

Planning: Turning a Chore Into an Asset

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From “we’ll see what happens” to “we saw it coming”.

“Planning. Budgeting. Forecasting. Ugh. I guess we have to do it, usually because someone else wants it done. Could be a lender. Could be the Board. But, what really is the purpose? We are going to do the best we can and other than comparing to what we guessed at an earlier time, it doesn’t have any impact on how we act during the period. There are so many things outside our control anyways, what difference does it make?” This is what is often said and sometimes not said but believed by many leadership teams of middle market companies. It often speaks the truth about how companies are managed and the somewhat fatalistic view of the market and the future by its leaders.

It plays out repeatedly. Managers produce a financial plan for a period (often a year) and then go about their business. The plan and activities are not connected because there’s nothing to connect them; the plan is not in enough detail to provide guidance to middle management, and middle management is not held accountable to performing against the plan. The resulting reality is that it wasn’t a plan that was produced, it was a projection, or best guess. At the end of the period, a comparison to plan can be made but it is more as a point of curiosity to test the accuracy of the prediction, but not really to

make any major adjustments to the next go-round. The managers did the best they could and that is what matters. The truth of that last sentence misconstrues the value of effective planning as it relates to decision making and achieving goals.

Planning is not about being a fortune teller. Nobody can predict the future, and since most organizations view planning as “predicting,” increasing uncertainty about the future of a business results in the dwindling of most planning activities.

In order to make a few suggestions about how to implement more effective planning, especially in organizations affected by the unknown, first we should break out the purpose of planning and why it is of value to a business and a CEO.



Planning is not about being a fortune teller. Nobody can predict the future, and since most organizations view planning as “predicting,” increasing uncertainty about the future of a business results in the dwindling of most planning activities. Planning is, however, about understanding tradeoffs and implications. Think of planning as a series of “if-then” considerations: *if* a certain set of circumstances comes to pass, *then* the impact to our organization is likely to be X, *and* that flows through the economic structure of the business to result in Y and Z financial impact. Once those relationships have been established, the organization can then use them proactively: to create contingency plans, to build flexibility around the largest unknowns, or to make changes to the organization itself.

Understanding how the system works and reacts to a wide variety of external stimuli is critical for answering all kinds of questions inherent to any business:

Capital Needs

A business needs capital. How much, when, and for how long are questions that should be answered to determine the best match

of capital to its purpose, thereby providing the lowest cost for the amount and flexibility that is prudent to support achieving the business plan.

Understanding the external capital need profile can only occur through having a perspective on the future outcomes of the company.

Compliance

If part of the capital used to fund the business is from a commercial lender, they will have covenants of financial performance that need to be met, or risk having that source of capital interrupted. Again, knowing with a high degree of confidence that those covenants can be met only comes from detailed forecasting of business activities and the resulting financial implications.

Alignment of Activities

Spreadsheets don't run companies, people do. Activities lead to numbers. Employees perform activities. Knowing the relationships between activities and financial metrics allows individual functions or departments within the company to plan out the activities each needs to achieve (and when) in order for the overall plan to be achieved. It gives a basis by which managers can monitor, adjust or stay the course. It allows everyone within the organization to know what they can do to positively impact the company's goal achievement.

Ongoing Business Decisions

Like product pricing, organization changes, inventory investments, capital expenditures, supply agreements, or collection timing and policies. All of these can be changed within a planning period, often with good reason, but each also has an impact on the amount and timing of cash flow to the business. Is the impact positive? Is it positive enough? Does timing matter?

The more complex the business, the less connected any single forecast will be from future activities. Everyone knows that a forecast will be wrong, and as the variables increase, the plan's utility as a single source of truth declines, and it ends up not being used in any decision-making structure as time plays out. Good planning should produce a most likely forecast, but that should be the result of a detailed consideration of the economics of the business and the impact of changes in all variables that affect its performance. The sensitivity analysis of the impacts of changes in the most likely set of assumptions is the most valuable, as it allows plans B, C, and D to be developed in real time as the world throws us curveballs. This kind of planning allows decision frameworks to be set up with forethought, event or condition.

The only way to combat fatalism is to have systems to collect and process operational data quickly, paired with a robust

interactive planning model that can quickly (with emphasis on the word "quickly") absorb changing conditions and project future results. Such a tool should allow sensitivity analyses to be conducted on sales prices, product volumes by form, costs, timing, and other metrics unique to any individual business. Issues such as the availability of cash to support operations, conformance with loan covenants, and the effect on economic returns can be known as actions are being considered.

The only way to contain chaos is with energy. Data accuracy requires systems, both human and electronic, and analysis of this data requires skilled people who can build robust analytical tools, working alongside those in the business who can link tangible activities to spreadsheet cells.

Each business faces forces that are not in its control, but that is not an excuse for lack of planning. In fact, it is a call for more planning, because the CEO needs to keep the ship on course regardless. In business, at sea, and in life, the unexpected should be expected: storms, equipment breakdowns or failures, sickness, lightning strikes, and plenty other. It is the CEO's responsibility to make sure the ship arrives in port on time. Without effective planning, the goal becomes aspirational and not of much use.

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