



ENHANCING THE EFFECTIVENESS OF ROLLING FORECASTS

Abstract

An effective rolling forecast is important to estimate long term financial plans. Every organization undertakes this process as a finance activity. However, when the forecasted data is examined on its effectiveness for decision making, more often than not the results are disappointing and the rolling forecast process needs to be redefined.

This paper discusses effective rolling forecasts that utilize resources, technology, processes, and business intelligence to deliver actionable insights. A best-in-class matured RF process will enable CFOs to deliver great results though increased revenue and cost reductions, and create new benchmarks for the organization.

Introduction

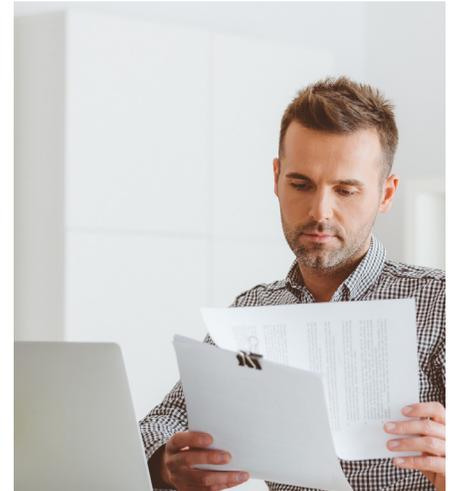
“If you have to forecast, forecast often” – Edgar Fiedler

To mitigate economic uncertainty, every organization must study its financial trends and their association with key external factors such as global presence, political changes, joint ventures, and forex transactions.

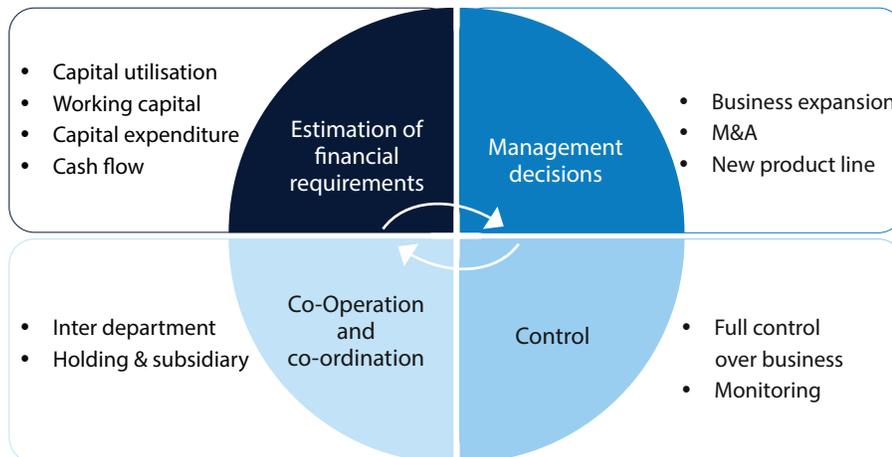
In the rolling forecast method, a forecast is prepared on a continuous basis, but is reviewed for a specific period, generally

for 12 months. For example, a “3+9” RF, uses 3 months’ actual data and 9 months’ forecasted data.

Any rolling forecast planning process requires revisions to accommodate the latest strategy decisions from a top-down approach. The rolling forecast is prepared regularly throughout the year to reflect changes in the industry or economy. A few industries undertake this as a monthly process while others follow a quarterly process.



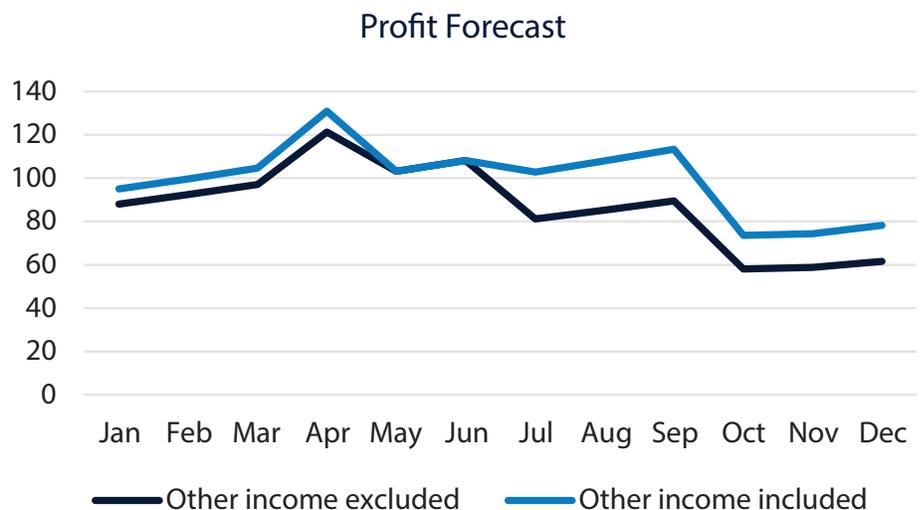
A rolling forecast helps with estimating long term financial requirements such as capital investments for new machinery and plants. It is also important for business expansion. For example, when an organization has a projected strong cash net inflow, then the management can consider potential mergers & acquisitions, joint ventures, or commencing a new product line. The consolidation of RFs of department and subsidiaries provides a broad perspective to management and allows for overall control and monitoring of the company’s financial performance.



Why rolling forecasts are often ineffective

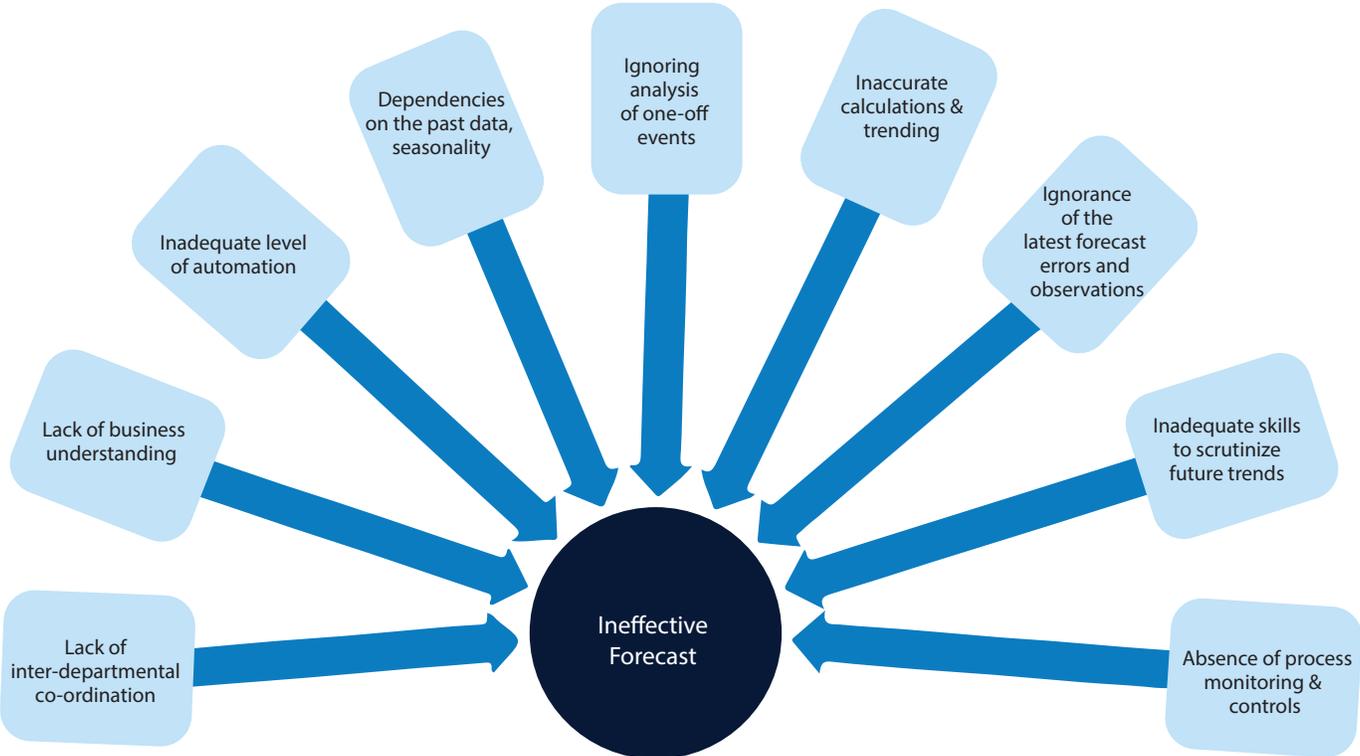
In today’s age of machine learning, many processes are getting automated. However, the process of forecasting involves personal judgement requiring human interventions to achieve an accurate outcome. The forecast is dependent on many assumptions, and returns incorrect outcomes if these assumptions turn out to be wrong. The figure shows how the forecast numbers vary if we include or exclude other income. Other income may include interest, dividends, royalty, rent, capital gains, and so on. Several other forecasting errors such as incorrect trending, inaccurate data sets, and

non-elimination of one-off items lead to ineffective forecasting.



The environment around us is changing rapidly due to new regulations, new government policies and changes in demand and supply factors. A rolling forecast provides for adding new assumptions in each forecast cycle. Not considering all these factors while preparing the rolling forecast, will lead to incorrect and varying projections of revenue/cost, making it increasingly difficult for CFOs to fix on long term strategic plans.

The list below present several internal process specific difficulties that result in ineffective forecasts:

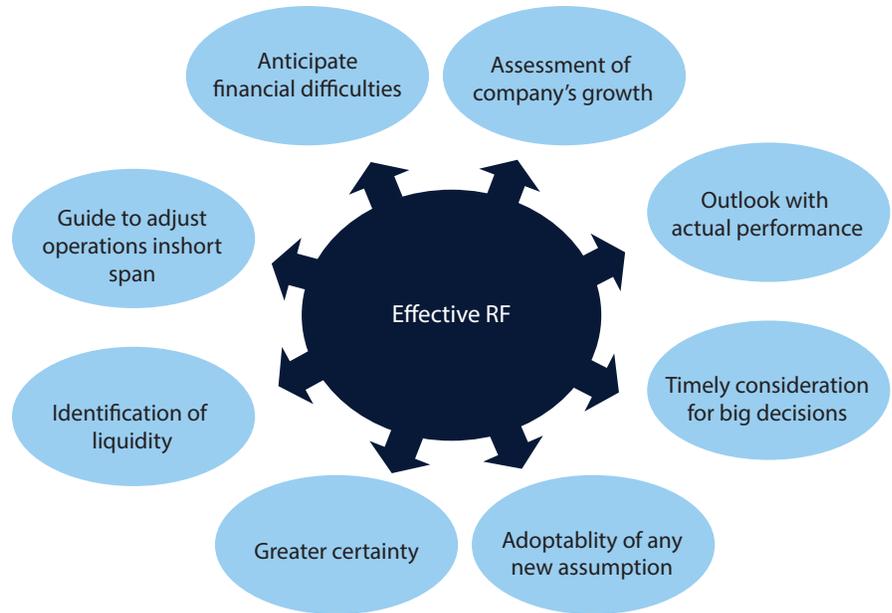




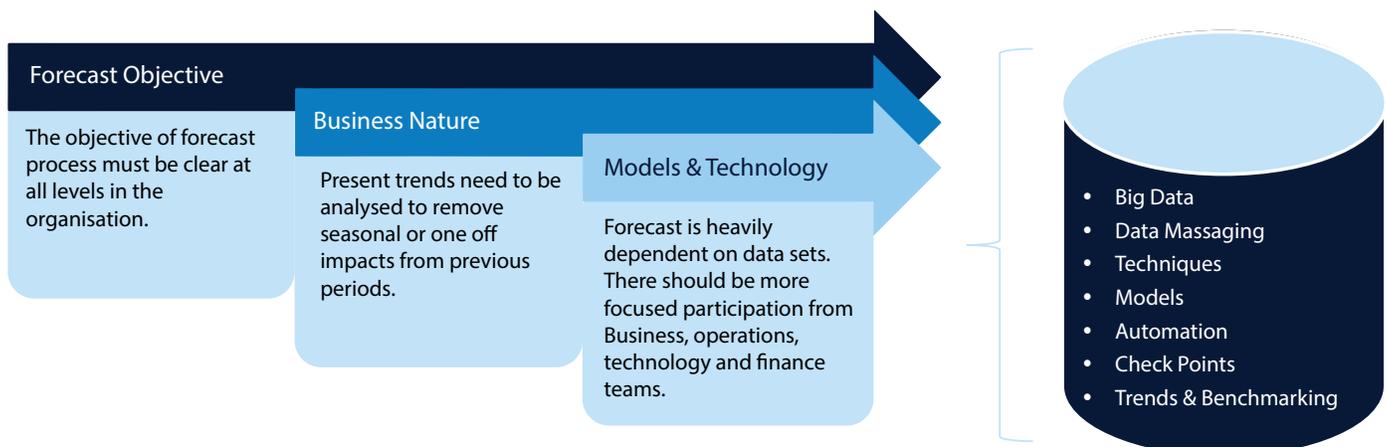
Towards more effective rolling forecasts

If a rolling forecast is done right, the benefits are numerous as illustrated in the figure. An effective rolling forecast provides scope for cost reductions, greater certainty, identification of cash flows, economic challenges, measurement of growth, and better controls.

These benefits accrue when the rolling forecast is based on activity based planning, uses the latest data and compares it to past performance, thus providing a more accurate view to adjust operations in a short span of time.



A planned approach as defined in the figure below is necessary to realize the rolling forecast benefits. Firstly, the top management objective of the rolling forecast must be clear across all levels of the organization. Secondly, the finance team must be aware of the core business and the strategies surrounding it. This will help them understand the business seasonality and one-off transactions. Thirdly, the forecasting analysts work on huge data sets and source a lot of information from different departments. These big data sets must be verified by the various department heads before it reaches the finance teams. The organization also needs to back up the forecast process with good technology support to accommodate big data, automation and effective forecast models.



In addition to the above, the steps below can be used as a best practices checklist for an effective rolling forecast.

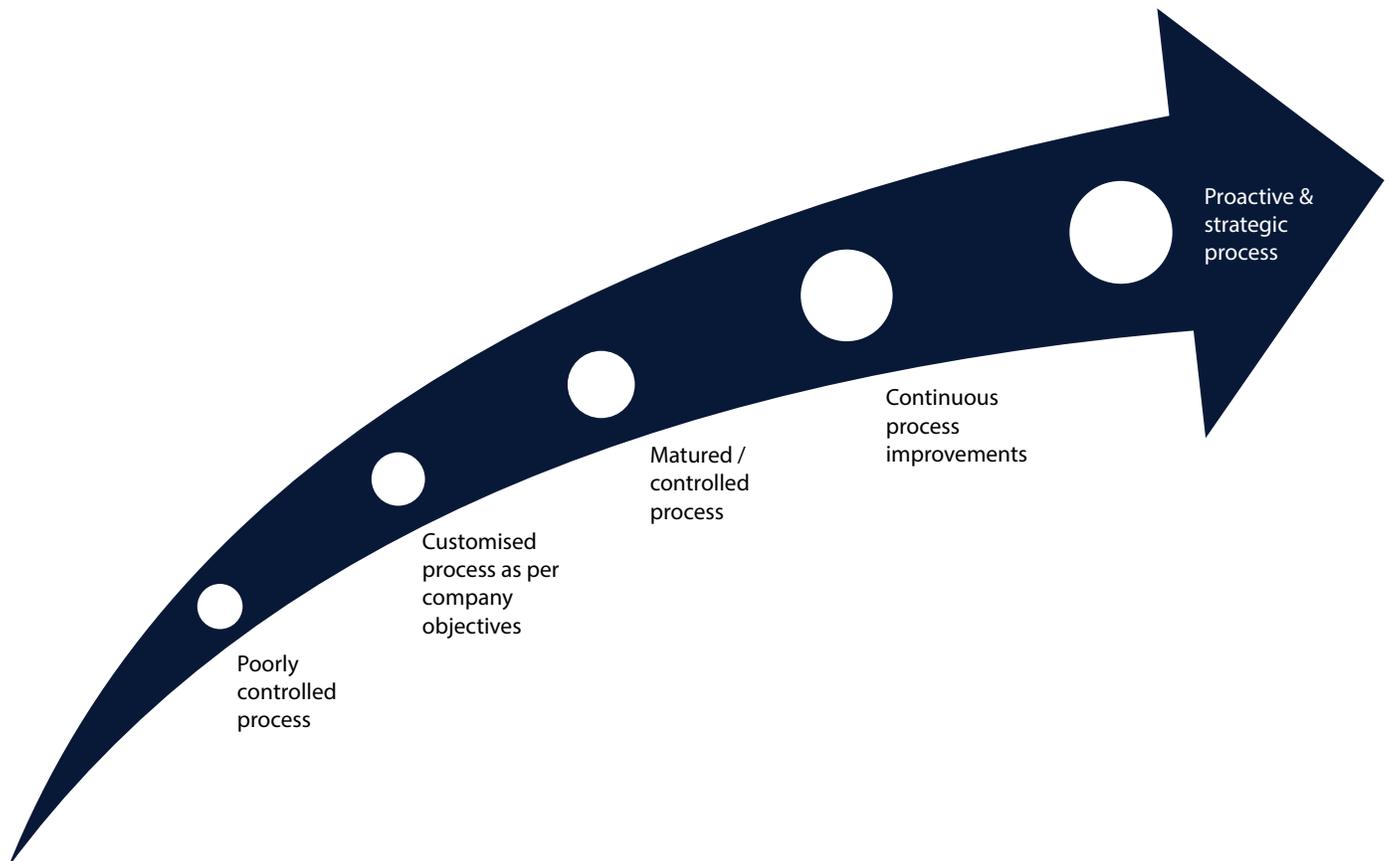
1. Communicate deadlines and expectations by sending the forecast calendar and templates to all departments with data input

2. Gather the data from different departments, input these into the forecast models, and perform the necessary calculations.
3. Schedule forecast reviews with department heads and top

management and upload the finalized version into the ERP.

4. Perform variance analysis and commentary writing for material variances on actual vs forecasted values.

Stages of rolling forecast maturity



As the organizations evolve their forecasting processes, the maturity of their rolling forecasts is defined by the existing technology, people, processes, and whether the results help in decision making. There are five broad stages that organizations need to traverse on their path to rolling forecast maturity:

1. **Poorly controlled process:** The organization starts with a rolling forecast using existing basic tools such as ERP for extraction and processing of data through Excel based forecast models.

2. **Customized processes:** Moving on, the organisation should consider automating a few processes, utilizing ERP or separate platforms to minimise manual efforts.
3. **Controlled process:** In the next stage, organisations need to implement inbuilt controls in the data gathering process and cross-check the results against the organisation vision and top management strategies.
4. **Continuous process improvements:** Further on, the organization makes use of predictive analysis and provides

options to the management for optimum utilisation of resources such as headcount, cash flows, margins. This will take the forecasting process into the proactive and strategic phase of maturity.

5. **Proactive & strategic decision maturity:** In this stage, predictive tools and Artificial Intelligence (AI) are used to comment on business strategy decisions, helping top management and CFO to decide on expansions through M&A, joint ventures, or investing excess resources towards new plants or products.

The best-in-class approach

The four key factors that determine effective rolling forecast are process, technology, resources, and focus on decision support. As organizations move along the forecasting maturity curve, their rolling forecasts can be categorized as start-

up, developing, or best-in-class as outlined in the table. Achieving the best-in-class approach is not a quick fix, but over the years and with continuous improvements organisations can move towards forecasting maturity through implementing best practices and automating manual efforts. In addition, they should monitor

and assess variances between actual performance and expected performance of the forecast at regular intervals. Variance analysis is a risk preventive measure and management should seek prescriptive guidance from the tool to understand what occurred, why it occurred, and what should be done about it.

Key Factors	Start-up Org	Developing Org	Best in class Approach
Process	<ul style="list-style-type: none"> • Non standardized processes • Incomplete data • No deadlines 	<ul style="list-style-type: none"> • Standardized processes • Data availability • Standard deadlines 	<ul style="list-style-type: none"> • Standardized automated processes • Complete data • Alarms / warning emails
Technology	<ul style="list-style-type: none"> • Basic IT tools • Manual templates 	<ul style="list-style-type: none"> • ERP enabled • Macro based Excel templates 	<ul style="list-style-type: none"> • AI to integrate Big Data • Automated tools • Dashboards
Resources	<ul style="list-style-type: none"> • Limited analytical skillsets • Limited domain expertise 	<ul style="list-style-type: none"> • Strong analytical skillsets • Strong domain expertise 	<ul style="list-style-type: none"> • Rule based analysis through robots and data massaging • Domain knowledge - online help and self-learning portals • More heads for revenue generation
Decision Support	<ul style="list-style-type: none"> • Focus on reporting numbers of variances 	<ul style="list-style-type: none"> • Good commentary writing on variances 	<ul style="list-style-type: none"> • Prescriptive analysis and commentary to show what is the impact and options available



Conclusion

An effective rolling forecast will assist CFOs with correct decision making through actionable insights. Organizations already using rolling forecasts must seek to move along the forecasting maturity curve to enable even better decision making and achieve the resultant benefits. Once more and more organizations improve the effectiveness of their rolling forecasts and realize benefits, the yearly budget cycle will rapidly become a relic of the past.



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