

## Generating cash internally in turbulent times

SINGAPORE

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Cash, or what is commonly known as 'liquidity' in a business, is the lifeblood of every company.

A business can generate profit, but without cash it may not survive long as cash is required to pay the bills. With the ongoing uncertainty in the global consumer and capital markets, ever shrinking consumer demand and the tightening of credit facilities, the total management of cash in an organisation must be a top priority.

Many small and medium enterprises (SMEs) experience the symptoms associated with poor cash management but may not recognise its signs. Examples include:

- Regular cash shortages in meeting current liabilities and servicing debt
- Little or no clarity on the short-term cash requirements
- Problems in obtaining financing for working capital
- Continuous calls for funds from subsidiaries
- No clear plans to reduce the need for financial leverage by better using internal resources
- No efficient controls over inventory, receivables and payables

Pressure has been mounting in recent months for SMEs to develop alternative financing arrangements. This is because banks have become increasingly risk-adverse when lending to SMEs owing to the higher perceived risks and lack of transparency. This has resulted in many SMEs grappling with a cash-crunch type situation impeding their ability to fund acquisitions, finance

further growth or simply ensure they have sufficient funds to meet operational requirements in order to continue as a going concern.

One such alternative involves looking inward at the availability of internal resources. Efforts are directed towards minimising the time during which working capital is tied up in the company. The ability to free cash and increase liquidity has a direct impact on the company's financial position.

Internal financing through efficient cash management aimed at reducing the amount of capital locked up within a company is by no means a new principle.

Unfortunately, objectives involving optimising working capital have often been relegated as priority to other corporate objectives and strategic financial measures such as earnings, sales and capital expenditure.

Historically, many businesses were rewarded for growing their top lines and increasing profits, even if these increased profits eroded their businesses' liquidity.

However, with banks reeling in their credit lines and stakeholders putting increasing pressure on businesses to generate more cash, many businesses are going back to basics and are starting to think about how to manage

their operations with a view to improve liquidity.

Besides enhancing liquidity, a well-planned cash management strategy may also lead to the strengthening of the underlying business and improve the visibility and reliability of decision making information. Furthermore, the ability of a business to convince its financiers that it has a strong 'cash culture' as part of its management philosophy could also go a long way to helping organisations secure lending at more competitive rates.

In times of crisis, total cash management may also serve businesses by helping to minimise the need for unanticipated injection of fresh funds into the business and also help reduce the likelihood of default on existing debt obligations.

To many SMEs, cash management simply entails managing one's receivable and payables, stretching payment to creditors and making additional effort at debt collection. This is especially prevalent near festive seasons.

Unfortunately, truly sustainable cash savings cannot be achieved through an annual 'blitz' on the working capital components of debtors, stocks and creditors.

Take for instance, the example of dealing with creditors. Companies may be able to agree on preferable payment terms in the short term, but they ultimately need to address issues such as vendor rationalisation and payment procedures in order to avoid cash issues re-occurring over time.

To optimise cash management on a more permanent basis and not just at the year end, active cash management initiatives must target, and work towards optimising monetary value chains within the company. This contributes towards a significant strengthening of internal financing resources and capital efficiency.

Such initiatives should extend beyond the fundamental liquidity related activities of (1) order to cash, (2) purchase to pay, and (3) forecast to fulfill processes, which in some cases may have to be designed or re-engineered in a way which enables them to be seamlessly integrated. This helps to reduce the process throughput times and minimise duration where capital is tied up. Other areas affecting the consumption of cash such as treasury, property, fixed assets, and taxes must also be considered in tandem.

Total cash management looks beyond working capital initiatives and also explores non-working capital areas. This may involve restructuring the balance sheet and 'rightsizing' the company's operations. Balance sheet restructuring measures can involve asset sales programmes and entering into sale and leaseback arrangements to monetise long-term assets.

How can organisations get started on embarking on a total cash management process? Some of the key areas that businesses can look into can include:

- **Forecasting**  
The first and perhaps the most important step is to improve visibility and control of cash by developing a robust rolling cash forecast. This helps to provide accurate and up to date information so that businesses are able to respond quickly to changing circumstances.

Many companies have also achieved a much better understanding of how cash flows through their business daily by merely carrying out this exercise.



An effective cash management process  
(Source: KPMG International)

- **Monitoring**  
Subsequent monitoring and adjustment of the cash forecasts helps to achieve a higher level of accuracy and improves the reliability of future forecasts. By reviewing peak cash requirements, forecasting can be an efficient tool for cash management.  
  
Keeping on top of cash in this way also helps to avoid unnecessary surprises for the company, and helps a business to focus firmly on cash issues and provides early-warnings of any funding issues.
- **Disciplined control over cash flows**  
Cash flow maximisation becomes the top priority in crisis situations. Businesses should look into discovering new opportunities in this area. These include the strengthening of credit control, prioritising payments, improving procedures for billing, cash collection and purchasing. Our experience shows that these and other timely measures can produce significant effects on cash flow.
- **Further initiatives**  
After implementing the above mentioned measures, additional initiatives to increase cash flows may be analysed. Examples of medium-term opportunities include supply terms rationalisation, reduction in inventory and asset sales.

Longer-term initiatives include exiting unprofitable market segments, launching new products, changes in the pricing, reducing capital expenditures and staff cost.

Some of these measures may be painful, but they often allow a release of substantial cash through mobilising internal resources while helping a business stay within its bank facility limits and reduces borrowing requirements.

In conclusion, effective management of cash is one of the most direct ways of reducing wastage and inefficiency, optimising the availability of internal funds to meet operational requirements or investment and reducing a company's reliance on external financing.

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