

# THE EFFECT OF STRATEGIC PLANNING AND BUDGET PREPARATION TO FINANCIAL PERFORMANCE: A STUDY ON THREE SDA HIGHER EDUCATIONAL INSTITUTIONS IN INDONESIA

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## Abstract

*The concept of financial performance is a series of financial activities in a given period of time that reported in the financial statements it also reflects the company's operational performance. The purpose of this study to determine whether the strategic planning and budget preparation effect on financial performance on the three SDA higher educational institutions in Indonesia. This research uses the questionnaire to collect data than to be processed using person product moment find the relationship and its effect. The results show there is a correlation between the strategic planning to financial performance with the correlation coefficient value of 0.509 and the relationship between budget preparation to financial performance is reflected with correlation coefficient value of 0.560. The  $r$  value (correlation) is 0.578 with the contribution of these two variables on financial performance is equal to 0.335. Also there is a significant relationship between strategic planning and budget preparation to the financial performance with  $F$ -value of 40.736. The regression equation results is,  $Z = 1,683 + 0.132 X + 0.318 Y$ , where the budget preparation is a better predictor if compared with strategic planning.*

**Keywords:** *Strategic Planning, Budget, Budgeting, Financial Performance*

## Introduction

Organizational performance can be characterized as a measure of a firm's efficiency and effectiveness. There are four basic reasons to monitor organizational performance: (a) maintain control, (b) assist in strategy formulation, (c) employ accountability, and d) report performance (Samuelsson *et al*, 2006).

Davis and Pett (2002) mainly identified two perspectives for measuring organizational performance: 1) efficiency versus effectiveness, and 2) financial performance and non financial performance. The first perspective on organizational performance is that organizational effectiveness and organizational efficiency should be included to measure organizational performance. Efficiency generally refers to profits as the ratio of inputs to outputs, whereas effectiveness represents a firm's capability to acquire scarce resources. In other words, efficiency is associated with profitability and effectiveness concerns growth.

Another perspective on measuring organizational performance is financial performance versus non-financial performance. Business performance consisted of financial performance and business performance, including both financial performance and non financial performance. In this conceptualization of organizational performance, it indicated financial performance as a narrow concept relative to business performance. Financial performance highlights the use of outcomes-based financial indicator. Typical indicators for financial performance are sales growth, profitability (ratio such as return on investment (ROI), return on sale (ROS), return on equity (ROE) and so on). Non-financial performance includes market share, new product introduction, product quality, marketing effectiveness, manufacturing value-added and other indicator of technology efficiency.

A plan is probably the way in which most people use the word strategy. This tends to imply something that is intentionally put in training and progress monitored from the start to a predetermined finish. Some business strategies follow this model. 'Planning' tends to produce internal documents that detail what the company will do for a period time in the future (i.e., 5years). It might include a schedule for new product launches, acquisition, financing (i.e., raising money), human resources change, etc. (Campbell *et al*, 2002).

According to Bryson as cited in Idalene (2008), strategic planning activities involve gathering of key decisions makers for their decision of what is important for the organization in order to make decision and take actions that improve organizational performance. He went to say that structured strategic thinking process entails eight steps course of action: (a) development of an initial agreement, (b) identification and clarification of mandates, (c) development and clarification of mission and values, (d) external environmental assessment, (e) internal environment assessment, (f) strategic issue identification, (g) strategic development, and (h) description of organization in the future.

Anthony and Govindarajan (2004) described that a strategic plan shows the financial and other implications, over the next several years of implementing the company strategies. They also mentioned that the strategic planning process involves the following steps: reviewing and updating the strategic plan from last year, deciding

on assumptions and guidelines, first iteration of the new strategic plan, analysis, second iteration of the new strategic plan, review and approval.

In another side, Anthony and Young (2003) stated that a budget is a plan expressed in quantitative, usually in monetary terms. It covers a specified period, usually a year. In the budget preparation phase of the management control process, each program's objectives are translated into terms that correspond to the spheres of responsibility of the manager charged with implementing them. Thus, during the budget preparation phase, plans made in program terms are converted into responsibility terms.

The process of arriving at the budget is essentially one of the negotiations between responsibility center managers and their superiors. The end product of these negotiations is a statement of the output expected during the budget year and the resources (inputs) to be used to achieve these outputs. As such, the agreed upon budget is a bilateral commitment. Responsibility center managers commit to producing the planned output with agreed amount of resources, and their superiors commit to agreeing that such performance is satisfactory. Both commitments are subject to the qualification unless circumstances change significantly.

According to Golombiewski and Robin (2000), budgeting has been undertaken consistently to plan and monitor expenditures and to ensure compliance in the strict auditing sense, but budgeting reforms in recent years have emphasized broader issues of macroeconomic management and the efficiency and effectiveness of resources used to achieve program objectives.

Based on the above description, this study aims to determine whether the strategic planning and budget preparation effect on financial performance in the SDA Higher Educational Institutions in Indonesia.

## **Review of Related Literature and Hypothesis**

### **Strategic Planning**

According to Shermerhon as cited in Stone (2008), strategy defines in which an organization intends to move and establishes the framework for action through which it intends to get there. It involves a consistent approach over time and reflects the organization's approach to achieving its objectives. The purpose of strategy is to maintain a position of advantage by capitalizing on an organization's strengths and

minimizing its weakness. To do this, an organization must identify and analyze the threats and opportunities present in the external and internal environment.

Certo (2003) mentioned that strategic planning is a long-range planning that focuses on the organization as a whole. In the strategic planning phase, senior management determines the major programs the organization will undertake during the coming period and the approximate expenses that each will incur. These decisions are made within the context of the goals and strategies that emerged from the strategy formulation activity. If a new program represents a change in strategy, the decision to initiate it effectively is part of the strategy formulation activity, rather than the management control process. The strategy formulation and management control merge in the strategy planning.

Mintzberget *al*(2005) indicated that traditional prescriptive process view is focused on “formulation, implementation, and control”. Formal planning processes underlying the approach to strategy include document strategy plan which covers time periods of three years or more, identifies goals and objectives and resources needed to achieve them.

A study conducted by Behzadfar (2011) among 214 respondents in Mazandaran found that using specified strategic plan increases employees’ participation which leads to increasing their productivity towards performance. Another study conducted by Arasa and K’Obonyo (2012) on organization, from both the private and public sector focusing on the relationship between strategic planning and organizational performance indicated the existence of a strong relationship between strategic planning and firms organization.

Similarly, an empirical research conducted in Jourdanian hotels in two cities (Aqaba and Petra) in which questionnaires were distributed to hotel managers found that strategic planning processes achieved a good fit (or alignment) between the environment and internal capability of organization. This is followed by formal strategic planning as an effective way to achieve improved financial performance (Aldehayyat *et al*, 2011).

## **Budget Preparation**

A budgeting process or system is necessary for any enterprise where needs and wants in terms of resources to carry out activities are unlimited. The inevitable conflict of decision making occurs because in most cases resources are limited. Further, colleges and universities face other constraints and uncertainties, for example, declining traditional college age student population and reduced earning for endowment and other funds, which will influence the future availability of resources. The budgeting process helps management examine carefully organizational operations, resolve competing demands and document how resources will be used. Subsequently, the budget serves as a fundamental control device that highlights for management where positive or negative variances have occurred (Rachlin, 2009).

Hogget *et al* (2006) said that the main objective of the financial planning phase of budgeting is to identify how management intends to acquire and use the entity's resources to achieve organizational goals during a budget period. A master budget consisting of several interrelated budgets provides the basis for financial planning. The master budget is a set of interrelated budgets representing a comprehensive plan of action for a specific time period. It is typically prepared for a one-year period that coincides with an entity's reporting period. The budget for the year is subdivided into shorter periods such as months or quarters to allow timely comparisons of actual results and budgeted figure. Alternatively, the budget may be developed for a continuous period of 12 months or more by adding a month or quarter in the future as the month or quarter just ended is eliminated.

Shim and Siegel (2009) listed six steps in the budgeting process. These are setting objectives, analyzing available resources, negotiating to estimate budget component, coordinating and reviewing component, obtaining final approval and distributing the approval budget. The success of the budgeting process requires the corporation of all levels within the organization.

The essence of budgeting and control system is captured by this quotation from the Chartered Institute of Public Finance and Accountancy (CIPFA) as mentioned by McGee *et al* (2010), all organizations need to manage performance so that their financial and strategic objectives are achieved and management and financial stakeholders can be confident in the associated control processes. The proper construction and control of

budgets is central to this, to safeguard the organization's viability and effective delivery of its objectives.

A budget is related to a one year slice of the strategic plan. An operating budget shows the details of revenues and expenses for the budget year. The process starts with the dissemination of guidelines approved by senior management and based on these guidelines, each responsibility center manager prepares a proposed budget and review with superior, and agreed position is negotiated. When these individual pieces reach the top of business unit, or of the whole organization, they review for consistency and adherence to overall corporate goals (Anthony and Govindarajan, 2004).

A study done by Qomoyi (2008) entitled "The Budget Preparation Process: a compliance review of the City of Tshwane Metropolitan Municipality" found that in budget preparation they need to request proposal from the department, receive departmental estimates for accuracy, then the department provides budget manual in order to assist them in capturing their income, expenditure, and activity planning. This is done to be able to extract reports, and do budget hearing to discuss their requested budget and required funding.

A study conducted by Shastri and Stout (2008) indicated that the majority of respondents believe that the budget is "useful" as it relates to the list of business objectives. Traditionally, the budget was considered to be important for planning and control purpose only. The mere fact is that the budget preparation indicated is also useful for other functions such as strategic planning, communication, team work, and incentive rewards determinations.

Silva and Jayamaha (2012) conducted a study which found that budgetary process has significant associations with the organizational performance of apparel industry in Sri Lanka. This confirms that efficient apparel companies maintain sound budgetary process which contributes to higher levels of organizational performance. John and Ngoason (2008) mentioned in their study that practices of integrating strategic management and budgeting which increase organizational performance.

### **Financial Performance**

Financial reporting may ultimately lead to the creation of financial statements that let managers, investors, and other stakeholders evaluate financial strength or

weakness. Naturally, a degree of uniformity is approached and presentation must exist in order for the statement to be useful. If no standard existed, then every company would simply do as it pleases, making it impossible to compare performance across companies or, indeed, within a company, if it decided to change its standards every year (Banks, 2007).

Titman *et al* (2011) stated that the basic objective of financial statement analysis is to assess the financial condition of the firm being analyzed. In a sense, the analyst performs a financial analysis so he or she can see the firm's financial performance the same way an outside investor would see it.

Power and Needles (2011) described financial performance measurement, as using all the techniques available to show how important items in a company's financial statement relate to the company's financial objectives. All the plans that management formulates to achieve a company's goal must eventually be stated in terms of financial objectives and related performance objectives.

According to Hilton *et al* (2008), areas of performance affecting financial performance are net interest margin, revenue growth, customer profitability, and overall return on asset.

The goal of a business is to make money by providing goods or services to customers. Businesses try to maximize their profits by generating high revenues, low costs, and thus high profit. However, business competitors are also trying to do the same and thus a business can only maximize its profit by gaining an advantage over its competitors (Warren *et al*, 2007). Profitability is ability to earn or the capacity to make a profit. It is the primary goal of all business ventures. Without profit the business will not survive in the long run. Measuring current and past profitability and projecting future profitability is very important (Hoffstrand, 2006).

Kimme *et al* (2007) indicated that there are three ratio to measure financial performance.

1. Liquidity ratios. Liquidity ratios measure the short-term ability of the enterprise to pay its maturing obligations and meet unexpected needs for cash. The measures used to determine the enterprise's short-term debt-paying ability are as follow: the current ratio, the current cash debt coverage ratio,

the receivables turnover ratio, the average collection period, the inventory turnover ratio, and average days in inventory.

2. Solvency ratios. Solvency ratios measure the ability of the enterprise survives over a long period of time. The measures used to determine are the following: debt to total asset ratio, times interest earned ratio, cash debt coverage ratio, and free cash flow.
3. Profitability ratios. Profitability ratio measure the income or operating of an enterprise for a given period of time. A company's income, or the lack of it, affects its ability to obtain debt and equity financing, its liquidity position, and its ability to grow. The measures used to determine are: return on common stockholders' equity ratio, return on assets ration, profit margin ratio, asset turnover ratio, and gross profit rate.

Measures of financial performance indicate whether the company's strategy, implementation, and execution are indeed contributing to bottom-line improvement. Typical financial goals include profitability, growth, and shareholder's value. Periodic financial statements remind manager that improved quality, response time, productivity, and innovative products benefit the firm only when they result in improved sales, increased market share, reduced operating expenses, or higher asset turnover (Deset *al*, 2007).

Revenue is simply the money that a company receives from its customers as compensation for its products or service. Ideally, you want to see a steady or accelerating rate of growth in company's revenue. If a company's revenue grows more slowly, it needs to inquire why. Is it because of poor service or product performance, better competitor offering, ineffective marketing, or all of the above?

Revenue growth refers to expanding product or service offerings, reaching new customers and markets, changing the products and services mix toward higher-value-added offering, and repricing products and services. The cost reduction and productivity objective refers to effort to lower the direct costs of products and services, reduce indirect costs, and share common resources with other business units (Norton and Kaplan, 2001).

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They added that in measuring the financial performance of an organization means to reveal its relative strengths and weaknesses of an organization as compared to other organizations in the same industry and being aware of the industry trend to show whether the firm's position has been improving or deteriorating over time.

According to Momanyi and Munene (2013). There were significant negative perceptions among the youth regarding budget and budgeting process. This is a clear signal that budgeting and planning has not taken root in the youth owned enterprises. Thus, more sensitization is needed in these youth owned enterprises so as to reap the benefits of the budget and the budgetary process. Many youth owned enterprises fail to survive due to lack of a business plan. Another factor that may cause failure of youth group owned enterprises is lack of information and knowledge to enable them effectively plan, manage and make sound decisions to enhance the growth and survival of their enterprises. Besides the training of the youth and business planning skills.

Based on the above literature we hypothesized that:

1. Strategic planning effect financial performance on higher educational institution in Indonesia.
2. Budget preparation effect financial performance on higher educational institution in Indonesia.

### **Method of Study**

The researcher used the descriptive research method, an approach considered appropriate to answer the research questions. The design of this research is descriptive-correlational and effect. This research involved SDA Higher Educational Institutions in Indonesia, with the population of this research were the regular employees of higher education institutions in Indonesia. The higher educational institutions are as follows: Indonesia Adventist University, Klabat University, and Surya Nusantara Adventist College.

**Table 1**  
**Respondents' Population and Questionnaires Distribution, Retrieved and Valid**

<b>Institution</b>	<b>Population</b>	<b>Distributed Questionnaires</b>	<b>Retrieved Questionnaires</b>	<b>Valid to be Processed</b>
Adventist University of Indonesia	120	112	81	79
Klabat University	131	80	57	56
Surya Nusantara Adventist Colleges	46	43	31	30
Total	297	235	169	165

The researcher used a self-constructed questionnaire for the data gathering. The questionnaire was constructed based on related literature and studies. The instrument used a five-scale of measurement in which respondents indicated their answer. The questionnaire is divided into four parts. Part I consists of the respondents' demographic profile: age, educational attainment, position, length of service. Part II deals with the respondents' perception on the Management control system involving strategic planning, budget preparation, operation and measurement, and reporting and evaluating dimensions. Part III deals with the respondents' perception on the level of human resource management practices involving recruitment, selection, training and development, performance management, compensation, and relationship dimensions and Part IV deals with respondents' perception on the level organizational performance relating to learning and growth, business and production process, and financial.

Correlation analysis using Pearson's Product Moment was used to determine the significant relationship between variables. Regression analysis was used to determine the effect of strategic planning and budget preparation toward financial performance.

Data analyze, interpret and determine the implications of date gathered, the statistical techniques Employed using the Statistical Package for Social Science (SPSS).

### **Result of the Study**

The collection of data through questionnaires distributed to permanent workers, both teaching and non-teaching staff for the staff to answer further processed for identification of problems that have been set.

**Table 2**  
**Reliability of Instruments**

Variables	Items	Reliability Coefficient
Strategic Planning	17	.9302
Budget Preparation	14	.8706
Financial Performance	15	.8900

**Table 3**  
**Descriptive Statistics**

	Mean	Std. Deviation	N
Strategic Pln	4.01	.690	165
Budget Prep	3.74	.749	165
Finc. Perform	3.60	.589	165

Table 2 above shows the results of reliability test for each indicator, which produces overall value above 0.8. While the results of descriptive statistics (in Table 3) showed that from the 165 respondents who gave answers to the questionnaire with the results of between 3.5 to 4.49, which is in the range of "good", with a standard deviation between 0.5 to 0.75. This means that the average overall perception of the respondents stated that the strategic planning, budget preparation and financial performance for high educational institution is already good.

**Table 4**  
**Correlations**

		Finc. Perform	Strategic Pln	Budget Prep
Pearson Correlation	Finc. Perform	1.000	.509	.560
	Strategic Pln	.509	1.000	.731
	Budget Prep	.560	.731	1.000
Sig. (1-tailed)	Finc. Perform	.	.000	.000
	Strategic Pln	.000	.	.000
	Budget Prep	.000	.000	.
N	Finc. Perform	165	165	165
	Strategic Pln	165	165	165
	Budget Prep	165	165	165

**Table 5**  
**Model Summary<sup>b</sup>**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.578 <sup>a</sup>	.335	.326	.483

a. Predictors: (Constant), Budget Prep, Strategic Pln

b. Dependent Variable: Finc. Perform

The results showed that the correlation between the variables are having a significant relationship between strategic planning to financial performance with large correlation coefficient of 0.509 and the relationship between financial performance with budget preparation as a correlation coefficient of 0.560. The value of r (correlation) is 0.578 with the contribution of these two variables on financial performance is equal to 0.335, or by 33.5% while the rest (66.5%) determined by other variables outside of this study (can be seen in Table 4 and table 5 above).

**Table 6**  
**ANOVA<sup>b</sup>**

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	19.033	2	9.517	40.736	.000 <sup>a</sup>
	Residual	37.846	162	.234		
	Total	56.880	164			

a. Predictors: (Constant), Budget Prep, Strategic Pln

b. Dependent Variable: Finc. Perform

The significance of the ANOVA can be found in the table above which shows there is a significant relationship between strategic planning and budget preparation to the financial performance with F-value of 40.736.

**Table 7**  
**Coefficients<sup>a</sup>**

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	1.683	.226		7.429	.000
	Strategic Pln	.132	.058	.214	2.276	.024
	Budget Prep	.318	.074	.404	4.299	.000

a. Dependent Variable: Finc. Perform

From table 7 above gives the regression equation with the following results:  $Z=1.683+0.132X+0.318Y$ , which means that when the strategic planning is ignored the magnitude of the financial performance of 1,683 units to 0,318 units plus time changes in involvement in budget preparation. The same thing also applies where at the time of involvement in budget preparation are ignored, then the magnitude of the financial performance of 1,683 units were coupled with 0.132 units of time changes in strategic planning. Which states that the best predictor of financial performance is budget preparation which means that the employees understanding to the budgeting will contribute to great financial performance on the three high educational institutions in Indonesia.

From the above findings, it can be said that engagement and understanding of the workers about budget is very important in order to achieve optimal financial performance, strategic planning for the subsequent determination that also supports the achievement of the organization's financial performance.

### **Conclusion and Recommendation**

The results show there is a correlation between the strategic planning to financial performance with the correlation coefficient value of 0.509 and the relationship between budget preparation to financial performance is reflected with correlation coefficient value of 0.560. The  $r$  value (correlation) is 0.578 with the contribution of these two variables on financial performance is equal to 0.335. Also there is a significant relationship between strategic planning and budget preparation to the financial performance with  $f$  value of 40 736. The regression equation results is,  $Z = 1,683 + 0.132 X + 0.318 Y$ , where the budget preparation is a better predictor if compared with strategic planning.

Were commend for researchers who are interested in researching the SDA high educational institutions in Indonesia to complete this study by adding a variety of other related variables in order to produce a more generalized findings of the factors affecting financial performance, and even that performance measurement is performed on further studies not only from the financials ideal one, but of then on-financial side, which later results will be the best in put for the development of educational institutions, especially in Indonesia.

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