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Next-generation forecasting:
How rolling forecasts can rescue your company's performance

Information Management

Cognos® software

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Abstract

Faster, more accurate forecasting is essential in today's turbulent business environment, where uncertainty, insecurity, declining markets and dwindling consumer demand have created significant challenges and require new ways of doing business. Rolling forecasting—supported by collaborative enterprise planning and analysis solutions such as those offered by IBM—can provide the kind of on-demand information and instant recalculations you need to adjust to the new reality that this economy has created.

Overview

The pessimist complains about the wind; the optimist expects it to change; the realist adjusts the sails. – William Arthur Ward.

Traditional businesses operate on an annual budget and forecast. This course of action may have been adequate in past business climates, but is no longer effective today. The global economic slowdown— with its reduced credit availability, falling demand, earnings pressure and overall volatility—has created a turbulent environment characterized by compromised cash flow, wildly fluctuating inventory levels and declining sales, revenues and profits.

This instability—regardless of industry—is felt most sharply in the office of the CFO and the finance department. Those in finance know that they need to cut costs, drive cash flow, improve profitability and manage risk in an environment that is quite different than it used to be. They must be agile and be able to change direction or adjust a plan quickly. A good planning system that provides easy analysis, modeling and collaboration can help them do that while taking into account the broader implications on the company—such as the business model and corporate strategy.

Moving from the behavior of annual financial activities into a more dynamic environment, companies are increasingly adopting the rolling forecast. In many cases, rolling forecasts are updated quarterly or monthly, facilitating reduced cycle time with more rapid reaction, realignment and readiness throughout the organization. Companies relying on rolling forecasts, such as those whose successes and recommendations appear in this paper, are those that adjust the sails, factoring in all the information on hand, including strength and direction of wind; the size, shape and weight of the boat; the distance to port and required speed to get there.

Business problems

The fundamentals of forecasting are the same: using empirical and financial data to anticipate and plan for the future performance of the business. The problem with an annual forecast, or even a quarterly forecast, is that it cannot anticipate change factors in a volatile business environment—factors such as inflation and deflation, stagnant or declining markets, wild fluctuations in exchange rates and the like. Essentially, they just don't provide enough time to adjust course when an unexpected storm hits.

Most companies use spreadsheets for financial analysis, management and reporting. But the difficulties are manifold: problems of version control, operational tactics that aren't linked with financial goals, lack of security, the inability to collaborate and the confusion created by hundreds of linked spreadsheets. Furthermore, as organizations drive accountability down to line-of business managers, they are requiring non-finance personnel, who may not be as comfortable with spreadsheets as finance people, to participate in the budgeting and forecasting process. All of these factors drive organizations to move from standalone spreadsheets to performance management solutions.

Rolling forecast: Elements and tools

A rolling forecast not only anticipates the swells and troughs of business, but also does so rapidly and continuously, with a rolling horizon, allowing for the corrections needed in performance gaps and positioning the company for long-term strategic planning.

Most performance management solutions today offer spreadsheet or spreadsheet-like front ends for financial activities. As transparency and accountability drive greater participation in planning activities, leading performance management vendors offer customers an assortment of interfaces for planning and budgeting. The most sophisticated enable users to select the interface they prefer: spreadsheet, Web-based, dashboards or scorecards, ensuring that they are easy to understand and use.

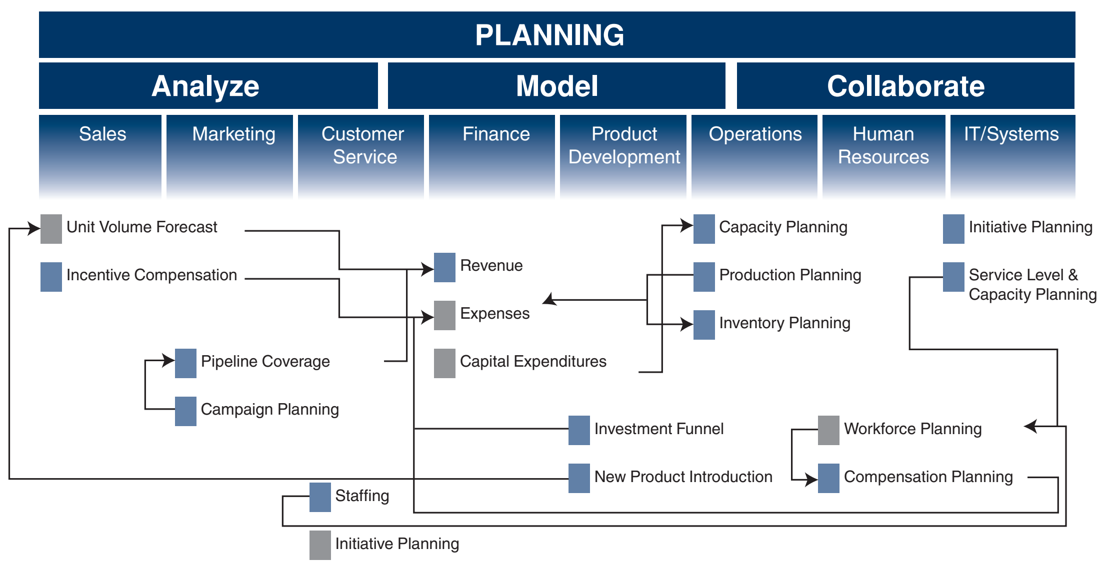
Analyzing, modeling and collaborating for strong forecasts

Although rolling forecasts fundamentally are about anticipation and reaction, they are also about control: Accurate action and reaction requires accuracy in the underlying data. The best way to ensure that accuracy is to rely on a performance management solution that enables analysis, modeling and collaboration as a basis for forecasting.

Organizations can validate assumptions, meet the dynamic needs of their companies and provide a fact-based approach to the planning process with a strong analysis capability. A modeling approach helps facilitate the rapid adoption of best practices that include rolling forecasts and driver-based planning while ensuring that the company's unique processes are being met and that all planners have a consistent set of data and metadata. One key to forecasting is to understand cost allocations. Performance management solutions, reflecting a company's business model, enable that company to create rules to automate the allocations, no matter how complex.[1]

And using collaborative capabilities, companies can develop timeframe-appropriate plans, can ensure high participation for a wider and deeper view of performance and can work against high data volumes, using a rich workflow and an interface that is familiar and easy to understand.

With a solid performance management solution, a company has dynamic control over the forecasting process because the whole company is linked; there are no missing parts or chinks in the plans. The top-down and bottom-up forecasts provide greater accuracy and they can be updated rapidly as situations change. Greater visibility is gained, along with greater control.



Accuracy, reliability and auditability in rolling forecasts

Performance management solutions bring a great deal of accuracy, reliability and auditability to any activity – but especially to rolling forecasting. Companies gain visibility into expenses and profitability by division, product line and even employee and can realign resources rapidly to meet financial targets.

Performance management solutions can easily import data from a number of core systems—general ledger, enterprise resource planning (ERP), spreadsheets and corporate databases—presenting all the data in one place, regardless of the size of the data or frequency with which the data changes. With this capability, users indicate how data should be mapped to their planning solution and then schedule the information import—either in real time or "right time" (such as daily or twice a day) so that they always have the latest intelligence at the push of a button.

The powerful information provided by a performance management solution can be used to generate cash flow statements and a balance sheet without any time-consuming reloading of data. Updated information is imported automatically, nearly eliminating the need to re-key data or move data from spreadsheet to spreadsheet. This significantly reduces the risk of error.

Additionally, some performance management solutions offer even greater assurances by delivering cell-level security, which ensures that only authorized people can view, manipulate or change specific information. They also provide an automatic audit log of who changed what and when. These features enable executives and managers to "rest well at night," assured that the information is accurate, secure and holds up to an audit trail.

Quite simply, what is nearly impossible to do in linked spreadsheets is simple to do with performance management solutions.

Let's look at a real-world scenario.

Case study: International hotel chain

An international hospitality company with more than 100 upscale full-service hotels and resorts struggled with financial data collection and analysis. Created through mergers and acquisitions, the international firm had "inherited" three centralized accounting operations and a number of stand-alone property operations. As a result, data was collected from many different sources and manually input into various and redundant reports.

As the company consolidated its financial data and operations on a single performance management platform, it realized the opportunities provided by a performance management solution. The company also concluded that a performance management solution is the perfect foundation for a rolling forecast.

The hospitality industry is notoriously volatile and it has become even more so in the face of the current economic downturn. An annual forecast or even a quarterly forecast simply cannot adjust for an economy that seems to change almost daily, for heavy or light hurricane seasons or for sudden interruptions in business, such as the recent casino closings in New Jersey.

Adding to forecasting complexity is the fact that most resorts are not just hotel rooms; they include restaurants and retail shops. After forecasting occupancy, the company must then look at the other areas of the property and project multiple related costs, including:

- Number of cleaning personnel needed
- Revenue per restaurant
- Staffing per restaurant
- Kinds and quantities of food per restaurant

Similarly, the demographics of a particular property, season or even guest group will impact many of those variables.

By changing its business processes, supported by performance management technology, the hotelier can now adjust its forecast to reflect the current environment. Because a majority of content is already captured in templates, the template might already exist or a new one can be developed quickly. Those templates coupled with a single, common set of data on which to base business decisions enable the company to make informed and value-driven business decisions. A streamlined and customized portal enables users to spend more time serving guests and operating hotels and less time grappling with access to multiple applications. Just as trimming the sails of a boat helps determine its speed and the time needed to reach port, this hospitality company now has the tools to make adjustments to continue to reach its business goals.

Business drivers

Dos and don'ts for rolling forecasting

Rolling forecasts need not be as oppressive and unpleasant as the annual budgeting and forecasting cycle. In fact, if implemented well, a rolling forecast, with a performance management platform that automates and streamlines the process, can be the proverbial well-oiled machine.

After you have integrated your disparate information systems in a single performance management solution to serve up all the necessary driver-based data, you are ready to move forward with rolling forecasts.

Here are some "dos" and "don'ts," provided by a specialty pharmaceutical company that uses innovative strategies for its internal and financial management. These tips come directly from the CFO and Senior Director for Planning and Decision Support:

- **Do** involve the senior management team early.
- **Do** start with the basics: revenue and P&Ls and major markets or divisions.
- **Do** incorporate driver-based forecasts. They are easier to input and facilitate top-down KPI and goal setting.
- **Do** increase participation. Rolling forecasts facilitate the process and enable greater participation.
- **Do** link accountability to those in control.

- **Do** train system users. Training puts you in front of them and enhances buy-in. Training also serves as a forum to discuss user requirements and agree upon common definitions.
- **Do** make sure there are IT systems in place that can support your implementation and processes. Where possible, you want to pre-populate the forecast to reduce both the time for manual entry and the possibility of errors creeping into the forecast.
- **Do** continually improve your processes to ensure that user and company needs are being met.
- **Don't** underestimate the significance of the change. Many of your team members, colleagues and executives have decades of experience with the annual process. This pattern is ingrained in how people work—often because it is a part of your business processes. Studies have shown that when corporate processes are changed, one-third of the people will willingly embrace those changes, one-third will resist those changes and one-third will leave the organization. To avoid this, you need to understand this is a significant change in mind-set. Instead, focus on the value of the activity—reduced effort for the budgeting process.
- **Don't** ask for excessive detail, especially at the initial roll-out. You don't need actuals—you need information for forecasting.

Forecasting in turbulent times

Companies that do well in turbulent times apply best-practice processes to their planning, budgeting and forecasting initiatives. They use performance management solutions to access actual data quickly and use it to understand what is coming.

According to a 2008 report from The Hackett Group, to survive tough economic times, it is imperative that companies have reliable forecasting mechanisms that anticipate future demand and sales. In the report, Hackett stated that their research indicates "effective enterprise planning is highly correlated to overall financial performance. The ability to anticipate demand not only facili¬tates the forecasting of sales-generated operating cash, it also allows for appropriate adjustment of underlying cost structures to businesses' activity levels."[2].

A report based on a study by APQC and the Beyond Budgeting Roundtable and sponsored by IBM supports the Hackett Group position. The APQC and the Beyond Budgeting Roundtable found that accompanies that use performance management solutions are 24% more likely than spreadsheet users to achieve forecast accuracy within 5% (in other words, 46% of commercial/internal application users forecast to within 5% accuracy, whereas only 37% of spreadsheet users do so).[3]

The solution

The companies noted previously use enterprise planning and analysis solutions powered by IBM Cognos 8 that support rolling forecasting for financial and operational planning and analysis and reporting. These solutions provide on-demand analysis of linked financial and operational plans, facilitate rapid business modeling and enable frequent and enterprise-wide participation for visibility, insight and control over performance.

Conclusion

A faster and easier forecasting process supported by an enterprise planning and analysis solution enables more strategic decision making. You can react more rapidly and realign resources to address not only today's ever-changing market conditions but also the framework for long-term transformation. As one finance executive commented, "Using performance management improves the bottom line for the company and is good for overall business, so why wouldn't you embrace rolling forecasting powered by performance management solutions?"

About IBM Cognos BI and Performance Management

IBM Cognos business intelligence (BI) and performance management solutions deliver world-leading enterprise planning, consolidation and BI software, support and services to help companies plan, understand and manage financial and operational performance. IBM Cognos solutions bring together technology, analytical applications, best practices, and a broad network of partners to give customers an open, adaptive and complete performance solution. Over 23,000 customers in more than 135 countries around the world choose IBM Cognos solutions.

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Endnotes

1 Rules allow real-time calculations to be performed on request efficiently and quickly

2 Wayne Mincey, Michel Janssen and Karlo Bustos, "Urgent and Precise Action Will Determine Winners and Losers in Today's Economic Turmoil." The Hackett Group, 2008.

3 "Charting the Course in Stormy Seas: Planning and Forecasting in Turbulent Times," a 2009 report based on research conducted by APQC and the Beyond Budgeting Round Table and sponsored by IBM.

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