Scenario planning: A tool for uncertain times

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What is scenario planning?

Scenario planning provides real-time forecasting for businesses. A scenario-planning model integrates cash-flow forecasting with business forecasting to help leaders envision different future outcomes for their business. It helps leaders make strategic decisions in the short term — typically in the span of 14, 30, 60 or 90 days.

“This isn’t a quarterly or annual strategic-planning process,” says Crawford. “It’s for real time, right now. So, as your business shifts from one scenario to the next, you will have already thought through and modeled out what you need to do. For example, if you need to quickly reduce cash outflows you will know what to do and where – e.g., implement a hiring freeze, defer operating expenses, freeze spending, cut wages, make layoffs or cut your own pay. This modeling process will help you consider all those factors in advance to solve for the scenario outcome you’ve defined.”

Why is scenario planning valuable for leaders in a crisis like COVID-19?

Scenario planning can help leaders gain clarity on decision-making when they’re operating in an uncertain and rapidly changing environment, like today. More specifically, scenario planning helps leaders anticipate scenarios that could happen before they happen (e.g., sales decline by 20% in one month) and then plan for the decisions they need to make (e.g., furlough 30% of employees) if any scenario does, in fact, happen.

“Going through the scenario-planning process removes the stress and removes the confusion around what you need to do,” explains Crawford. “It creates a clearly defined path, and it gives you a platform for identifying strategic priorities and taking action on them now.”

What’s the difference between forecasting and scenario planning?

Forecasting takes what you know today about your business and makes a single prediction about your business for the future. Typically, this future state is not radically different from a past state.

Scenario planning starts with historical information about your cashflow. But, unlike forecasting, it takes uncertainty into consideration to predict the future state of your business. Rather than running a single scenario, it runs several different scenarios — typically three or more — based on different assumptions.

How do you build a scenario-planning model?

At a high level, a scenario-planning model looks like a one-page accounting spreadsheet that uses cash flow concepts from both a P&L and a balance sheet.

To build it, start by gathering historical information about your incoming cash and outgoing cash, focusing on the most important variables that impact your revenue and costs.

Then, run three different scenarios for the future based on different assumptions.

- For Scenario #1, you might assume that your incoming cash and outgoing cash will stay the same as in the recent past.
- For Scenario #2, you might assume that your incoming cash will decline by 20%.
- For Scenario #3, you might assume that your incoming cash will decline by 40%. (View the webinar for a more detailed breakdown of how this works.)

Once you've created these three scenarios, you can start to explore what levers you need to pull to adjust costs or outgoing cash in order to achieve a desired outcome for the business. For example, if your desired outcome is just to break even, you might want to look at postponing rent payments, laying off staff or reducing salaries.

What other steps are needed to apply a scenario-planning model?

You also need to consider your strategic priorities for the short term. We recommend using a four-step method to gain clarity on these priorities:

1. **Decide what's most important:** Decide what you want your organization to look like at a particular end state. For example, given the COVID-19 crisis, your business goal may be just to avoid increasing debt for the next three months. When setting these priorities, take into consideration what could go wrong and/or what variables are out of your control (e.g., legislative changes that might take place). Also consider the variables that are under your control and/or what levers you could pull in the next two, four or eight weeks.
2. **Establish objectives and key results:** Once you've set your objectives, break them down into tasks. Figure out who needs to do what by when, and be as precise as possible to avoid confusion.

3. **Communicate the strategy:** Let everyone know in the organization what you're aiming for and give them the opportunity to align with those goals. "I love the quote from Samuel Jackson, 'People need to be reminded more than they need to be instructed,'" says Michie. "So, once you set your company objectives, just keep saying the same thing. Become the Chief Reminding Officer."
4. **Hold people accountable to results:** To build this accountability, establish meeting rhythms and make every effort to talk to your people more often, whether via phone, Zoom, Microsoft Teams or another platform. "This is where the rubber meets the road," Michie says.

The overarching goal for leaders is two-fold: It's to ask yourself what could go wrong so you can find ways to mitigate risk. And it's to ask yourself what's under your control so you know what levers to pull and when. In a time of crisis, taking those steps can make all the difference.