

# Characteristics of Quality Forecast: A Review Study

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## ABSTRACT

A quality forecast is a reliable and accurate prediction of future events or outcomes based on available data and analysis. This abstract explores the key characteristics that contribute to a quality forecast and its significance in decision-making and planning. It emphasizes the importance of data quality, forecasting techniques, validation and monitoring, transparency, and adaptability in producing high-quality forecasts. Additionally, it highlights the benefits of quality forecasts in various sectors, including business, finance, economics, and weather forecasting. Data quality is a fundamental characteristic of a quality forecast. The accuracy, completeness, and relevance of the data used in the forecasting process are crucial in ensuring the reliability of the forecasted outcomes. Quality forecasts rely on robust data sources, appropriate data collection methods, and effective data cleansing and validation techniques to minimize errors and biases.

## KEYWORDS

Accuracy, Consistency, Data Integrity, External Factors, Flexibility, Forecast Horizon.

## I. INTRODUCTION

The future is reflected in a prediction. Working with a high-quality projection allows an executive to confidently make a significant choice requiring the commitment of significant resources. Does the prediction include all the data that is relevant to the choice being considered? Here are a few forecasting qualities that might reassure the analyst and the decision-maker.

### Incrementality

The financial projection should incorporate all advantages, costs, and investments that will alter as a consequence of the choice. The idea of incrementality is that. This covers the price of extra support employees as well as indirect costs. It is incrementally expensive to add an engineer to the team in order to support the product. The price of the marketing research required to make certain market judgments is also included. Any expenditure is incremental if it arises from carrying out the choice; otherwise, it won't if the project isn't carried out.

Allotments for current company overhead should not be included in the financial projection. The forecast's goal is to determine the project's likely financial effect on the business. No matter what the choice, the corporate overhead will remain the same [1]–[3].

### Prediction Time Frame

With a few rare exceptions, the majority of predictions should indicate cash inflows for a maximum of five years. Future prediction is more challenging than ever due to significant technological advancements and the current state of the world economy. Although we hope the new company will be there forever, we are aware that this is unlikely to happen. The risk factors significantly rise if five years of cash inflows do not support the investment and allow the company to reach its ROI objectives.

Whether deliberate or not, adding years to the prediction may be considered analytical manipulation. Adding additional years of cash inflows can boost ROI. Therefore, employing a predetermined period of time gives the prediction legitimacy and assures comparability and objectivity.

The five-year rule does not apply for assessing the ROI for projects like pharmaceutical research or the building of large oil pipelines and nuclear power reactors. Even here, any new oil refineries built or drilling investments made between 2011 and 2014 were calculated based on the current price of \$100 per barrel of oil. In fact, at that period, the price of oil peaked at \$140 per barrel. Drilling technology has made incredible strides that have significantly improved oil access and reduced extraction costs. The recent settling of political unrest in Libya, Nigeria, and other significant oil-producing nations has increased the availability of oil. The cost of a barrel of oil increased to \$45 in 2015. The forecasting assumptions made in and after 2011 have all turned out to be disastrously wrong. And since the Fukushima nuclear power plant burned down in 2011 after the magnitude 9.0 earthquake, all investments in nuclear power have ceased, as have plans for new development. These investments may very well need time spans of ten years or more, and they should be evaluated in accordance.

## II. DISCUSSION

### Accounting Rules

The projection should adhere to the accounting principles and standards that will guide the company's reporting over the forecasted period. This is especially crucial since it pertains to tax filing, which will have a big impact on cash flow. The accounting format's rules should be followed, but only to the extent that doing so may affect cash flow. After all, the analysis predicts the future rather than just recounts the past.

### Outside Funding

The assumption that investments will be made entirely in cash should be made in cash flow predictions, and this assumption should be made at the time when agreements to buy assets are made. Even if the business anticipates receiving project funding from a bank or even the equipment suppliers, this should be done. The project and underlying risk start when pledges are made, which might happen before any money is ever paid out. Even while using external finance may be advantageous and even required, doing so raises risk. Debt service payments are a fixed expense that lowers the breakeven threshold for the business [4]–[6].

The first analysis needs to take into account the anticipated upfront financial investment if external funding is chosen. The basic case refers to this. The ROI determined using this methodology should be higher than the business's ROI hurdle rate. Then, analyses of potential sources of funding may be contrasted with this initial scenario. As a result, discounted cash flow analysis is used to assess loan offers from banks and other lenders. The ROI will dramatically rise after external finance is taken into account in the study. In reality, financing only delays cash withdrawals. The new projection will include the price of such loan. The ROI on the overall project should increase as a result of the before-tax cost of borrowing being much more than the after-tax ROI.

### Working capital expenditure

As previously stated, an investment is a monetary exposure with the intention of generating future cash flow advantages. If a project includes growing a company, more inventory will be required to make the extra items, and more receivables will be required to fund the sales that will be made. Investments include adding to inventory and accounts receivable as well as buying fixed assets. They have to be included completely into the project analysis.

### Prices and Economics

Forecasts should take into account existing operational expenses and product pricing. For three reasons, the corporation should never depend on greater potential selling prices to support existing investments:

1. As company grows, technology causes prices to decrease rather than increase. Every firm is exposed to growing price pressures due to global competition.
2. Potential rivals will be drawn to the market and will soon become genuine competitors if the project's execution is effective. Because of this, prices won't go up. The best examples of this include computers, computer software, operating systems, and drugs. Investing in a company with the assumption that selling prices will rise in the future is very risky.
3. You have to review the yearly economic estimates presented in the leading trade periodicals. These are polls of the top 50 economists in the nation. Their professional assessments' differences are startling. Extreme disparities exist between the most optimistic and pessimistic predictions for the gross national product, inflation, and unemployment. Most of these predictions will be inaccurate. Amazingly, these economists are just making predictions for the next year. How can we amateurs superimpose our economic projections on a ROI study and hope to be somewhat correct if professional economists couldn't estimate one year with accuracy? The best way to

cope with this uncertainty is to assume that the economy will remain as it is, maybe altering it for known occurrences that will last into the next year [7]–[9].

### **Calculating the ROI Goal**

A crucial step in the process is figuring out what the organization considers an acceptable return on investment. The target ROI could be the outcome of complex mathematical modeling, or, on the other extreme, it might just be a continuation of what has previously worked. For this ROI aim, we'll use the term hurdle rate. It might be quite deceptive to use both the terms hurdle rate and cost of capital. The ROI aim should take into account:

1. the current and prospective costs of obtaining loan and equity capital
2. The anticipated risk and the company's tolerance for it
3. Alternative uses for the money, include paying off debt and dividends
4. The corporation has to increase profitability if it wants to achieve its long-term objectives.
5. Supplemental Financial Data
6. financing the enterprise

A great company strategy is borrowing money. It aids the business with accelerating its growth, funding seasonal lulls, and making investments in prospects that will secure its future. However, although the right finance strategy will assist these goals, the incorrect financing approach will increase the risk of failure for what would otherwise be good business projects.

Our global economy and business are quite dynamic. They are perpetually evolving, and the rules are often changed. Consequently, finance plans must also be flexible. What was suitable for the business six months ago may suddenly be very undesirable. Because of this, the company's finance strategy has to be continually reviewed, just like most other elements of the organization need.

The management team members in charge of operations, marketing, human resources, and technology do not directly oversee the company's interactions with the financial community, though in a smaller business they might take part in this process when a significant project is involved. All top executives of publicly traded firms will be required to respond to inquiries from investors and the financial community.

The presence, kind, and volume of funding that the firm is able to get will eventually have an impact on every significant initiative the company undertakes. Due to increasing funding, budgets are increased and personnel are employed. When financing cannot be acquired or the conditions are onerous, budgets and employee numbers are decreased.

Every businessperson has a significant stake in finance and financial strategy, hence it is covered in this book. The primary concerns with finance are:

1. Maturity
2. Cost
3. stipulations and limitations
4. Schedule for payments
5. Collateral

### **Debt and equity are the two types of finance available**

**Debt** A corporation that borrows money to fund its operations may do so on a short-term or long-term basis. Loans having a one-year or less duration are considered short-term loans. It is used to meet urgent financial requirements, including funding business expansion, seasonal cash flow requirements, and large client purchases. Because they finance working capital, loans in this category are often referred to as such.

Loans with a lengthy duration have maturities that are longer than a year. Companies use long-term borrowing to fund significant capital expansions, longer-term research and development initiatives, and real estate [10].

### **Debt of the moment**

Both short-term and long-term debt come in a variety of forms, along with a number of associated components. We start with those pertaining to recent debt:

1. Financing for accounts receivable
2. Factoring

3. Finance for inventory
4. Floor preparation
5. Rotating credit
6. Accounts with a zero balance
7. Lines of Credit
8. Charge cards
9. Making up balances

Finance for Accounts Receivable. This is a great kind of short-term financing that aids in the management of the company's cash flow. It entails utilizing a portion or the whole of the company's accounts receivable as security for quick loans. If any of the invoices are more than 90 days old or if some of the clients have poor credit, the collateral could simply consist of a few individual invoices. The bank is preventing itself from lending against the receivables of clients with poor credit ratings by refusing to lend against these invoices. At the same time, it offers the business some wise counsel on how to deal with these clients.

With accounts receivable financing, the business is still responsible for collecting from its customers even when there is a credit risk involved. Schedules for repayment for this kind of borrowing are quite negotiable. The business should make sure that the repayment conditions do not include any unfavorable inflexibilities. There are many "gray areas" between bank-imposed restrictions and financial restraint. The standard practice among banks and other lenders is to establish a line of credit that is between 70 and 90 percent of the eligible accounts receivable. Factoring. In this option to financing, the business actually sells its qualifying accounts receivable at a loss to a bank or a separate factoring firm. For its bills, the company obtains quick payment. Customers will be instructed to pay the bank or factoring provider directly on the bills. Compared to other kinds of funding, this one is costlier. Additionally, it might cause clients to misinterpret the company's financial situation and assume that it is experiencing problems. The factor may be permitted to initiate contact with past-due customers directly.

The monthly cost of factoring might range from 2 to 5 percent. If the borrower operates a low-margin firm, this might severely reduce profitability. However, factoring can be a preferable choice if the conditions of the transaction are now 2/10, n/30. Selling under terms of 2/10, n/30 indicates that payments must be made within 30 days of the invoice date and that the client may get a 2 percent discount off the invoice amount if the invoice is paid within 10 days of the invoice date. Customers will either accept the 2 percent discount or postpone payment for up to 30 days under these conditions. This is an appealing option if factoring costs 2 percent and the firm can get its cash right away.

It is possible to sell receivables to a factor with or without recourse. The buyer of the accounts receivable carries the whole credit risk if the transaction is made without recourse. The factor loses the money if the consumer doesn't pay. If the transaction has recourse, the business will be ultimately liable for any credit losses if the buyer defaults. Selling without training costs a lot of money. There is seldom ever a credit loss since this kind of financing is only available for extremely high-quality receivables. Selling without recourse is thus seldom beneficial. In fact, businesses may get credit insurance to safeguard them against credit loss.

**Financing for inventory.** Typically, only inventory of completed items and raw materials qualifies as collateral. The market for work in progress does not exist. Lenders often provide credit in the amount of 50% of the qualifying collateral. For example, in a seasonal firm, this is an excellent kind of financing to cover a time of high cash demands that will be followed by a period of high cash inflows. It may also be used to cover the expense of satisfying a very big order from a high-quality client. It takes highly advanced inventory management techniques, including system assistance, to use inventory as collateral. The organization should already have self-discipline, but this requires it.

**Floor preparation.** In the retail sale of particularly expensive goods like yachts, vehicles, and appliances, floor planning is a unique kind of inventory financing that is often used. The seller and its goods must both be credit-qualified for this kind of financing. The lender effectively lends the goods to the retailer by purchasing them from the producer and putting them in the shop and supporting warehouse.

**The goods remain in the lender's ownership.** When a product is sold at retail, the retailer must first make a payment to the lender in order to get ownership to the item, which it may then transfer to the consumer making the

purchase. The seller may only get the difference between the selling price and the loan amount in a simultaneous transaction like this.

A manufacturer-owned financing firm often provides floor planning. Various "bargains" will be offered by the manufacturer and its affiliated lending business to persuade the store to stock up on too much inventory. This streamlines the production process and loads up the dealer's showroom with merchandise, which should boost sales. As a solution for the manufacturer to deal with surplus inventory, slow-moving merchandise is sometimes given to the dealer at no financing cost.

Consider counting the number of vehicles on a dealer's lot, estimating their worth, and multiplying that by one percent every month as a business lesson. It may very well be less than 1% every month, but it's still a simpler calculation in the head. You may estimate how many vehicles a dealer has to sell each month in order to pay for its floor plan interest costs.

### **Continual Credit**

This loan is essentially a working capital loan with inventory and accounts receivable as security. Based on a formula linked to high-quality inventories and accounts receivable, the loan's maximum amount is determined. The maximum percentage can be, for instance, 75% of accounts receivable with a maturity of fewer than 60 days and 50% of inventories with completed products and raw materials with a maturity of less than 60 days. When the inventory is used up and the receivables are collected, the formula pushes the business to make recurring payments and lower the balance owed.

It would be very risky for a business to employ this kind of finance to support long-term initiatives because to the pressure to repay and the regular monitoring of working capital. "Cleanup" periods are necessary according to certain banks. The loan amount must be zero for a certain length of time, maybe one month every year.

### **Zero-Balance Accounts**

Another loan arrangement may very well need this kind of account. In a "normal" loan, the borrower receives money from consumers, puts it in the corporate checking account, and then sends some kind of payment to the lender for the loan's principle and interest. The loan and the checking account are linked via a zero-balance feature. Payments from customers are automatically applied to the loan amount and accrued interest as they are put into the checking account. The corporation makes checks, which raise the loan amount since the account balance is thus zero.

Conceptually, this function is quite similar to the overdraft rights associated with individual checking accounts. Due to the fact that the float is lowered to zero, this feature may be highly advantageous to the business. The loan debt is automatically reduced by customer payments. Because the bank is certain that the loan will be repaid when the business gets payments from its clients, the interest rate may also be advantageous. Additionally, the business only loans the precise amount needed.

**Credit lines.** Although a line of credit is a highly advantageous way to get a loan, it is not a loan. The adage "borrow when you don't need it so that you will have it when you do" perfectly sums up this arrangement.

Let's say a business is thinking about expanding or making a significant investment that will happen during the next six months. The company's financial sheet is healthy, and it doesn't really need the loan now, or at least not right away. The business may visit the bank to make arrangements for a line of credit. This advance reservation makes money accessible, but it should only be spent if and when it is really necessary.

One benefit of a line of credit is that:

1. The borrower chooses the time for the loan arrangement.
2. The money is there; the borrower has the option of using it or not.
3. Because of this and maybe more financing alternatives, the corporation is in a position to commit to large purchases.
4. It gives you a lot of negotiating leverage when negotiating the price.
5. Once the money is actually spent, interest starts to accrue.

A reservation charge, which will most likely amount to around 1% of the total line, will be paid by the firm. The same as with any other loan, there will be negotiated payment periods, interest rates, additional fees, and collateral requirements. Similar to a homeowner's equity line of credit in concept.

**Cards of credit.** Customers are placing an increasing number of purchases online or over the phone. Giving the client the option to pay with a credit card achieves many goals:

1. It gets rid of the paperwork and waiting for the money that comes with accounts receivable.
2. It is not necessary to assess the creditworthiness of the consumer.
3. There won't be any unpaid accounts receivable.
4. The consumers are free to take as much time as they like.

Waiting for client payments and making the often-unnecessary phone calls to collect might result in the loss of revenues for smaller transactions. Accepting credit cards will increase profits for small businesses even if the firm must pay the credit card processing charge, which is around 2%. This payment method was often rejected. People and businesses are becoming increasingly used to automated payment methods as a result of the proliferation of debit cards, point-of-sale payment systems connected to smartphones, PayPal, and other Internet mechanisms. By doing this, credit risk is transferred from the selling firm to the credit company, which is often better equipped to assess credit riskiness. Additionally, it reduces—if not completely eliminates—expensive invoicing, bad debts, and waiting for payment.

**Equipping Balances.** A bank tactic that raises the actual cost of borrowing money without raising the apparent interest rate is the need for compensatory balances. An obligation to maintain a minimum balance in the checking account at all times is known as a compensating balance.

If a business takes out a \$1,000,000 loan for a year at a rate of 10%, the interest rate is plainly 10%. However, if a compensatory balance of 10% is necessary, the borrower's actual usage is only \$900,000. An effective rate of roughly 11% is the consequence. The borrower will need to borrow around \$1.1 million if it really needs \$1.0 million. Compensating balances are a cost of borrowing and may be negotiated, much like loan origination costs, collateral audit fees, search fees, and other similar expenses.

### **Contingent Debt**

The forms of long-term debt discussed here include:

1. Term debt
2. Bonds
3. Debentures
4. Home loan bonds
5. Bonds that convert
6. Senior Debt
7. Lower-level debt
8. Subpar bonds

Loans with a set term. Businesses most typically employ this kind of long-term financing. It is a loan given by a bank to a business in order to fund its growth plans. It has a set maturity date that is typically five to seven years after the loan's origination date. The loan will be repaid by the business in interest and principal payments made each month. Loan amortization is the process of paying down the principle over the course of the loan. Debt service refers to the principal and interest payments made each month. The principal may also be amortized over a time frame that is longer than the loan term. The remaining principal under this arrangement is payable at the conclusion of the loan term. A balloon payment is what's known as the final balance. Bonds. Many properties of a bond are comparable to those of a term loan.

### **III. CONCLUSION**

In conclusion, Data quality, sui forecasting methods, validation and monitoring, transparency, and flexibility are examples of qualities that an excellent forecast demonstrates. These traits support the predictability and precision of the results, facilitating defensible choices and efficient planning. In business, finance, economics, and other fields, good projections have a broad range of uses and are essential for directing activities and reducing risks. In many different industries, accurate projections are quite advantageous. They support risk management, demand forecasting, resource allocation, and strategic planning in business. Quality projections influence monetary policy,

investment choices, and economic planning in finance and economics. Accurate and fast weather predictions aid in planning for disaster preparation, agriculture, and transportation.

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