Strategic Financial Planning and Management

About the Analyst

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Robert was an equity research analyst at several firms including First Albany Corporation, Morgan Stanley, and Drexel Burnham, and a consultant with McKinsey and Company prior to joining Ventana Research. Rob was an Institutional Investor All-American Team member and on the Wall Street Journal All-Star list.

What are the most important trends in financial planning?

RK Three trends in particular are worth noting. One is “finance transformation” – the idea that finance departments need to shift the balance of the work they do from repetitive mechanical tasks to more valuable analysis. In that way, they increase their strategic value to the rest of the company. The second is the shift toward greater integration of financial and operating planning. Companies do a lot of planning, much of it in silos. Typically, the most integrated plan is the company budget, but its focus usually is financial. Bringing together sales plans, head-count plans and other operating plans in a single planning environment makes financial planning timelier and therefore more accurate. It also simplifies the planning process because individual plan data can be quickly consolidated. The third trend is adoption of a rolling-quarters approach to planning and forecasting. This method continually pushes the planning horizon outward to suit the needs of the business for planning visibility rather than truncating it at the end of the fiscal period.

What are the biggest challenges that companies face in financial planning?

RK One is simply to manage the process well. Only about half of the people in companies we recently benchmarked said that their planning processes are managed well. A contributing factor to this is that, according to midlevel managers, executives don't communicate their strategy and objectives well. About one-fourth of executives said they communicate these very well, compared to just 7 percent of managers. Executives may think they communicate effectively because the goals are clear to the senior leadership team, but that finding suggests they shouldn't be complacent and should risk communicating too much rather than too little. On the technology side, limited data access and uneven data quality are challenges that make it difficult for managers to understand trends and the direction of the business. Only one-third of companies said they have all or even most of the numbers they need to assess the impact of trade-offs they are considering in their plans. And not enough companies have the right tools and training to make optimal use of analytics to improve the accuracy of their planning processes.

What new technology trends are most likely to impact financial planning?

RK Companies increasingly recognize they need a central, easy-to use environment for all forms of company planning, not just financial planning. Dedicated planning applications provide that environment. One technology trend that supports this environment is cloud computing, which makes it easier for people to participate and remain connected to planning processes regardless of where they are. In-memory processing isn't really new, but software vendors are making increasing use of it to enable more interactive and immediate planning. Vendors also recognize the need to provide companies with easier-to-use advanced analytics such as predictive analytics built into their planning applications. For example, companies can use predictive analytics to help identify customers who are likely to defect or machinery that's about to break so that problems can be prevented or negative impacts limited. We also expect to see more built-in optimization so that companies can quickly figure out the best way to balance trade-offs in their plans. Examples might be trading short-term profitability for longer-term market share gains or assessing how best to allocate their marketing spend. Mobile devices are entrenched in day-to-day business now, but we see the start of what we expect to be an ongoing increase in their use because they make it easier to foster participation and collaboration. They also enhance the accessibility of data to support business conversations.

You have been advocating integrating all forms of business planning for more than a decade. What are the most valuable benefits of this approach?

RK The research we've done suggests that an integrated process works better for everyone. It cuts the workloads of the participants in the planning process. It makes it simpler for FP&A organizations to manage the process, perform analyses and create reports. And it can shorten planning and forecasting cycles. Rather than having planning data scattered around a company – often in desktop spreadsheets – integrating all of a company's business planning activities in a single planning software environment makes all planning data easier to access. Integrating all of the planning data and analyses provides forward-looking business visibility, especially for senior management. This type of environment also makes it easier to construct models that focus executives' attention on key business drivers and their financial consequences. Easier access to data in the other plans enables everyone to be able to examine both the "things" about the business – such as units sold, labor hours and purchased parts – and their associated revenue and costs. Integrated planning improves forecast reliability and provides a clearer picture of performance and forecast accuracy. And having easier access to data from a range of plans makes it feasible to create a richer set of metrics and analysis to assess performance.

Everyone realizes that spreadsheets can be a problem when they're used in planning and budgeting, but nobody seems to want to get rid of them. What do you advise people to do with them?

RK Use a balanced approach, understanding where spreadsheets can be useful and where you should avoid them. It's not practical to try to get rid of spreadsheets altogether. But establish an ongoing review of where they are used in planning and budgeting and a process for identifying the ones that must be replaced because they undermine accuracy and reliability.

How well do companies use analytics in planning and budgeting?

RK Not well. Our research shows that most get the basics right and are able to perform standard financial analysis but make limited use of advanced analytics. For example, predictive analytics is valuable for multiple purposes across multiple roles. Using statistical models, analysts can derive new insights into business drivers directly from data or create more reliable baseline forecasts. It can help identify strong correlations that can improve forecast accuracy or understanding of where there is a lack of predictability in the business and therefore greater risk in planning successful outcomes. Some of these models may involve internal operating relationships, but others can determine the impact of weather, the timing of movable holidays such as Easter or Thanksgiving in North America and published leading indicators (such as purchasing managers' indices). Still, our research finds that fewer than half of companies use predictive analytics or leading indicators regularly; only 36 percent said it's very important to apply predictive analytics.

Companies aren't able to make full use of analytics in their planning and budgeting because of their heavy use of desktop spreadsheets. Spreadsheets are great for the basics but not for advanced analytics. One reason is that they don't do well in enabling manipulation of more than a couple of business dimensions at once – dimensions such as sales territories, business units, products, customers, currency and time. Pivot tables can take you only so far. Using spreadsheets also consumes time that could be better spent in expanding the range of analyses and reports available to everyone. Increasing the scope and sophistication of the analytics produced by the finance organization can have a positive impact on a company's performance. Analytics is an important tool whose ultimate purpose is to enable executives and managers to make better-informed decisions.

You have emphasized the value of contingency or what-if scenario planning. How well do companies use it?

RK We find limited use of in-depth contingency planning that enables executives and managers to understand both the operational and financial consequences of specific choices they make or the impacts of external conditions such as changes in a competitor's strategy or in the economy. Contingency planning usually is limited to a financially focused set of plans including a base case, a conservative case and an upside or optimistic case. Only 23 percent of people doing demand planning, for example, said they can explore all relevant scenarios to quantify and understand the implications of various assumptions. Simplistic scenario planning was fine when there was no practical alternative, but today's software can make it much easier to understand how certain events will affect operations and the bottom line.

What is the value of using dedicated software for financial planning?

RK Our research shows that dedicated applications are superior to spreadsheets in terms of how well they perform and how satisfied their users are with the planning process. Organizations that use such software get better results: 87 percent of companies that said their software performs very well also said they have a process for creating finance analytics that works well or very well. Only 37 percent of companies with software that works neither well nor poorly have a good planning process. Companies invest a considerable amount of time in financial planning, and they should insist on getting the highest return on that investment by cutting the amount of time it takes to plan and making the results of that financial planning and analysis much more valuable.

