Demand Forecasting - I

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Demand Forecasting

- **Definition**
- According to Evan J. Douglas, “Demand estimation (forecasting) may be defined as a process of finding values for demand in future time periods.”
- In the words of Cundiff and Still, “Demand forecasting is an estimate of sales during a specified future period based on proposed marketing plan and a set of particular uncontrollable and competitive forces

Demand Forecasting

- Demand forecasting enables an organization to take various business decisions, such as planning the production process, purchasing raw materials, managing funds, and deciding the price of the product.

- An organization can forecast demand by making own estimates called guess estimate or taking the help of specialized consultants or market research agencies.

Demand Forecasting

The significance of demand forecasting

i. Fulfilling objectives:

Implies that every business unit starts with certain pre-decided objectives. Demand forecasting helps in fulfilling pre decided objectives. An organization estimates the current demand for its products and services in the market and move forward to achieve the set goals.

For example, an organization has set a target of selling 50, 000 units of its products. In such a case, if the demand for the organization’s products is low, the organization would take corrective actions, so that the set objective can be achieved.

Demand Forecasting

The significance of demand forecasting

ii. Preparing the budget:

preparing budget by estimating costs and expected revenues. For instance, an organization has forecasted that the demand for its product, which is priced at Rs. 10, would be 10, 00, 00 units. In such a case, the total expected revenue would be 10* 100000 = Rs. 10, 00, 000. In this way, demand forecasting enables organizations to prepare their budget.

iii. Stabilizing employment and production:
Producing according to the forecasted demand of products helps in avoiding the wastage of the resources of an organization. This further helps an organization to hire human resource according to requirement. For example, if an organization expects a rise in the demand for its products, it may opt for extra labor to fulfill the increased demand.

Demand Forecasting

The significance of demand forecasting

iv. Expanding organizations:

Implies that demand forecasting helps in deciding about the expansion of the business of the organization. If the expected demand for products is higher, then the organization may plan to expand further. On the other hand, if the demand for products is expected to fall, the organization may cut down the investment in the business.

v. Taking Management Decisions:

Helps in making critical decisions, such as deciding the plant capacity, determining the requirement of raw material, and ensuring the availability of labor and capital.

Demand Forecasting

objectives of demand forecasting

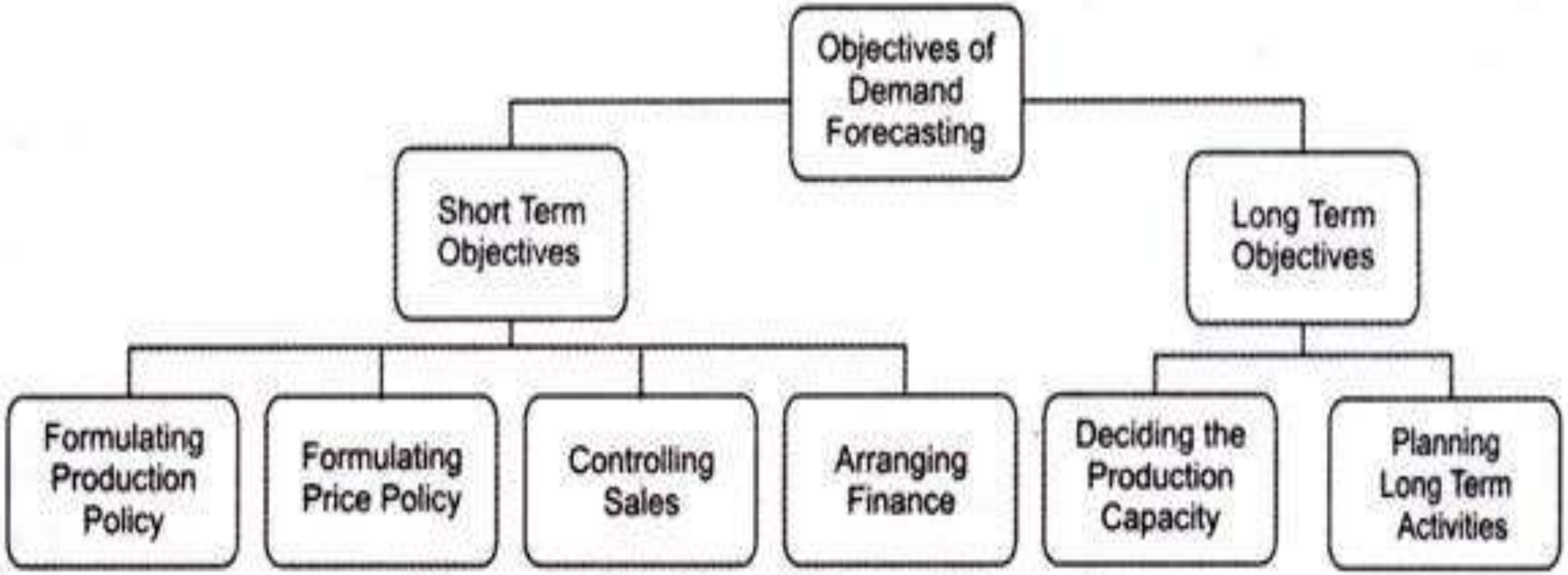

Figure-1: Objectives of Demand Forecasting

Demand Forecasting

i. Short-term Objectives:

Include the following:

a. Formulating production policy:
Helps in covering the gap between the demand and supply of the product. The demand forecasting helps in estimating the requirement of raw material in future, so that the regular supply of raw material can be maintained. It further helps in maximum utilization of resources as operations are planned according to forecasts.

b. Formulating price policy:
Refers to one of the most important objectives of demand forecasting. An organization sets prices of its products according to their demand. For example, if an economy enters into depression or recession phase, the demand for products falls. In such a case, the organization sets low prices of its products.

Demand Forecasting

i. Short-term Objectives:

Include the following:

c. Controlling sales:

Helps in setting sales targets, which act as a basis for evaluating sales performance. An organization make demand forecasts for different regions and fix sales targets for each region accordingly.

d. Arranging finance:

Implies that the financial requirements of the enterprise are estimated with the help of demand forecasting. This helps in ensuring proper liquidity within the organization.

Demand Forecasting

ii. Long-term Objectives:

Include the following:

1. Deciding the production capacity:
Implies that with the help of demand forecasting, an organization can determine the size of the plant required for production. The size of the plant should conform to the sales requirement of the organization.

2. Planning long-term activities:
Implies that demand forecasting helps in planning for long term. For example, if the forecasted demand for the organization's products is high, then it may plan to invest in various expansion and development projects in the long term.

Demand Forecasting

Factors Influencing Demand Forecasting:

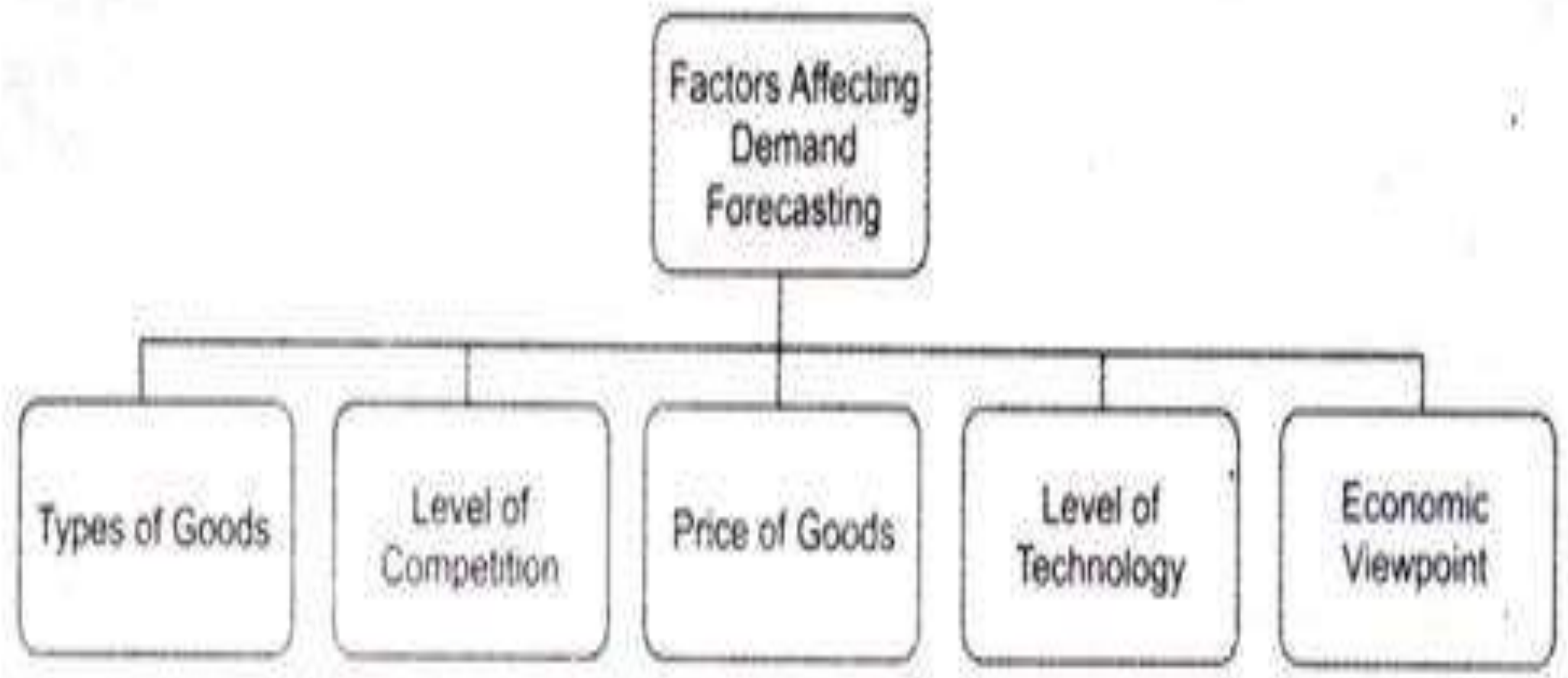

Figure-2: Factors Affecting Demand Forecasting

Demand Forecasting

1.Types of Goods:

- Affect the demand forecasting process to a larger extent. Goods can be producer's goods, consumer goods, or services. Apart from this, goods can be established and new goods. Established goods are those goods which already exist in the market, whereas new goods are those which are yet to be introduced in the market.

- Information regarding the demand, substitutes and level of competition of goods is known only in case of established goods. On the other hand, it is difficult to forecast demand for the new goods. Therefore, forecasting is different for different types of goods.

Demand Forecasting

ii. Competition Level:

Influence the process of demand forecasting. In a highly competitive market, demand for products also depend on the number of competitors existing in the market. Moreover, in a highly competitive market, there is always a risk of new entrants. In such a case, demand forecasting becomes difficult and challenging.

iii. Price of Goods:

Acts as a major factor that influences the demand forecasting process. The demand forecasts of organizations are highly affected by change in their pricing policies. In such a scenario, it is difficult to estimate the exact demand of products.

Demand Forecasting

iv. Level of Technology:

Constitutes an important factor in obtaining reliable demand forecasts. If there is a rapid change in technology, the existing technology or products may become obsolete. For example, there is a high decline in the demand of floppy disks with the introduction of compact disks (CDs) and pen drives for saving data in computer. In such a case, it is difficult to forecast demand for existing products in future.

v. Economic Viewpoint:

Play a crucial role in obtaining demand forecasts. For example, if there is a positive development in an economy, such as globalization and high level of investment, the demand forecasts of organizations would also be positive.