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Financial and Operational Forecasting—Crossing the Departmental Divide

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Operational, technical and cultural barriers have often prevented companies from developing forecasts that reflect both financial and operational views of the business.

Q What can controllers and others in the office of finance do to encourage a forecasting process that spans finance and operations?

There has always been an uneasy relationship between financial and operational forecasting. Historically, operational, technical and cultural barriers have prevented a more cohesive approach. This has adversely affected the accuracy and timely delivery of forecasts, ultimately limiting business insight and the ease and confidence with which management can make decisions. So what can the finance function do to encourage more effective forecasting that spans finance and operations?

The first step is to recognise that forecasting is a collaborative process and needs to transcend functional boundaries if it is to be insightful and accurate. But what does that mean in practice? In general terms, there are two rules of thumb worth following. The first is to involve as many people as possible from different functional areas (and backgrounds) to enhance the richness of the business information gathered.

The second aim should be to expand data collection to the fringes of the organization to allow information to be collected as close as possible to the 'sharp end' of the business. Once again, the aim is to develop an accurate picture of what is happening in the business by drawing on the collective knowledge of personnel who have the best visibility to current and foreseeable business conditions.

In the past, the ability to reach out across the business was limited by technology, especially spreadsheets, which confined the development of a forecast to a limited number of loosely connected budget holders. But with the advent of modern collaborative technologies such as workflow and integrated Microsoft® Office applications (such as email and Word) embedded in performance management systems, many of the barriers to working effectively across functional boundaries have evaporated. This has set the scene for the unification of financial and operational forecasting.



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It means that functional models such as human resources (HR) and production plans can be linked to financial plans in the same environment so that there is immediate visibility to the financial effect of any operational decisions. This not only helps to align functional areas with strategic objectives but also helps to ensure the integrity of forecasting assumptions between different areas of the business.

Take, for example, the simple relationship between ‘revenue’ in the financial plan, ‘sales by product’ in the sales plan and ‘sales force headcount’ in the HR plan. Total sales by product should, of course, accord with revenue in the financial plan. But the HR plan should confirm that there are sufficient sales personnel either employed or to be recruited who can deliver the projected sales activity. In the absence of this three-way planning the resulting financial forecast and any subsequent revisions are likely to be inaccurate. Similar considerations apply to the matching of sales forecasts (demand) to production forecasts (supply).

In fact, there are numerous examples of the need to link operational to financial forecasts. But it would be a mistake to ignore the cultural benefits of these linkages, for much of the value of integrating these plans comes from the collaborative planning that it encourages across departmental divides.

Modern technology allows not only the passing of data between functional areas but also the active participation of people in the shared development of the forecasts. This produces a heightened awareness of the pressures and constraints that affect people in different areas of the business and encourages budget holders to work together to optimize the business as a whole rather than one particular area at a time. In other words, integrating financial and operational forecasting leads not only to more accurate forecasts but also to better business insight and a more fulfilling work experience.

About Gary Simon

Gary Simon is the Group Publisher of FSN Publishing Limited, Managing Editor of FSN Newswire and the author of many product reviews and white papers on financial software. Simon is a graduate of London University, a Chartered Accountant and a Fellow of the British Computer Society, with more than 23 years of experience implementing management and financial reporting systems. Simon was a partner with Deloitte for more than 16 years and has led some of the most complex information management assignments for global enterprises in the private and public sector. Gary Simon may be contacted at gary.simon@fsn.co.uk.



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