how rolling forecasting facilitates dynamic, agile planning

An alternative to the annual budgeting process allows hospitals and health systems to make more accurate operating projections and be agile in responding to changes.

In today’s rapidly evolving healthcare environment, provider organizations must be able to identify financial performance gaps continuously and quickly “course correct” with operating changes that align with their long-range plans. The need for a nimble response is further evidenced by the increased interest of investors and rating agencies in seeing these organizations display a more dynamic financial planning process.

Many healthcare organizations are turning to rolling forecasting to provide that flexibility. Rolling forecasting is a quarterly process that enables an organization to keep a close eye on its financial trajectory, looking in a systemic, structured way beyond the current fiscal year covered by an annual budget. It compares historical trends, current operating conditions, and future planning assumptions, enabling leaders to gauge their organization’s performance against long-term goals. This method fosters meaningful feedback and connectivity between finance and operations, which can result in improved organizational performance.

Some organizations are using rolling forecasting instead of an annual budget process, while others are using it to supplement their annual budget and extend the planning horizon. Regardless of how it is applied, effective rolling forecasting as an integral part of overall financial management provides an important means for organizations to:

- Drive organizational change to improve efficiencies
- Reduce waste, both in time and resources
- Support continuous performance improvement
- Allow for more agility under rapidly changing market conditions
- Provide for more current and dynamic forecasting

How Rolling Forecasting Works

The rolling forecast builds on an organization’s strategic financial plan. A strategic financial plan projects the organization’s desired financial course.
out five to 10 years, providing assumptions and targets related to volume, inflation, and productivity improvement. It serves as a macro-level financial planning tool for healthcare leaders as they make capital allocation decisions, develop operating margin targets, and evaluate risks and strategies over time.

The future assumptions and targets used in the strategic financial plan are the same as those used in the traditional annual budget. For example, volume assumptions may include metrics on patient days, discharges, admissions, or physician and ambulatory visits. Inflationary assumptions may include measures such as price increases, reimbursement changes, or expense inflation.

The rolling forecast typically focuses on the first three years (12 quarters) of such projections, comparing the strategic financial plan assumptions with the organization’s expected trajectory, given current conditions and historical relationships. This approach allows leaders to identify and respond to gaps between the plan and the forecast on an ongoing or rolling basis, as shown in the exhibit below.

Instead of itemizing by individual departments or units, as is done in an annual budget, the rolling forecast focuses on higher-level “forecast groups”—that is, groupings of functional departments that define a service. For example, the “surgical services group” might combine surgery, anesthesia, and recovery—all of which serve the same patient population.

Department leaders in each forecast group work together to identify the key volume indicator that should be used as the basis for the key performance indicators (KPIs) by which their combined operations will be measured. Examples of KPIs include total cost per unit, revenue per unit, or hours per unit.

Once the initial rolling forecast is in place, monthly KPI monitoring can be performed at a department, division, or forecast group level. The results then can be compared with other findings, including results for the previous month and the same month in the previous year, and averages over three months, six months, and year to date.

Rolling forecasting is not an “off the shelf,” one-size-fits-all solution. The process must be tailored to meet each organization’s unique needs. Identifying forecast groups and selecting the most appropriate KPIs are critical, organization-specific steps, because they will serve as the basis for planning and tracking performance over time.
A rolling forecast neither reflects an annual budget level of detail nor is meant to be a quarterly budget process. Implementation of rolling forecasting requires flexible software and tools that can adapt to changes in planning and monitoring requirements, and overall healthcare changes.

**Improving Organizational Performance: Winona Health**

Winona Health, a 100-bed community hospital in Winona, Minn., with post-acute facilities including a nursing home and two assisted living communities, stopped developing an annual budget in 2011. The system now uses rolling forecasting as its primary financial management tool. The change, which was driven by Winona Health’s executive leadership and board, stemmed from a belief that the annual budget process was out of sync with the pace of change in the industry, wasted resources and time, and did not provide the agility needed for real continuous performance improvement. A 17-month lead time meant the actual budget quickly became stale.

Winona Health recently completed its first fiscal year using only rolling forecasting, thereby achieving a better balance between control and agility and committing finite resources to one process rather than two. With strong controls in place to monitor the system’s financial activities, the organization focuses on performance at the service line level. Service line leaders are responsible for holding department directors accountable for achieving targeted KPIs.

Rolling forecasting aligns with the system’s Lean management system and allows the organization to build performance improvement efforts into the forecast. It reduces the cycle time for decision making and enables leaders to identify problems early.

The use of rolling forecasting is an ongoing, top-down learning process. A quarterly forecasting meeting fosters important new dialogue among senior leaders. Preparation for the meetings has had the added benefit of triggering more meaningful interaction between finance and operations.

**Extending the Planning Horizon: Inova Health System**

Inova Health System, a five-hospital health system based in Falls Church, Va., began using rolling forecasting in August 2012. System leaders believed the traditional annual budget didn’t support the organization’s five-year financial plan. Increasing competition was difficult to predict, and the annual budget couldn’t keep up with the system’s business expansion strategies, such as the addition of physician practices, a joint venture with an insurer, and the purchase of a Medicaid HMO.

Inova Health needed a process to keep it on track in a business environment with a higher degree of volatility, allowing for adequate cash flow and liquidity to support new capital expenditures. Leaders wanted more flexibility to respond to market changes and pursue major initiatives such as the conversion to electronic health records and investments in translational genomic medicine.

On the broader scale of healthcare reform, Inova Health leaders also wanted the ability to adjust financial targets as they gained more information on changes in payments, payer mix, and the 2014 implementation of Medicaid expansion and health insurance exchanges.

Separate forecast groups were set up for major organizational initiatives, such as risk contracting and population health management, as part of the implementation of rolling forecasting. Inova Health still has an annual budget, but not to the level of detail that it maintained in the past.

The health system continues to provide productivity and cost targets at the department level, but integrates the higher-level rolling forecasts into its five-year financial plan. The five-year plan includes current-year forecasts and targets for incentive compensation and performance evaluation purposes. Inova Health also must meet certain reporting requirements to the county government and to Inova’s Board of Trustees. That information in the five-year financial plan is
provided in sufficient detail to meet those requirements without having to do a detailed annual budget.

**Streamlining the Financial Management Process: PinnacleHealth**

PinnacleHealth is a multihospital health system in central Pennsylvania that began its implementation of rolling forecasting in early 2013. The system is eliminating its annual budget process starting with FY14 and plans to use its five-year financial plan, supplemented by rolling forecasting, to track organizational performance.

The change is being driven by multiple factors. PinnacleHealth leaders wanted to increase efficiency. They found the previous operating budget became quickly outdated, and managers spent too much time trying to determine why actual financials didn’t match budget projections. In developing forecast groups for the rolling forecast, PinnacleHealth reduced more than 500 cost centers to 40 forecast groups based on organizational structure.

Organizational leaders anticipate the new process will allow them to better respond to changes, particularly with ongoing capital projects such as the scheduled opening of a new hospital in 2014. Rolling forecasting allows them to consider funding requirements on a quarterly basis, as needed.

New reports based on benchmark data and trends in key metrics are replacing the actual-to-budget comparisons previously used. This new approach requires ongoing communication between department managers and leadership. Accountability is based on actual performance in each forecast group, with an emphasis on showing quarter-over-quarter KPI improvements.

**Advancing Operations in the Post-Reform Environment**

The goal of rolling forecasting is to enable an organization’s leaders to drive continuous improvement by using period-over-period measurement of changes in KPIs to ensure that the organization’s financial trajectory aligns with long-term goals. The potential benefits of this financial tool are many. Rolling forecasting allows organizations to extend the planning horizon and streamline financial management. The process provides a platform for continuous planning and assessment, and allows organizations to be nimble in responding to changes.

Rolling forecasting is not about creating numbers as targets; rather, it is about performance improvement and advancing operations in the post-reform environment. It is an evolving, adaptable process, and implementing it requires flexible forecasting tools and leaders prepared to position their organizations for continued successful performance in a dynamic healthcare environment.

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