Financial Planning & Analysis: What It Is & Why It's Important

Arthur F. Rothberg, Managing Director, CFO Edge, LLC

When they hear the term "financial planning and analysis," or FP&A as it's often referred to, many small and mid-sized business owners tune out, assuming it's something that only large corporations can benefit from. But this can be a big mistake: Any size firm can benefit from conducting the forward-looking and strategic exercises that are a part of the FP&A process.

What Exactly Is FP&A?

Financial planning and analysis goes several steps beyond simple accounting. It encompasses everything involved in the creation of an organization's long-term financial strategy. This includes the generation of management reports, analysis of financial trends, forecasting of sales and earnings, establishment of budgets, and calculation of the financial effects of decisions made at all levels of the company — but especially the executive level.

FP&A is focused more on looking forward and planning ahead than it is on looking back and measuring what has already happened in the past, which is what traditional accounting does. Employees performing FP&A use a wide range of different financial tools, including budgeting, planning and forecasting software; corporate performance management software; core financial management systems; and ERP platforms.

In December, *The Wall Street Journal*[1] reported that The Association for Financial Professionals (AFP) has created a credentialing program for FP&A that requires students to spend approximately 72 hours preparing for a two-part exam that tests their basic financial knowledge and ability to perform free-form spreadsheet modeling. To enroll, students must have between two and three years of work experience and pay an exam fee.

Rising Up the Maturity Ladder

An article published last year on CFO.com – *Why Is Financial Planning and Analysis Falling Flat?*[2] – pointed out research conducted by the American Productivity & Quality Center (APQC) that found only 40 percent of finance executives rated their FP&A capabilities as effective. The article stated that, "FP&A at many companies is not very far up on the maturity ladder."

The main reason why, according to the APQC study cited, is because most finance teams are overwhelmed by basic financial management tasks, such as periodic forecasting of current performance trends compared to budget targets. This leaves staff with little time for more strategic FP&A activities like investigating cost drivers or testing possible outcomes of pricing and bundling options.

There's little question that if small and mid-sized firms want to incorporate more strategy into their long-term financial planning, they need to incorporate FP&A into their planning process. But while most CFOs who participated in the APQC research said they're willing to invest in better financial systems and data models, they were not as willing to polish their FP&A process models or develop analytical talent on their finance teams.

However, the APQC research did conclude that more organizations are moving toward rolling budgeting and forecasting, which is a key component of FP&A. The study recommends forecasting revenue and margins between four and eight months into the future so that companies are able to better anticipate and plan for emerging trends and be more agile when it comes to adapting to these changes. By contrast, we prefer forecasting four to six quarters into the future. With this longer perspective, for example, a company halfway through its fiscal year gains enhanced decision-making views of both the balance of the current year and the entire next year. According to the research, companies that conduct rolling forecasting:

- Are better aligned with unfolding business strategy
- Are more effective at business analysis
- Derive greater value from the budgeting and planning processes
- Enjoy more reliable forecasts

Perhaps most tellingly, 94 percent of the companies that participated in the research who use rolling forecasts said that their business analysis is effective, but only 50 percent of those who don't use rolling forecasts said the same thing. Using rolling forecasting and budgeting is a fairly basic FP&A task — most CFOs in the study who used more advanced FP&A techniques like scenario analysis and predictive analysis said they are better aligned with their company's unfolding strategy.

If you own a small or mid-sized firm, you might not have the capabilities or expertise on staff to engage in most FP&A activities. By hiring an outsourced CFO services provider, you can benefit from the same advanced FP&A techniques used by large corporations, but at a fraction of the cost of hiring this high level of financial expertise on a full-time basis. An experienced outsourced CFO has helped many other companies like yours reap the strategic financial benefits of FP&A.

Concluding Thoughts

Financial planning and analysis isn't just for big corporations — any size firm can benefit. FP&A is focused more on looking forward than it is on looking back and measuring what has already happened in the past. If you want to incorporate more strategy into your long-term financial planning, you should incorporate FP&A into your planning process. An outsourced CFO can help you benefit from the same advanced FP&A techniques used by large corporations.

1 http://www.wsj.com/articles/metrics-sell-doughnuts-and-more-1450744304
2 http://ww2.cfo.com/accounting-tax/2015/03/financial-planning-analysis-falling-flat

About CFO Edge

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