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# Exploring Optimizing Performance Appraisal Systems Based on Budget Management

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## ABSTRACT

In corporate management, the degree of synergy between budget management and performance appraisal directly impacts the efficiency of organizational resource allocation and the effectiveness of strategic implementation. According to the "Enterprise Budget Performance Management Development Report" released by the Chinese Academy of Fiscal Sciences, 60%-75% of enterprises experience a misalignment between budget targets and performance indicators. The resulting sunk costs average 10%-15% of an enterprise's annual budget, resulting in wasted resources and weakening the support provided by management tools for the business. Based on the balanced scorecard theory and dynamic budget management theory, this article explores optimization paths for a performance appraisal system based on budget management from five perspectives: current situation diagnosis, theoretical integration, technical support, mechanism innovation, and cultural support. The study found that enterprises currently face common problems such as unrealistic goal setting, unbalanced indicator design, and ineffective execution and monitoring. Deep integration of budget and performance can be achieved through strategies such as establishing a dynamic target adjustment mechanism, improving a multidimensional indicator system, strengthening ERP system technology capabilities, implementing quantitative management and control throughout the entire process, and promoting organizational cultural transformation. Practice has shown that the optimized system can improve resource allocation efficiency by about 20%, enhance corporate strategic execution, and provide reference management upgrade solutions for organizations of different sizes and industries. The relevant conclusions can be verified through industry statistics and theoretical practice.

## KEYWORDS

Budget management; Performance appraisal; System optimization; Dynamic budgeting; Balanced scorecard; ERP system

## 1. INTRODUCTION

With the increasing complexity of the market economy and the expansion of business operations, budget management and performance appraisal have become core management tools for corporate operations. Their synergy is directly related to the survival and development of an organization. Under traditional management models, budgeting and performance appraisal often present a "two-faced" phenomenon: budget preparation often relies on linear deductions from historical data, ignoring market dynamics and internal resource changes; performance appraisals focus on short-term financial indicators, disconnected from the logic of budget resource allocation. This leads to a disconnect between "budget management allocation and performance management evaluation."

According to the "China Enterprise Management Modernization Report," as a result of this, organizational inertia leads to resource waste accounting for 20%-30% of annual corporate budgets. Some companies even engage in short-sighted behavior, such as sacrificing long-term strategy to meet performance targets, due to the disconnect between budgeting and performance. On a theoretical level, the balanced scorecard (BSC) theory, proposed by Kaplan and Norton in 1992, breaks the limitations of single financial indicators by constructing a performance evaluation system across four dimensions: finance, customers, internal operations, and learning and growth, providing a framework for integrating budgeting and performance. Dynamic budget management theory, through rolling forecasts and continuous updates, addresses the shortcomings of traditional fixed budgets in coping with market uncertainty. Currently, digital transformation has accelerated management model innovation, but most companies have yet to overcome the management bottleneck of the "divergence between budgeting and performance." How to organically integrate the resource allocation function of budgeting with the strategic guidance of performance has become a key issue in upgrading corporate management. Based on authoritative industry report data and established management theories, this article systematically explores optimization paths for performance appraisal systems from five dimensions: current situation diagnosis, theoretical integration, technological support, mechanism innovation, and cultural support, providing practical and implementable references for companies.

## 2. CURRENT SITUATION DIAGNOSIS: MULTIDIMENSIONAL MANIFESTATIONS OF THE DISCONNECT BETWEEN BUDGETING AND PERFORMANCE

The disconnect between budgeting and performance permeates the entire management process, resulting in systemic efficiency losses and is a common phenomenon in industry statistics. The problem of being out of touch with reality is prominent in target setting: When compiling budgets, most companies tend to extrapolate growth based on previous years' data, failing to fully consider external factors such as rising raw material prices and intensified market competition, nor do they objectively assess their own production and R&D capabilities. This closed-door target setting often leads to a disconnect between budgets and actual performance. Some companies' sales growth targets exceed market capacity by more than 20%, making it difficult for employees to achieve even with their full commitment. This not only renders assessments ineffective as motivators, but also wastes budgetary resources. Imbalanced indicator design is a core issue. A survey by the Chinese Academy of Fiscal Sciences shows that 45% of companies focus solely on financial indicators, focusing on cost reduction and sales growth while ignoring non-financial dimensions such as product quality and customer retention. This imbalance can easily lead to short-sightedness: some companies cut R&D costs to maintain costs, resulting in a decline in product competitiveness; others relax customer reviews to boost sales, increasing the risk of bad debt. Another 30% of companies resort to a "comprehensive" stacking of indicators, with some positions having over 30 indicators, with no logical connections and weightings determined based on experience. This prevents employees from focusing on key areas, making assessments difficult to reflect true performance. Implementation loopholes further amplify these shortcomings. Irregular data collection is common [1]. Due to the lack of a unified standard, different departments use different recording standards. For example, sales uses "contract value" while finance uses "received value." This results in inconsistent performance data and lacks objective evidence. Sixty percent of companies fail to communicate promptly when adjusting budgets or performance metrics, leading employees to question fairness. Twenty-five percent of companies fail to factor performance metrics into salary increases or promotions, leading employees to believe that performance is useless and gradually lose their motivation to participate. These issues create a cycle of "disconnected goals, ineffective metrics, and inefficient execution." Statistics show that this wastes an average of 10%-15% of the annual budget.

## 3. THEORETICAL FOUNDATION: THE LOGIC OF INTEGRATING THE BALANCED SCORECARD AND DYNAMIC BUDGETING

The balanced scorecard theory is the core framework for integrating budgeting and performance, a point that has been extensively validated in both academic research and business practice. Kaplan and Norton proposed the theory in a 1992 Harvard Business Review paper, arguing that traditional financial indicators only reflect a company's past performance and fail to gauge future potential. They therefore developed an evaluation system encompassing four dimensions: finance, customers, internal operations, and learning and growth. This theory breaks the limitation of solely focusing on financial data, allowing performance evaluation to be closely aligned with corporate strategy. The financial dimension focuses on the economic benefits of resource investment; the customer dimension measures market competitiveness; the internal operations dimension optimizes process efficiency; and the learning and growth dimension ensures long-term development capabilities. These four dimensions support each other, providing a clear basis for the optimal allocation of budget resources. Dynamic budget management theory addresses the rigidity of budgets caused by market uncertainty and addresses the shortcomings of traditional annual fixed budgets [2]. Traditional budgets are prepared annually and are difficult to change, making them unable to adapt to unexpected events such as shifting market demand and policy adjustments. Dynamic budgets, on the other hand, rely on rolling forecasts and continuous updates to maintain flexibility. Typically, dynamic budgets are updated monthly on a quarterly basis for the next 12-18 months, ensuring the budget keeps pace with business development. Its core characteristics are forward-looking and integrated with business and finance. Foresight is reflected in not simply relying on historical data, but rather in multi-dimensional analysis and forecasting based on market trends, policy guidance, and industry competition. Integration requires finance and business departments to jointly develop and adjust budgets: the business department analyzes market dynamics and demand, while the finance department calculates resources and assesses risks, thus avoiding the disconnected nature of finance's "closed-door" budgeting. Combining these two theories creates a closed loop of "strategy-budget-performance." The balanced scorecard clarifies what should be measured, using four-dimensional indicators to set performance targets and provide direction for budget compilation. For example, if the customer dimension states "increase satisfaction by 5%," the budget should be allocated to customer training and quality improvement. Dynamic budgeting addresses the question of "how to allocate resources," adjusting the budget in real time based on changes in performance targets. For example, if a surge in market demand leads to an increase in sales targets, dynamic budgeting can be used to increase production and marketing investments. This integration ensures that the strategy remains on track while also enabling flexible response to change: the balanced scorecard ensures that budget allocations are aligned with the strategy, while dynamic budgeting ensures that resource allocations adapt to performance targets. In practice, many local governments and enterprises are using this approach. For example, some local finance bureaus use the balanced scorecard to set performance targets for fiscal funds and combine it with dynamic budgeting to adjust allocations, demonstrating the effectiveness of this approach [3].

## 4. TECHNOLOGY EMPOWERMENT: THE APPLICATION OF ERP SYSTEMS IN BUDGET-PERFORMANCE INTEGRATION

As digital management tools, ERP systems enable real-time linkage between budget and performance, and their value has been widely recognized in industry practice. It integrates data from multiple departments, including finance, production, sales, and human resources, breaking down information silos and digitizing the entire budget preparation, execution monitoring, and performance evaluation process. This addresses the challenges of traditional manual management, characterized by slow data collection, complex statistics, and difficult traceability. Its core benefits lie in three key areas: Real-time monitoring ensures that budget execution is synchronized with performance targets. Traditional

budgeting relies on manual statistics, resulting in delayed data feedback, making it difficult to detect overspending in a timely manner. ERP systems, however, integrate all expenditures and investments into digital management, linking each item to a budget item in real time. The finance department can check balances and progress at any time, and automatically issue alerts before overspending occurs. For example, in expense management, the system sets limits based on accounting items. When expenditures approach 80%, an alert is triggered, and reimbursement cannot be made for items not included in the budget, thus technically adhering to budgetary regulations. Data integration provides an objective basis for performance evaluation. Performance evaluation requires accurate and unified data. Traditional management systems, with data scattered across systems like CRM and MES, generate inconsistent data and make verification difficult. ERP systems consolidate data into a unified platform and establish statistical rules to ensure data consistency [4]. The system also allows for tracing back to the source, allowing each performance data point to be identified with the specific link and individual responsible. For example, if "production efficiency falls short of target," it can quickly identify whether it's a raw material, equipment, or operational issue, eliminating impression-based assessments. Flexible adjustments support dynamic budgeting and performance alignment. The system allows for set adjustment rules. When external environmental changes necessitate adjustments to performance targets, the business department submits a request. After financial review and management approval, the system automatically updates the budget and adjusts the indicators accordingly. For example, if raw material price increases necessitate a relaxation of cost targets, the system can increase the procurement budget and adjust the "unit product cost" standard. This "rigid control + flexible adjustment" architecture ensures budget integrity while allowing for assessment flexibility, ensuring consistent alignment between the two. According to industry reports, enterprises using ERP have seen an average 30% increase in budget accuracy, a 50% reduction in performance evaluation time, and an approximately 20% increase in capital efficiency.

## 5. MECHANISM INNOVATION: ESTABLISHING DYNAMIC TARGETS AND FULL-PROCESS QUANTITATIVE CONTROL

Establishing a dynamic target adjustment mechanism is the first step in system optimization. The core is to establish a cyclical process of "market forecasting-resource assessment-target calibration" to ensure that budgets and performance targets are realistic. Adjustments must adhere to two principles: First, on a quarterly basis, the rationality of targets should be evaluated in combination with monthly business data and market changes. For example, if demand exceeds expectations, sales targets and corresponding budgets should be appropriately increased; if raw material price increases cause overspending, cost targets should be recalculated and budgets adjusted. Second, a 5%-10% flexible budget should be retained to deal with emergencies such as temporary orders and equipment repairs, thereby avoiding a disconnect between budget and performance. Goal setting also requires "top-to-bottom consultation": management discusses the strategic direction, and business departments discuss feasibility based on their own capabilities and the market. Multiple rounds of communication should be conducted to reach consensus. Don't let management make the final decision on unrealistic targets. Quantitative control throughout the entire process is key to ensuring budget execution and performance targets are met, and it should be promoted from three aspects. To quantify performance indicators, break down performance goals into specific, measurable items, avoiding vague phrases. For example, "improve customer service quality" should be broken down into "reduce customer complaint rates by 5%" or "decrease response time to within 2 hours." The corresponding budgets should also be quantified, such as "add 100,000 yuan to the customer service training budget" or "invest 50,000 yuan in system upgrades." Data management requires a standardized collection and review process: clarify departmental responsibilities, establish review milestones, and synchronize data in real time using tools like ERP and a data center. Ensure that data lags hinder performance evaluations. Results should be applied by integrating performance appraisals with budget adjustments and incentives, creating a virtuous cycle of "performance improvement and budget optimization." If

a department meets performance targets, it should receive an increase in budget. If it doesn't, the budget should be adjusted based on the cause. For example, if poor production efficiency is due to aging equipment, the budget should be allocated to upgrades. Regarding incentives, performance appraisal results should be directly linked to salary, promotion, and training: high-performing employees receive a 10%-15% salary increase and priority in management training, while poor performers receive supplementary training and improvement before being considered for promotion [5]. This mechanism ensures that employees understand that budget execution and performance are closely linked to their own interests and encourages them to actively participate in management. According to the "China Enterprise Human Resources Management Report", companies that have linked performance and incentives have an average increase of 30% in employee budget execution enthusiasm.

## 6. OPTIMIZATION AND GUARANTEE: ORGANIZATIONAL CULTURE TRANSFORMATION AND CROSS-DEPARTMENTAL COLLABORATION

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# 7. CONCLUSION

Optimizing a performance appraisal system based on budget management requires a coordinated approach encompassing current situation diagnosis, theoretical integration, technical support, mechanism innovation, and cultural support. This is a systematic approach. Current problems faced by companies include unrealistic goals, unbalanced indicators, and a lack of monitoring of execution. The root cause lies in the disconnect between budget and performance management. The integration of the balanced scorecard and dynamic budgeting theory provides a theoretical framework for addressing these issues. ERP system technical support enables real-time linkage between budget and performance management. Mechanism innovations such as dynamic target adjustment and full-process quantitative control ensure the implementation of optimization. Organizational culture transformation underpins long-term progress. These mutually reinforcing approaches form a comprehensive system of "theory-technology-mechanism-culture," effectively improving resource allocation efficiency, reducing sunk costs to less than 10% of the annual budget, and enhancing strategic execution. The practical value of this research lies in providing practical solutions for different organizations: manufacturing companies can focus on production budgeting and performance monitoring within ERP systems; service industries should strengthen the integration of customer-centric indicators with dynamic budgeting; and small and medium-sized enterprises can initially simplify their indicator systems and prioritize the development of dynamic target adjustment and results application mechanisms. Of course, there are limitations: given the significant differences between industries, the suitability of strategies like ERP systems for small and micro enterprises with limited resources remains to be explored. In the future, optimization paths can be refined, tailored to specific industries, and solutions can be tailored to specific needs. With the advancement of digitalization, AI-driven intelligent budgeting and real-time performance evaluation will become a new trend. Companies can use AI to improve the accuracy of budget forecasts and address performance issues promptly through real-time data monitoring. In short, the coordinated optimization of budgeting and performance is key for companies to respond to market changes and achieve sustainable development. Only by closely aligning budget resource allocation with performance goals can we avoid "resource waste" and "strategic inertia" and ensure that management tools truly serve organizational development. Going forward, organizations must continuously identify the intersection of theory and practice, continuously refine optimization paths, and advance budget performance systems towards greater efficiency, flexibility, and strategic alignment.

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