Listen to two MBA students discussing that morning's lecture on types of financial forecasting and their uses.

Optional exercise Listen to the conversation and match the halves of the sentence to summarise the points made.

1	Financial forecasting can be categorised	A	caused by a change in a particular variable.
2	Businesses use qualitative forecasting to	B	into three main types.
3	Managers are sometimes reluctant to	C	of a business over a period of time.
4	A time series monitors a particular strand	D	share estimates that are extreme.
5	Time series forecasts are useful	E	supplement their quantitative forecasting.
6	Causal forecasts examine changes that are	F	when variables are constant.

A: Hi Barbara, did you go to the lecture this morning – about financial forecasting?

B: Hi Alan. Yes, I've just come from there.

A: Oh great. Do you think you could tell me what I missed? Over a coffee?

B: Sure. Let's sit here. I'll just get my notes out.

A: Thanks Barbara. You don't mind, do you?

B: Not at all – it will help me to remember too. Ok. Let's see – yes. Financial forecasting. The types.

A: There are three types, aren't there?

B: Yes. The qualitative – that's sometimes called the judgemental forecast, the time series forecast and the causal forecast. I'll tell you about each one in turn.

A: You took a lot of notes, didn't you?

B: Yes. I always do. Anyway, let's get started. Qualitative forecasting. Years ago businesses used to rely heavily on quantitative forecasting but recently that's changed. These days companies make decisions based on forecasts that depend on somebody's judgement or experience.

A: But they do use statistics too, don't they?

B: Yes. Afterwards. To supplement the findings. The main problem with this type of forecasting is that managers don't like to share their views when their views are extreme.

A: What do you mean?

B: Well, if a manager sees future sales as being unusually low or unusually high he tends to moderate his estimates. Especially when there are a group of managers all giving their forecasts – and when the rest of the group's estimates are less extreme.

A: Yes. That makes sense.

B: Let's move on to the time series forecasts.

A: That's the second type, isn't it?

B: Yes. A time series is the monitoring of a particular strand of a business over a period of time.

A: I'm not sure I understand.

B: Well, for example when one employee's annual salary is tracked over the last ten years and a prediction is made from that. Time series forecasts are useful when variables are more constant. When there are changes but when the changes are regular – or seasonal. Do you know what I mean?

B: Yes. Thanks. And the third type of forecasting was "causal forecasting" wasn't it?

A: Yes, that's right. In a time series forecast the analyst doesn't identify the specific factors that cause the movement of a variable over time. He isn't really interested in the reasons – or the causes. But, when he uses a causal forecast that is *exactly* what he does.

B: So causal forecasts analyse the causes that bring about changes in a variable?

A: Yes! Ideally causal forecasts are used when the causal variables are easy to predict. Imagine a company sells baby clothes. And imagine they want to make a ten year sales forecast. They need to have an idea of how many babies will be born over the next ten years. This information can be forecast quite accurately in the UK. Censuses are regular and accurate and, more importantly, the causes of variables are reasonably easy to identify.

A: Ok. I'm with you.

B: Why don't you explain the three types of forecasting to me now – just to check you've understood.

A: Like a test?

B: Yeah … come on …

Answers: 1 B, 2 E, 3 D, 4 C, 5 F, 6 A