Tromp (2009) stated in his conclusion that, budgeting participation is a complex process, affected by many variables and conditions, therefore it is hard to measure the absolute effect of participative budgeting on employee performance.

Qi (2010), also conducted a study on the impact of the budgeting process on performance in SMEs in China and the main empirical question for the study was whether the budgeting process significantly and positively impacts the performance of Chinese SMEs. There was a positive effect of the formal budgeting process on firm performance. First, the study revealed that more formalised budgeting planning leads to higher sales revenue. Secondly, budget goal characteristics strongly affect the budgetary performance of Chinese SMEs, thus clear budget goals lead to higher goal achievement, whereas, difficult (but attainable) budget goals increase the motivation of employees to achieve budget standards. Thirdly, the study discovered that the more formalised budgetary control tends to lead to a higher growth in profit of a firm.

In a study conducted by Sugioko (2010) on "the impact of budget participation on job performance of University Executives: a study of APTIK- member Universities in Indonesia". This research aimed to test empirical evidence regarding the role of mediating variables on the impact of budget participation on job performance. The study concluded that budget participation has a positive and significant impact on job performance, while structural equation tests showed that, trust, organizational commitment, budget adequacy, and job satisfaction variables positively and significantly mediated the relationship between budget participation and the job.

Onduso (2013) in a study on "the effect of budgets on financial performance of manufacturing companies in Nairobi County" concluded that the financial performance as measured by ROA is strongly influenced by using budget and managerial performance respectively. The findings of the study concurs with this study.

Mohammed and Ali (2013) in a study "the relationship between budgeting and performance of Remittance companies in Somalia" concluded that the correlation between budgeting and firm performance is 0.514, which means that one level increase of budgeting effectiveness will lead to 0.514 higher firm performance. The probability of this correlation coefficient occurring by chance is 0.00. This coefficient shows that a statistically significant moderate positive relationship between budgeting and firm performance.

Faith (2013) conducted a study entitled "the effects of budgeting process on financial performance of commercial and manufacturing parastatals in Kenya". The key findings were that; more formal budgeting planning promotes higher growth of sales revenues in the parastatals, formal budgetary control leads to a higher growth of profit in parastatals and greater budgetary participation leads to better managerial performance. The study enhances the researchers understanding regarding budgeting activities.

METHODOLOGY

Research design

The research fits into an experimental research design, as it seeks to find the effects of budgeting on firm performance among non-bank financial institutions in Ghana. A cross-section survey was used for this study since it employed a single point of data collection for each participant. The study engaged different respondents who differ regarding their interest, but share other characteristics such as socioeconomic status, educational background and ethnicity. While the design may sound relatively simple; finding participants who are very similar except in one specific variable can be difficult. Also, groups can be affected by cohort differences that arise from the particular experiences of a unique group of people.

Population and sampling

All companies classified as Non-Bank Financial Institutions as per the Bank of Ghana, financial sector report as at June 2015 were considered for the study. In all, sixty three Non-Bank financial Institutions classified into seven groups were considered.

Target population

The population of interest for this study is defined as all firms classified as Non-Bank Financial Institutions as per the Bank of Ghana, financial sector report as at June 2015. The respondents are in managerial positions such as Finance Managers, Finance Officers, Operations Managers, Marketing Managers and Production Managers.

Sample Frame

Out of the population target, seven Non-Bank Financial Institutions were selected using convenience sampling but strategically to reflect the characteristics of the population.

Instrumentation

Primary data was collected by use of a questionnaire through the self-administered drop and pick. Questionnaires were administered to the top level managers of the selected firms. The use of questionnaires have some advantages; less expensive, convenient and unbiased. A five (5) point Likert scale questionnaire that was administered had three sections composed of: General Information, Budget Process and Firm Performance. The budget process comprises of themes such as budget planning, budget coordination, budget control and budget evaluation.

Measurement of variables

The independent variables used in the study were; budget planning, budget coordination, budget control, and budget evaluation.
The dependent variables on the other hand were: net profit margin (NPM), return on investment (ROI), revenue growth (RG), market share (MS) and liquidity (LQ).

Model specifications

From the study variables, the following equation is formulated and used
(Financial Performance)it= α+ β1(Budget Process)it +eit

Financial Performance = α + β1 (Budget Coordination)………………………….... Model 1
Financial Performance =α + β1 (Budget Coordination) + β2 (Budget Planning)…… Model 2
Where:
Financial Performance = Net Profit Margin, Return on Investment, Market Share, and Liquidity
α = constant term
β = coefficient term
e = error term

Data validity and reliability

A pilot test was done on some four Non-Bank financial institutions in Ghana, to ensure validity of the data. The research instruments were pretested to ensure they served the intended purpose. After the pretest the questionnaire was appropriately amended and revised.The reliability of the data was tested using the Cronbach's alpha, the results of which are shown below:

Instrument reliability test

Table 1.1 - Instrument Reliability Test

Variables	Cronbach Alpha Coefficient
Budget Planning	0.889
Budget Coordination	0.865
Budget Control	0.837
Budget Evaluation	0.844

Source: Field Survey Data, (2016).

Analytical technique

In addition to the regression, descriptive statistics and correlation analysis were employed in the study. The regression model was estimated with the ordinary least squared techniques by pulling the data together. The summary statistics used to explain the data included mean, maximum, minimum and standard deviation. The hypothesis was tested using the t-values and the associated probability. The correlation of the various variables as well as the regression was carried out using Statistical Package for Social Sciences (SPSS) Version 21.

RESULTS

The researchers investigated the profile of the 81 respondents. The results are shown below:

Table 2.1: Gender Distribution of Respondents

	Frequency	Percentage
Male	41	50.6
Female	40	49.4
Total	81	100

Source: Field Survey Data, (2016).

Table 2.2. Age Distribution of Respondents

	Frequency	Percent
20-29 Years	36	44.4
30-39 Years	39	48.1
40-49 Years	6	7.4
Total	81	100

Source: Field Survey Data, (2016).

Table 2.3. Recent Qualification Distribution of Respondents

	Frequency	Percent
Diploma	2	2.5
Degree	58	71.6
Masters	13	16
Professional	5	6.2
Other	3	3.7
Total	81	100

Source: Field Survey Data, (2016).

Table 2.4. Position Held in Organization

	Frequency	Percent
Finance Manager	2	2.5
Accountant	6	7.4
Operations Managers	8	9.9
Marketing Manager	13	16
HR manager	6	7.4
Others	46	56.8
Total	81	100

Source: Field Survey Data, (2016).

Descriptive statistics
Budget process

The respondents were requested to indicate the extent at which they use different budgeting process in their organization in a five point Likert scale. The range was "strongly disagree (1)" to "strongly agree (5)". The scores of strongly disagree have been taken to represent a variable which had mean score of 0 to 2.4 on the continuous Likert scale; (0≤ S.D <2.4). The scores of "neutral" have been taken to represent a variable with a mean score of 2.5 to 3.4 on the continuous Likert scale: (2.5 ≤ M.E. <3.4) and the score of both agree and strongly agree have been taken to represent a variable which had a mean score of 3.5 to 5.0 on a continuous Likert scale; (3.5≤ S.A. <5.0). A standard deviation of >0.8 implies a significant difference on the impact of the variable among respondents.

Budget planning

The budget planning process was found to influence to a greater extent the performance. "There is an overall organizational strategy on budgetary" had a mean of 3.73, "laid down guidelines and time table for budgetary planning" obtained a mean of 3.71. The respondents also indicated that they strongly agreed with past data being used as a starting point for producing the budget while considering the contingencies (mean = 3.62). "Top management communicates the budget plan and helps in reduction of wastage of resources" with a mean of 3.59. The variable obtained an average standard deviation of 0.868 which implies that there is a significant difference among the respondents.

Budget coordination

The respondents strongly agreed with the variable used in determining budget coordination. "The budget originates from at the lowest level of management and it is refined and coordinated at the highest level" had a mean of 2.95 which signifies strongly disagree from the Continuous Likert Scale.

Budget control

Regarding budget control, the respondents strongly agreed that budget control is an important process in improving the financial performance of the firm. It obtained an average mean of 3.66 which is within the strongly agreed category for the Likert continuous scale.

Budget evaluation

The findings on budget evaluation indicated that the most important aspect of the budget processes and its impact on financial performance was budget evaluation with a mean of 3.74. It was found that variances when properly analyzed would go a long way in improving the financial performance of the firms. Variance determination aids in management in the adoption of exceptional strategy. The respondents also indicated that the variance guides the overall budget strategy for the next period.

Financial performance

The respondents were to give independent opinion of how budgeting affects the performance of various financial parameters. The findings revealed that most of the respondents considered budget process to influence the general financial performance of the firm. They pointed out an effective budgetary process will increase net profit (3.99), increase returns to investment by shareholders (3.83), enhance market growth of the firm (3.76), improve the sales growth of the firms (3.63). It was found that financial liquidity is the least of indicators that affects financial performance (3.61). With a standard deviation averaging 0.93 for most of the results, it implies that there was a moderate variability among the respondents as to the extent of the effect of budgeting on the financial performance of the firm.

Fitting the linear regression models (Step-Wise)

The Step-Wise method was employed in putting together the model that is ideal for the analysis given the significance level of 95%.
The model generated is shown below:
Financial Performance = $\alpha + \beta 1$ (Budget Coordination)……………………………... Model 1
Financial Performance =$\alpha + \beta 1$ (Budget Coordination) + $\beta 2$ (Budget Planning)…… Model 2

Test for Assumption of linearity and multicollinearity

Linear regression model is based on the hypothesis that, there is linear relationship between the dependent variable and the independent variable(s). Thus, the existence of significant regression model is principally based on the existence of linear relationship between the dependent variable and each of the independent variable.

Another condition that can be problematic is multicollinearity, which can lead to disingenuous and erroneous results. Multicollinearity or collinearity occurs when there are high inter-correlations among some set of the predictor or independent variables. The existence of collinearity means that, two or more predictors contain much of the same information.

To confirm the existence or otherwise of the multicollinearity, the researchers used Variance Inflation Factor (VIF) and Tolerance to test for collinearity. Tolerance is calculated by 1 minus covariance between one and other independent variables. A Tolerance close to 1 means there is little multicollinearity, whereas a value close to zero (0) suggests that multicollinearity may be a threat. The reciprocal of the tolerance is known as the Variance Inflation Factor (VIF). The VIF shows us how much the variance of the coefficient estimate is being inflated by multicollinearity. Theoretically, it is good if VIF is smaller than 5.

Regression Analysis

Model Summary

Model	R	R Square	Adjusted R Square
1	0.7777	0.6048	0.5367
2	0.8461	0.7159	0.6669

a. Predictors: (Constant), budget coordination

b. Predictors: (Constant), budget coordination, budget planning

c. Dependent Variable: financial performance

The R is termed as multiple correlation coefficients and measures the relationship between the observed and predicted values of the dependent variable. Larger values of R indicate stronger relationships and vice versa. Also, the adjusted R square, also known as the coefficient of multiple determinations, is the percent of the variance in the dependent variable explained uniquely or jointly by the independent variables. From model one which had an adjusted``` R square of 53.67%, R square of 60.48% and R figure of 77.77%. This indicated that 53.67% of the variation in financial performance is explained by budget coordination. The model two realized R figure of 84.61%, R square of 71.59% and an adjusted R square of 66.69%. 66.69% of the variation in the dependent variable is explained by the independent variables of Budget Coordination and Budget Planning.

ANOVA

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	264.718	1	264.718	30.33	.000
	Residual	689.504	79	8.728		
	Total	954.222	80			
2	Regression	315.343	2	157.672	19.25	.000
	Residual	638.879	78	8.191		
	Total	**954.222**	**80**			

a. Predictors: (Constant), budget coordination

b. Predictors: (Constant), budget coordination, budget planning

c. Dependent Variable: financial performance

Coefficients(a)

		Unstandardized Coefficients		Standardized Coefficients			95% Confidence Interval for B	
Model		**B**	**Std. Error**	**Beta**	**t**	**Sig.**	**Lower Bound**	**Upper Bound**
1	(Constant)	9.759	1.271	-	7.681	0.000	7.23	12.288
	Budget Coordination	0.365	0.066	0.527	5.507	0.000	0.233	0.496
2	(Constant)	8.652	1.309	-	6.61	0.000	6.046	11.258
	Budget Coordination	0.255	0.078	0.369	3.283	0.002	0.1	0.41
	Budget Planning	0.243	0.098	0.279	2.486	0.015	0.048	0.437

a. Dependent Variable: Financial Performance

The B constitutes the unstandardized regression coefficients while the "Beta" constitutes the standardized regression coefficients with their corresponding independent variables. The unstandardized coefficients are the coefficients of the estimated regression model when the independent variables are measured in the same unit whereas standardized coefficients are the estimates resulting from a regression analysis that have been standardized so the variances of dependent and independent variables are 1. Where the units of measurement are different the beta or the standardized coefficients are used. For this study, the standardized values were used as that made the regression coefficients more comparable. The t values and their corresponding p-values test the significant of each of the estimated regression coefficients. A significant coefficient means that the attached independent variable largely contributes to the significance of the overall regression model in explaining the variations in the dependent variable.

From the regression result, model 1 show that Budget coordination has a Beta of 0.527 with a significance level of 0.00. Hence it can be concluded that, budget coordination has a statistically significant moderate positive relationship on firm performance. This result is similar to findings by Mohammed and Ali (2013) in their research but contradicts the findings of Tromp (2009) where he opined that, it is hard to measure the absolute effect of budgeting on performance.

From the regression results, model 2 shows that both budget coordination and budget planning has a significant relationship on firm performance with fairly moderate beta of 0.369 and 0.279 respectively. The results confirm the results illustrated in model 1 above.
By inference, it can be concluded that, budgeting has a statistically significant fairly moderate effect on financial performance of non-bank financial institutions in Ghana. This finding hence confirms the alternate hypothesis (H1 = there is a relationship between budgeting and firm performance), hence the null hypothesis (Ho = there is no relationship between budgeting and firm performance) is rejected and is consistent with finding of the Goal Setting Theory (Lock and Latham, 1990 & 2002) as well as empirical studies by Mohamed and Ali (2003), Sugioko (2010) and Onduso (2013).

CONCLUSIONS

The purpose of this study was to assess the effect of budgeting on the firm performance of non- bank financial institutions in Ghana. An empirical investigation was undertaken, using the regression analytical technique with fitting models generated using the Step Wise model generation technique. The analysis of variance was also carried out on the regression model. The finding confirms the alternate hypothesis (H1 = there is a relationship between budgeting and firm performance), hence the null hypothesis (Ho = there is no relationship between budgeting and firm performance) is rejected and is consistent with finding of the Goal Setting Theory (Lock and Latham, 1990 & 2002) as well as empirical studies by Mohamed and Ali (2003), Sugioko (2010) and Onduso (2013).

The second objective was to establish the extent to which budgeting practices are used by non-bank financial institutions in Ghana. The study resulted that, all the respondents of the firms indicated that there is an established budget process. This gives an indication that the companies budgetary process goes through a budget planning, budget control, budget coordination and budget evaluation.

Hence it can be concluded that, budget coordination has a statistically significant moderate positive relationship on firm performance.

REFERENCES

Bank of Ghana- Official Site: https://bog.gov.gh

Bawumia, M., & Owusu-Danso, T. (2000). African Financial reform; Ghana's reform transforms its financial sector. *IMF survey Magazine*, 1-2.

Faith, M. C. (2013). The effects of budgeting process on financial performance of commercial and manufacturing Parastatals in Kenya. *accounting, organisations and society*.

Hollenbeck, Williams, & Klein. (1989). An empirical examination of the antecedents of commktment to difficult goals. *Journal of applied psychology*, 18-23.

Kenis, I. (1979). Effects of budgetary goal characteristics on managerial attitudes and performance. *The accounting Review*, 707-721.

LaPorte, R. E., & Nath, R. (1969). Role of Performance goals in prose learning. *Journal of Educational psychology*.

Lazaridis, L. (2006, June). relationship between working capital management and profitability of listed companies in Athens stock exchange. *Journal of financial management and analysis, 19*, 5-7.

Locke, E. A., & Bryan, J. F. (1969). Goal Setting and Task Performance. *Journal of Applied Psychology*.

Locke, E. A., Alavi, M., & Wagner III, J. A. (1997). Participation in decision making: an informative exchange perspective. *Research in personnel and human resource management*, 15:293-331.

Locke, E. A., & Latham, G. P. (1990). *Goal setting Theory, theory building by induction.* New York: Oxford University Press.

Milani. (1975). The relationship of paticipating budget setting industrial supervisor performance and attitudes: a field study. *The accounting review*, 274-283.

Mohamed, & Ali. (2013). relationship between budgeting and performance of remittance companies in somalia. *educaational research international*, *2*, 7.

Naser , K., Kabhari, Y., & Zulkifli, M. (2004). Impact of ISO 9000 registration on company performance: Evidence from Malaysia. *Managerial Auditing Journal*, *19*(4), 509-516.

Onduso, E. O. (2013). The Effect Of Budgets On Financial Performance Of Manufacturing Companies In Nairobi County. *New Business Journal*, 7,46,74.

Sugioko, S. (2010). the impact of budget participation on job performance of university executives: a study of APTIK-member universities in indonesia. *Kasetsart journal of social science*, 276-277.

Tromp, J. F. (2009). The participative budgeting process and its impact on employee performance. *JStor*, 18,28.

Qi, Y. (2010). the impact of budgeting process on performance in SMEs in China. *Jstor*, 117-122.

Smith, & Lynch. (2004). Is income inequality a determinant of population health. part 1 a systematic review. *Accounting, Organizations and sociiety*.

Wijewardena, H., & De Zoysa, A. (2001). the impact of financial planning and control on performance of SMEs in Australia. *journal of enterprising culture*, 353-365.