How can Finance Leaders Bridge the FP&A Gap?

Insights & Opportunities for Finance Transformation

Prophix® | FSN® The Modern Finance Forum

Inside this document

Introduction

Transforming the finance function goes deeper than upgrading technology. It's using that technology to fundamentally change the role of Finance – from reactive to proactive, reporting to predicting, observing to advising. Taking on this new role, however, requires finance professionals to develop new capabilities and presently, planning, budgeting and forecasting are in the spotlight.

FSN & Prophix recently conducted a survey of CFOs to see how Finance functions are progressing with the digital transformation of their planning, budgeting and forecasting process. The survey sought to understand their capabilities in forecasting, automation, analytics and more.

The study found there are sizable gaps in abilities and outcomes in nearly every category. But every gap is an opportunity to build a bridge and drive collaboration internally.

The COVID-19 pandemic has been a notoriously difficult period for every business. In this period of tumult, the role of planning, budgeting and forecasting is becoming even more pivotal to the success of a business, and those falling short of accuracy and insightfulness are adding to their burden. Producing accurate, far-sighted forecasts and being able to respond quickly to change within and outside an organization are invaluably agile skills, but not ones universally demonstrated.

The Agility in Planning, Budgeting and Forecasting survey found some organizations fall well short of the basic competencies necessary to maintain an agile planning, budgeting and forecasting (PBF) process.

The survey finds that around two thirds of organizations manage to reforecast their earnings in under a week, but only 39% are able to do so within +/-5% accuracy, reflecting a decline from the 42% who were able to do so four years ago.

The picture deteriorates substantially when determining whether companies have agility in forecasting further into the future. 80% of companies are unable to forecast beyond a year, and over 50% cannot see further than 6 months ahead.

Companies are reasonably agile when making changes to the PBF process in times of flux, with around two-thirds able to quickly make minor changes to a cost line or business model. However, making more substantial changes to organizational hierarchies is proving more challenging.

Solutions

Solutions

While agility is lacking in many areas, the survey finds that organizations that had made headway in transforming their PBF process are better equipped to handle change. Around a third of participants had made some efforts to transform PBF, although only 5% claim to have completely transformed the process. That said, those 5% are able to forecast quicker, more accurately and with greater foresight into the future than the transformation laggards. They are also able to manage their data better and used more advanced BPF tools.

The importance of data – its validity, trustworthiness and relevance – is widely recognized as a key component of agile planning, budgeting and forecasting. What is not as universally accepted is the importance of connecting with more users outside of the finance function. In addition, internal data sources are valued above external ones. However, including a variety of perspectives and data sources from across the spectrum is crucial to extracting the best insight from the PBF process.

Process Power

Process power

Even as many organizations fall short of a truly agile planning, budgeting and forecasting process, there are others that improved their lot substantially by introducing process improvements. The survey found that rolling forecasts lend more agility than quarterly ones, zero-based budgeting improves outcomes ahead of more traditional budgeting methods, and companies that find time to implement scenario planning are much more agile than their competitors over the longer term.

Twelve-month rolling forecasts are used by between 19% and 25% of companies depending on size (larger organizations are more inclined towards this), and it helps with many aspects of agility. Reforecasting time improves, accuracy is positively affected and the ability to respond to organizational change is markedly better than companies that only reforecast quarterly. Rolling forecasts are difficult to implement using cumbersome spreadsheets, which is why the survey finds that those that choose to use this method are likely to have already invested in specialist PBF software.

Meanwhile, companies committed to improving their budgeting outcomes are turning to other helpful methodologies including zero based budgeting (ZBB), and this is having a positive impact on agility. ZBB requires budget holders to 'start from zero' and justify their resource requirements at each budget setting. It is particularly pertinent in the context of profound business changes such as COVID-19. The survey shows that ZBB improves all round performance of the PBF process, particularly, in the area of forecast accuracy. The survey finds that this foresight can be significantly improved when companies use scenario planning. This strategic method of analyzing alternative scenarios and their potential outcomes is a significant indicator of better future forecasting.

A mere 4% of organizations make sufficient time for effective scenario planning, although there has been a surge of interest in scenario planning since the pandemic swept away assumptions and forecasts with unprecedented speed and ferocity. The complexity of managing and running various scenarios means companies that are still wedded to spreadsheets will be severely limited in what they can achieve. Only those organizations that have mastered their data and deployed specialist tools are able to properly enjoy the benefits of scenario planning.

Scenario planners are faster, more accurate and can see out further into the future than companies which fail to make the time for scenario planning, and they are able to make changes to their systems and processes quickly and with more agility. They make use of a wider range of stakeholders from within and outside the company in order to produce the most effective plans, and they manage their data as a corporate asset which allows them to use cutting edge tools, artificial intelligence and machine learning to drive predictive analysis.

The improvements seen in companies that produce 12-month rolling forecasts, engage in zero based budgeting or make time for scenario planning are not mutually exclusive.

The survey confirms that companies that utilize all these techniques and have transformed their PBF processes, (mastered their data sources and implemented specialist tools) significantly enhance their agility in all aspects of planning, budgeting and forecasting. There are opportunities to adapt as the world changes around us, but organizations won't be able to take advantage of them unless they have a clear vision of their future, and for that they need supreme agility in planning, budgeting and forecasting.

What is agility?

- The ability to move quickly and easily = The velocity (speed & direction) of the PBF process
- The ability to think quickly and clearly = The quality of analysis for decision-making
- A recognition that making changes is an important part of the job = How easy is it to change the PBF process under strain

Source: Cambridge dictionary - What does this mean for business?

Where is Your Organization on the Agility Dial?

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Where is your organization on the agility dial?

The ramifications for businesses from the global pandemic have ranged from catastrophic to opportunistic, with all shades in between. Many faced closures, furlough, customer losses and supply chain disruption and have had to navigate rapid changes internally and externally with little or no warning.

With visibility already severely compromised, organizations were often slow to respond, had difficulty understanding where the business was in the maelstrom and failed to plan, budget or forecast effectively. As the economic, social and political variables changed, companies needed to reforecast, sometimes weekly, with reasonable accuracy and with organizational precision. But many couldn't. FSN's Future of Automation in the Finance Function survey last year found pervasive pandemic disruption in planning, budgeting and forecasting (PBF), hamstrung by the twin impacts of a lack of automation and the vastly altered economic situation.

The unprecedented nature of the pandemic is not an excuse for inadequate planning, budgeting or forecasting, because organizations must be able to shift focus and respond to stressors in 'normal' times too.

Competitor activity, disruptors in the market, organizational change or acquisitions and disposals all require agility in planning, budgeting and forecasting.

This means companies must be able to budget and forecast quickly and accurately as well as being able to easily make changes to the PBF process when circumstances require.

This survey explores the depth of the issue, identifying the necessary drivers of agility and the ways organizations on the wrong side of the PBF agility curve can improve their response to change. The evidence shows, that while there is speed, PBF is not always accurate, fails to provide insight further into the future, and is only superficially efficient, failing to reflect complex change quickly.

Agility is benchmarked against 3 key areas:

Velocity

Accuracy

Ability to change the PBF process under strain

Organizations can benchmark their own agility against three key stress tests:

Velocity - The time to reforecast earnings and revenue should be under a week (speed), and organizations should be able to forecast a year ahead with confidence (direction).

Accuracy - Agile companies should be able to forecast earnings and revenues to within +/- 5%.

Ability to change the PBF process under strain - Companies should be able to make a minor change to their budget, and should be able to roll out that change to budget holders' templates, within half a day. Agile companies should also be able to make a simple change to their hierarchy in the same time-frame.

So How Did Respondents to the Survey Compare on Headline Agility Benchmarks?

So how did respondents to the survey compare on headline agility benchmarks?

Two thirds demonstrate agile speed, reforecasting earnings in under a week, but the remaining third struggle to turn their forecasts around in that time and 6% take more than a month to reforecast.

Smaller organizations are more able to reforecast earnings within a week, which may be impacted by the smaller number of people involved in their processes, whereas large organizations are most at risk of an extended reforecasting process.

The bottlenecks in the process are clustered around the human interface, where data collection and budget reviews require input from people. Even as technology takes on many of the previously manual tasks, and data is increasingly recognized as a managed asset, survey respondents appear to spend a disproportionate amount of time collecting current year's data from budget holders as well as finalizing or signing off the budget.

The research finds that there is no correlation between the amount of time spent on the PBF process and the accuracy or ability to forecast further into the future. So while people issues are causing the bottlenecks, they aren't adding to agility.

66%

of finance functions are able to reforecast within one week.

While speed is relatively dependable, accuracy is more elusive. Only 39% of senior finance executives are able to forecast earnings within a +/-5% margin of error. It seems that even companies that take longer to reforecast (more than a week) are still stymied by accuracy. 58% of those slow to reforecast are unable to do so within +/-5%.

FSN's Future of Planning Budgeting and Forecasting study in 2017 found that 42% were able to forecast earnings within +/- 5% accuracy. Three years later that figure has fallen to 39%.

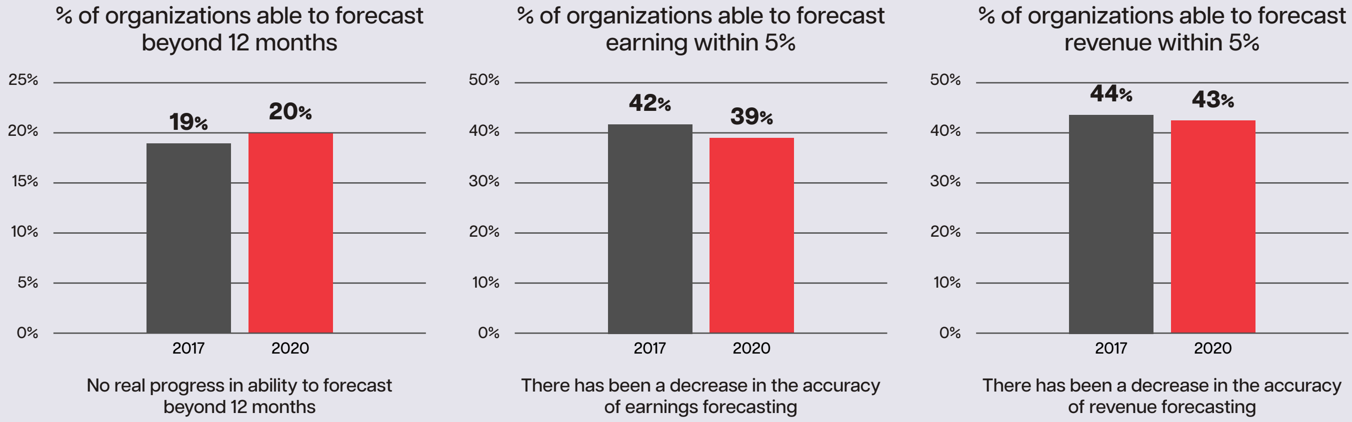
Organizations face a similar issue forecasting revenue with any accuracy as only 43% are able to forecast within +/- 5%. This represents another decline from the 44% which were accurate to within 5% four years ago.

The picture deteriorates substantially when determining whether companies have agility in forecasting further into the future. 80% of companies are unable to forecast beyond a year, and over 50% cannot see out further than 6 months. Four years ago the situation was just as dire, with only 20% able to forecast beyond 12 months, and there has been little progress since then.

Corporate agility came to the fore during the pandemic when organizations needed to make simple changes quickly and accurately as the environment around them changed. For two thirds of organizations this was relatively easy to do. 64% of respondents said they are able to make a minor change, for example, to a new cost line in their budget or forecast models, within half a day. And 68% said they could have that change reflected in budget holders' data entry template, reflecting the change within all of the reports, within the same time frame.

Only
39%
of finance functions are able to forecast earnings within +/-5% accuracy.

Figure 1: There has been no progress in speed and direction since 2017.



But that percentage falls to 34% when the change is one of organizational hierarchy. When a business needs to reflect a new entity, cost center or product, only a third can manage this within half a day, another third within 2 days and the rest at some point between 2 days and more than a week. The COVID-19 lock-downs forced many companies to contract or close down parts of their operation, but most were unable to reflect these in their forecasts as they happened.

Without the agility to flex the content and participation in the budget process depending on need, organizations are not able to tap into the wider knowledge base across the business, especially drawing on input from outside the finance function. This is important because previous FSN research shows that involving people from different functional areas, who might be closer to the sharp end of the business, improves the richness of the forecasts.

High budget participation (the percentage of employees that provide input into the budgeting and planning process) is only possible when the process is agile and adaptable. But a third of companies draw on just 1% of the workforce, 22% draw on 5%, and 16% draw on 10% of the people in the organization.

80%

of finance functions unable to look out more than a year.

Only 28% reach 25% to 50%, a level which incorporates a broad range of corporate inputs that likely improves depth of insight.

Simple quick changes to the budget lines and relatively speedy reforecasting are within the grasp of around two thirds of companies, but accuracy remains elusive for many more than that. Whether it is a combination of low participation, haste (speed is important but not at the cost of accuracy) or outdated processes, there is a long way to go to build truly agile planning, budgeting and forecasting.

Transformation Improves Agility

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Transformation improves agility

Preparing for and managing change is a fundamental part of business success. This includes both the tectonic shifts in social and economic stability that occur during unexpected events like the financial crisis and COVID-19 pandemic, as well as the shifts that take place normally through the course of business, like changes in consumer demand, new business models, acquisitions or competitor disruption.

Effective planning, budgeting and forecasting enables organizations to thrive in the face of change, although many businesses have not embraced change within the PBF process itself.

The majority of organizations have not made any major changes to their PBF processes in the last three years. Only 36% have made substantial or transformative changes during that period, with the remaining 64% either implementing minimal improvements or no change at all.

In looking to understand how transformation impacts the agility of planning, budgeting and forecasting, the survey compared the 5% of companies that have enacted complete transformation of PBF with the 14% that have put no effort into it in the last three years. The results show a distinct difference in how each manage their data. Those that have achieved complete transformation are able to manage data as a corporate asset rather than being overwhelmed by disconnected spreadsheets with poor data governance.

Just 36% able to say they have made a significant change or completely transformed their PBF process.

Figure 2: degree of transformation achieved

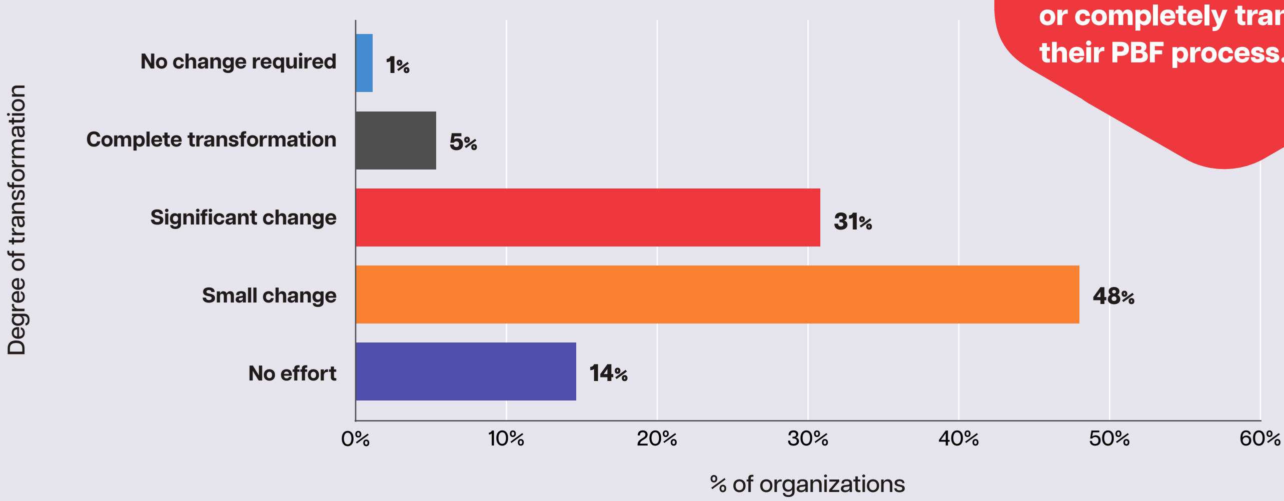
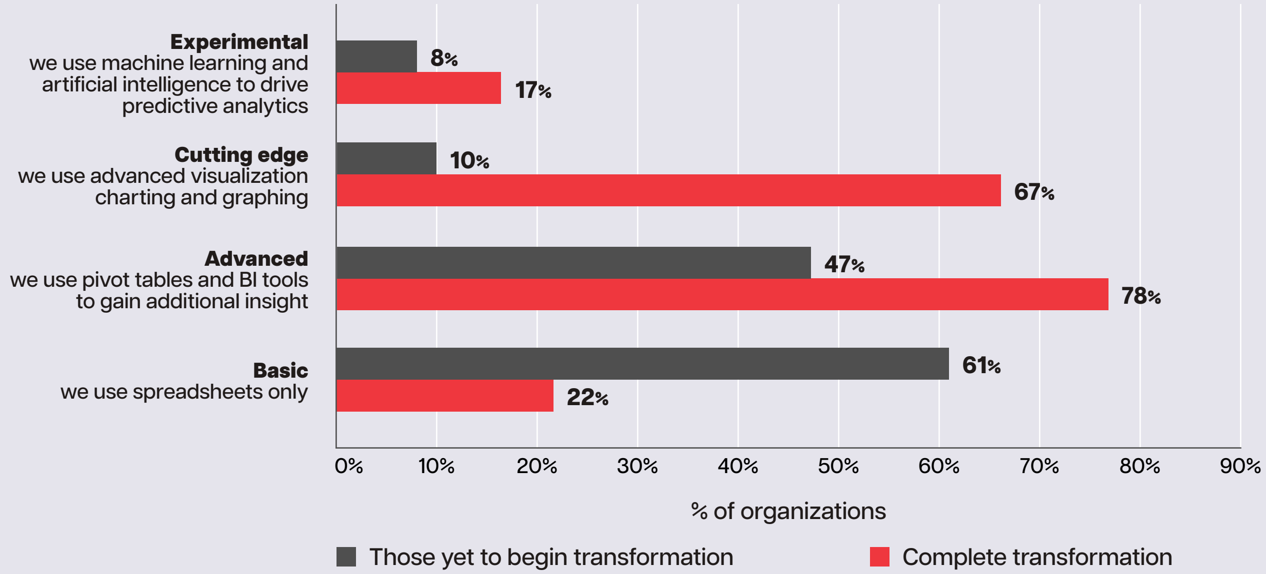


Figure 3: Percentage of organizations using basic, advanced, cutting edge and experimental tools



With this ability to manage their data, they have made the move away from basic spreadsheets to more “advanced” spreadsheets (pivot tables) coupled with BI tools and “cutting edge tools” for data visualization, although truly “experimental tools” (Machine Learning and Artificial Intelligence) are still out of reach even for those that have completely transformed their process. Earlier FSN research from Innovation In the Finance Function found that AI and Machine Learning are the preserve of just 14% of companies with more than 10,000 employees.

31% of transformation leaders able to forecast beyond 12 months, compared to just 11% of those who have yet to begin transformation.

Verified, well-managed data is a clear priority for improving the agility of the PBF process, and transformation improves the speed of reforecasting, essentially halving the time it takes to reforecast earnings and revenue and allowing organizations to reforecast more frequently.

In comparison to the transformation laggards, transformation leaders are able to forecast further out on the time horizon, with 31% looking out 12 months and beyond, compared with just 11% for transformation laggards.

Transformation experts are turning their attention to unifying and standardizing the budget process and managing the process in the cloud, which will ultimately add to their already robust PBF agility.

Foresight is a key component of PBF and being able to see beyond a few months is a must. Transformation programs improve the integrity or trustworthiness of data, improve analytic capabilities, and enable faster and more accurate forecasting further out into the future.

How Data Can Improve Forecasting Agility?

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How data can improve forecasting agility?

Investment in automation is misdirected

The accuracy of planning, budgeting and forecasting is critical to preparing businesses for their future and ensuring they are well-equipped to fulfill their potential. But as the research shows, there has been little improvement in accuracy over the last four years. In order to improve accuracy, organizations need to go to the source of the insight – the data they collect and the tools they use to analyze it.

Data

The quality of data used determines the quality of forecasting outcomes, an important aspect of agility. Senior finance executives understand this, and 84% said that improving the relevance of data captured is the most fundamental area that needs to change in order to improve agility.

A further 70% consider that exploiting non-financial data would improve agility, while 59% would consider a move to rolling forecasts. But only half see the value of connecting with more users outside of the finance function. The other half are missing an important tool in their PBF arsenal because casting the net beyond the finance function broadens the data pool which can increase forecast accuracy and the richness of insights.

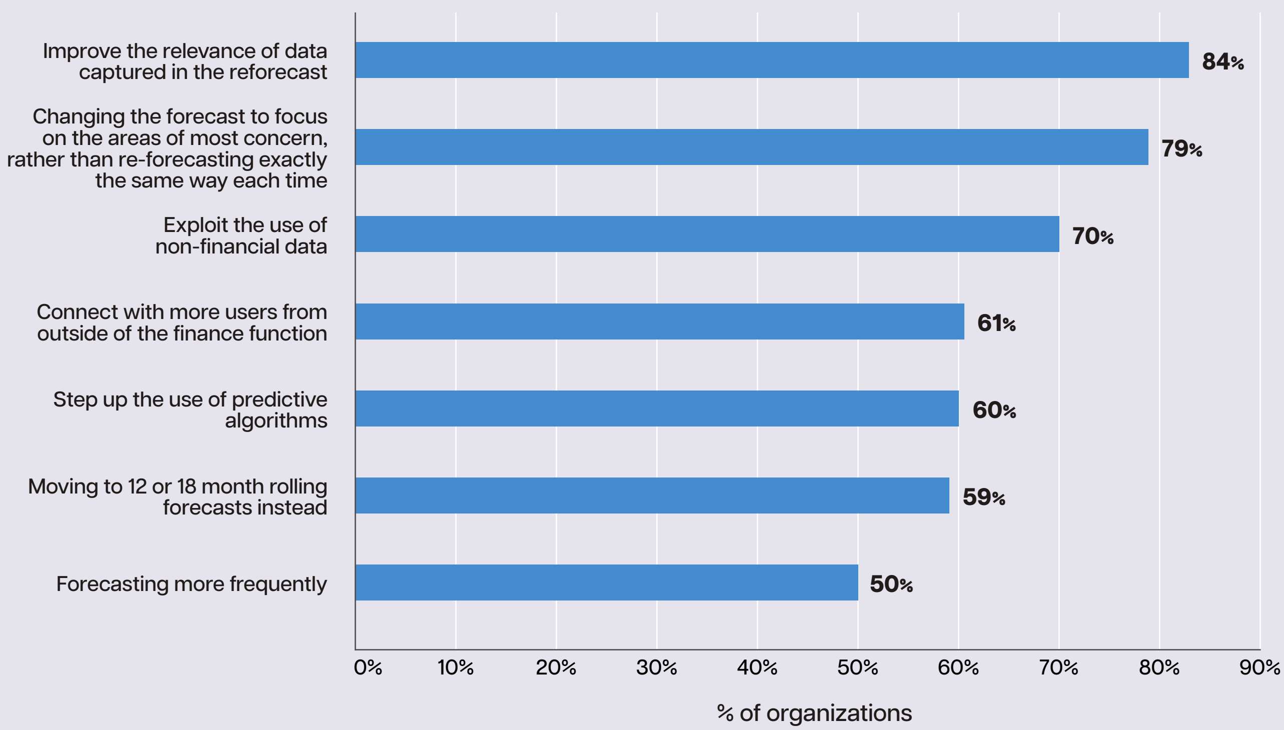
Respondents are more inclined to look internally for new data sources, relying heavily on what they already know. But, identifying operational data outside the general ledger (83%), customer relationship data (65%) and other sources of non-financial data (76%) would lend an even more insightful and agile perspective to PBF.

84% of respondents said that improving the relevance of data captured is the most fundamental area that needs to change in order to improve agility.

Disappointingly however, fewer finance executives consider that looking outside the organization adds insight and agility to the PBF process, although some recognize the value more than others. 63% see external data sources as a key PBF contributor, with 53% recognizing the value in customer web analytics and 37% turning to social media analytics to provide richer context for their planning, budgeting and forecasting.

It's perhaps unsurprising that external data takes a back seat to internal data, as on the continuum of necessity, the information within an organization tends to be mined first, yet many organizations aren't even doing that well enough. But the importance of external and non-financial data can't be overlooked. Previous FSN research has pointed towards the competitive advantage gained by using non-financial data, especially against more agile start-ups or rivals that are already using non-financial data for added insight.

Figure 4: How would you improve the agility of the forecasting process?



The explosion of social media engagement is commonplace in consumers' day to day life, but organizations have been slow to recognize the value in these interactions. For example, some traders use social information arbitrage to spot new trends and buy into them before they take off, the sort of advantage that companies in competitive markets could use. That's not to say social media is the answer to the accuracy issue in PBF, but it's important for finance professionals to look outside their daily remit for data that will help improve their accuracy, and it could come from unusual places.

Tooling up

As the data pool increases and becomes more diverse, so must the tools used to analyze the data. In the planning, budgeting and forecasting space, the right tools, like specialist software, are profoundly under-utilized. Almost two thirds of organizations do not take advantage of specialist PBF software, instead relying on spreadsheets.

54% of respondents said they were looking to unify the budget model across the enterprise.

Vocalizing their technology priorities, just over half of respondents said they were looking to unify their budget model across the enterprise, 49% wanted to remove standalone spreadsheets for reporting and 46% wanted to remove spreadsheet data entry.

Meanwhile 37% would like to use just one vendor for budgeting solutions, whilst 30% would like to manage the entire process in the cloud. Surprisingly, cloud applications are not yet seen as a unifying platform, capable of bringing data together for the whole organization in one place.

Figure 5: What are your priorities for improving agility through technology?

Prophix Customer Story

Milo’s Tea is steeped in budgeting and forecasting success

Prophix

Milo's Tea is steeped in budgeting and forecasting success

Milo's Tea, a family-owned manufacturer of 100% natural ready to drink beverages including sweet tea and lemonade, struggled to involve department managers in the budgeting process while relying on Excel as their primary finance tool. Prophix has allowed their finance team to budget and forecast collaboratively by involving staff in the process.

Establishing a forecasting process and cadence was one of the top priorities of Milo's Prophix implementation. With an FPM solution, Milo's Tea can easily create flexible, accurate forecasts that empower their finance team to make strategic business decisions based on real-time information.

Read the full customer story here.

About Prophix

Your business is evolving. And the way you plan your business activities and report on them should evolve too. To empower mid-market companies to achieve their goals, Prophix provides an integrated, cloud-based platform to the Office of Finance; one that delivers planning, budgeting, reporting, forecasting and consolidation solutions. With Prophix, finance leaders improve profitability and minimize risk and puts the focus back on what matters most – uncovering business opportunities. Prophix supports your future with AI innovations that adapts to meet your strategic realities, today and tomorrow. Over 2,500 active customers around the globe rely on Prophix to transform the way they work.

NORTH AMERICA

CANADA

350 Burnhamthorpe
Road West,
Suite 1000
Mississauga, Ontario
L5B 3J1
1 (800) 387-5915
+1-905-279-8711

UNITED STATES

707 SW Washington St.
Suite 1100
Portland, OR 97205
1 (800) 387-5915

UNITED KINGDOM

Davidson House
The Forbury
Reading
RG1 3EU
+44 (0) 118 900 1900

EUROPE

BELGIUM

Lenniksebaan 451
1070 Brussels
+32 (0) 2 456 89 60

DENMARK

Sankt Knuds Vej 41
1903 Frederiksberg C
+ 45 7023 2375

FRANCE

Roosevelt House 6
avenue Franklin Roosevelt
75008 Paris
+33 1 88 86 00 24

GERMANY

Messeturm
60308 Frankfurt am Main
+49 69 509 565 607

ITALY

Via Paracelso, 26
20864 Agrate Brianza (MB)
+39 039 890 1574

LUXEMBOURG

22, rue de l'Industrie
L-8399 Windhof
+352 27 02 01 20

THE NETHERLANDS

De Boelelaan 7, 7th floor
1083 HJ Amsterdam
+31 (0)85 400 01 30

PORTUGAL

Av. D. João II n°35
Edificio Infante 11°A
1990-083 Lisbon
+351 308 806 770

ASIA

INDONESIA

Jl. Letjen S. Parman Kav. 28
West Jakarta 11470
+6221 5021 2222

MALAYSIA

No. 2A, Jalan Sepadu
Off Jalan Klang Lama
58200 Kuala Lumpur
+603 7972 9129

SINGAPORE

Blk 18 Boon Lay Way #07-109
Singapore 609966
+65 6316 8681

SOUTH AMERICA

BRAZIL – SÃO PAULO

Rua André Ampére,
153/7o andar
Novo Brooklin – SP
04562-080
+55 11 3583-1678

BRAZIL – RIO DE JANEIRO

Av. Marechal Câmara 160 cj 932
Centro – RJ
20.020-080
+55 21 3094-3900

FIND US ONLINE

prophix.com

info@prophix.com

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