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Financial forecasts

Business Link

What is a financial forecast?

Financial forecasting is a planning tool for predicting the probability of something happening in response to a given set of circumstances. Financial forecasts are used to support a business plan.

Whereas the business plan details the objectives and intentions of an enterprise the forecast translates these intentions into numbers. The numbers show the likely outcomes of the intended activities and the resource requirements needed to achieve them. Financial forecasts are therefore the key resource used to identify the funding requirements for a new venture, a new project, or the ongoing activities of an existing enterprise.

Financial management is usually the greatest weakness for most enterprises and therefore the area that funders and lenders always concentrate on. The forecasts will give them an insight into the enterprise management team's understanding of finance, approach to risk and approach to reality.

How does a financial forecast work?

Your financial forecast allows you to validate what you are hoping to achieve in your business plan. By using numerical data you can:

- see whether your targets are possible
- show that your predictions are realistic
- examine the timing of delivery or sales
- see if you have sufficient resources
- identify additional resources e.g. cash, people, facilities etc.
- demonstrate the desired outcomes
- prove the sustainability of the project/ enterprise
- manage your enterprises within given resources

For those reading the business plan the forecast informs them about:

- the logic of the delivery plan
- how the outcome targets are going to be achieved
- the timing of the delivery
- the necessity of the additional resource requirement
- the sustainability of the project/ enterprise
- the ability of the management team to manage limited resources

The forecast, once agreed, is used to create more detailed budgets. These are used by the enterprise, either as a whole or department by department, to plan, implement and later measure actual activity against what has been predicted.

What financial forecasts should include

Financial forecasts should ideally consist of:

- a profit forecast
- a cash flow forecast
- a balance sheet
- notes to cash flow
- assumptions supporting the profit and cash forecasts

Most enterprises attempt to only present a cash flow. However, if you are looking for bank funding (an overdraft or loan), soft loans (from social lenders) or investment funding, having the other components in

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place allows for a better appreciation and judgement of your business plan. The more answers you provide the stronger your business case.

The figures should be supported by a set of assumptions. The assumptions form the basis of the forecasts and explain how the information in the forecasts has been derived.

It is normal for the financial forecasts to cover a three-year period. However, many lenders often request five or even ten year forecasts. This may depend on the amount you wish to borrow and the expected repayment period or the enterprise's maturity.

A well-structured forecast allows the user to change various assumptions to measure the impact of these changes on the predicted outcomes.

Further information

Read our guide on Developing assumptions for financial forecasts:
www.bllondon.com/SocialEnterprise/Fundingandfinance/Financialplanning/Developingassumptionsforfinancialforecasts.aspx