

## **Best Practices in Financial Modelling**

A financial model is a tool that helps businesses forecast their financial future. Financial models are normally built into spreadsheet software, such as Excel or Google Sheets. Be it an abstract spreadsheet or a real-world application, financial models have become an inextricable part of business growth and an indispensable part of every company's strategic roadmap.

Financial models are typically structured around the three financial statements of accounting—namely: income statement, balance sheet, and cash flow statement. Although each business may have its own suitable financial modeling practices, there are a few industry guidelines that are generally followed and common for all financial models.

### **Why Best Practices?**

1. A successful financial model needs a vision and a goal throughout the model's building process. A robust model contains three core building blocks: inputs, processing, and outputs. It is important to note that the inputs must be clearly separated from the processing and outputs of a financial model. This also helps when conducting a sensitivity analysis or budgeting for the future.
2. Users need to be able to distinguish between areas that need manual intervention and areas where the excel does the calculations. Therefore gathering all your assumptions in one place can also help minimize a large number of errors.
3. Financial modelling works off of assumptions. Along with good assumptions, a key to accurate modelling is the data you use to carry out the calculations. The model is only as good as your input.
4. End users aren't very keen on going through a whole lot of guidelines before they start using the model. They'd prefer being able to intuitively use it with minimum assistance or explanation. The more elegant your formulas are and the more accurate your data is, the more effective your model can be.

In general these best practice guidelines outlined above are aspects that are followed by some of the leading investment banking firms and professional organizations. These points are predominantly for the purposes of reducing error and bringing increased robustness and clarity to the model.