



Protecting working capital: How to find cash in a time of need

March 27, 2020

The COVID-19 outbreak suddenly threatens the financial health of many companies. Authorities have told people to shelter at home. Restaurants and shops have become no-go zones. Supply chains across industries have come apart. The commercial life of the country is freezing up and normal cash flow is being interrupted.

Getting ahead of this unprecedented and rapidly evolving situation is proving extremely difficult. But companies still have time to take steps to control the damage. Companies that prepare a structured response to the cash-flow challenge stand a better chance of weathering this unprecedented disruption and emerging fit and strong when the storm passes—in weeks, months, or even several quarters of recession after the epidemic peaks. Companies in different sectors will be affected differently, but across sectors companies need to address liquidity challenges now.

Four steps to pre-empt a liquidity crunch

Efforts to contain the COVID-19 pandemic have triggered a perfect storm of demand shocks and supply-chain disruptions. The cash crunch is already threatening airlines and the travel industry, where operations have been curtailed,¹ and is rapidly spreading as the effects of plunging demand ripple across the economy.² Now, as customers delay purchases or payments because they face the same interruptions in their own cash flow, all aspects of business slow down—an escalating cycle that can wreak havoc on working capital management.

Some very large corporations—if they're in the right sectors—may have a cushion for this unprecedented storm. But most companies need to move immediately to preserve liquidity.

They can follow a structured, four-step response:



1. Establish visibility



2. Optimize cash-management processes



3. Get ahead of spending



4. Tap external sources of cash

¹ Jamie Freed, Tim Hephner, "'Single biggest shock': Aviation battles coronavirus cash crunch," Reuters, March 16, 2020.

² Stephanie Segal and Dylan Gerstel, "The Global Economic Impacts of COVID-19," Center for Strategic & International Studies, March 10, 2020.

1. Establish visibility



The first thing to do is to get a clear picture of the cash situation. This visibility allows companies to make quick decisions about where they can eliminate or stretch out cash expenditures and where they can tap sources of cash.

- Use analytics to identify the level of liquidity and cash needs, as well as identify actions that can be taken immediately to optimize short-term cash flow (e.g., determine exposures and risks from potential demand changes, prepare responses for customer cash receipts, inventory, suppliers, capital expenditures, etc.).
- Improve cash metrics and visibility into ongoing cash requirements and impacts by preparing a 13-week rolling cash flow forecast, based on receipts and payments for all business lines. Then carry out weekly analysis of cash flows to determine whether variations are due to COVID-19-related or more long-standing factors.
- The finance team should not be the sole stakeholder in cash flow management. Set up a cash “control tower” with heads of all relevant functions (treasury, production, sales, finance, etc.) to meet weekly and drive cash-preservation initiatives.
- Proactively tackle any forecasted deficiencies to head off problems as they arise.

2. Optimize cash-management processes



It is not too late to address gaps in existing commercial and cash-management processes. Most businesses are able to unlock cash from at least one or two areas through process improvements. Companies can also look for opportunities to offer special terms for valued customers to keep the cash flowing during these difficult times.

- Actively engage customers to understand what you can do for them now to keep them paying. Redeploy resources to better meet changing customer needs.
- Evaluate the risk in the customer base, and draft scenarios and risk mitigation plans
- Get invoices out in a timely manner and streamline billing processes. Analyze consumer payment behaviors and proactively align them with contractual terms.
- Manage accounts receivable with more rigor. Review invoice timing and discounting strategies. Evaluate the cost/benefit of alternative tools such as credit/payment cards to potentially speed access to cash while giving your customers flexibility.
- For organizations with factoring and securitization facilities, evaluate their impacts and options.

3. Get ahead of spending



Scour all categories of spending—accounts payable, inventory, purchases, and capital expenditures—for places to cut or stretch out payments. Triage discretionary expenses.

- Implement spending controls to review existing expenses so that unnecessary outlays can be curtailed before they arise.
- Review aging and slow-moving inventory, and consume stock on hand. Critically examine the forecast-to-fulfill cycle and modify it to meet shifting business planning requirements.
- Review purchase orders that have been issued and determine their necessity before completing them. Optimize purchases on both cost and flexibility of terms.
- Review the accounts payable process to maximize the terms (e.g., pay-cycle frequency and payment trigger upon receipt) and hold cash as long as possible.
- Maximize unique bill-to-hold arrangements to optimize payment timing.
- Draw down prepaid expenses and existing credits.

4. Tap external sources of cash



The door has already closed on some forms of financing, such as high-yield debt, but there are still opportunities to secure funding. But you want to be first in line, so the time to act is now.

- Draw down unused lines of credit, as required.
- Engage creditors and banking partners to line up their support for continued and flexible funding.
- Verify if your company qualifies for government stimulus aid.
- Asset sales can take time, but this downturn may last a while. It's a good time to divest businesses that are not core and take the cash.

Conclusion

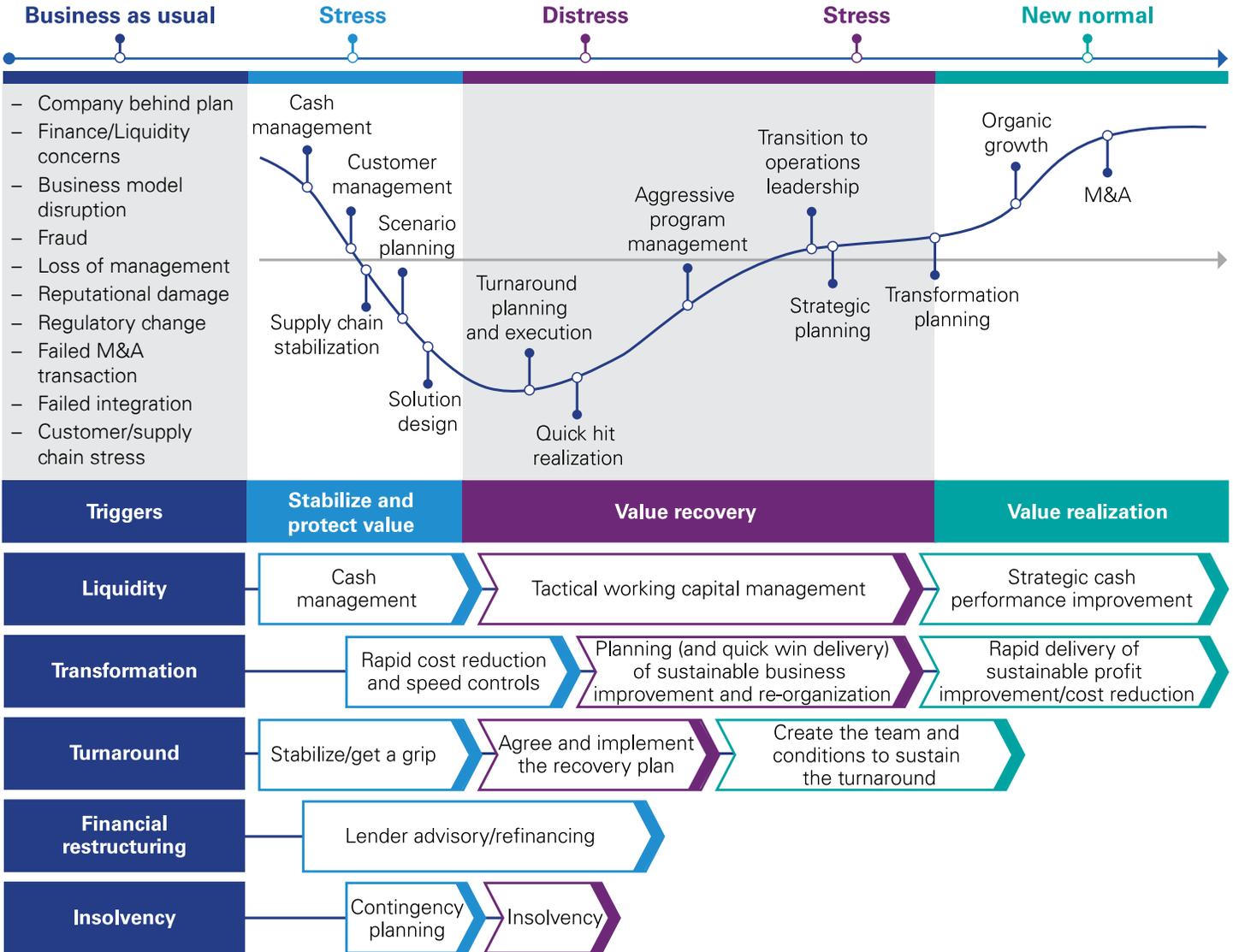
The economic disruptions from the COVID-19 outbreak are unprecedented. There is no standard playbook for companies to follow. The severity of the business impact will depend on how long the this unprecedented disruption lasts, but it seems certain that revenue for most industries will be depressed for much of 2020 and possibly longer. This situation calls for immediate action on the part of executives to plan for all contingencies. And the task begins with a fit-for-purpose working capital management strategy.

How KPMG can help

KPMG has a stress test analytics toolkit to rapidly assess a company's capital dimensions and to offer a comprehensive solution for driving cash and containing cost. Focusing on short-term cash forecasting (weekly cash forecasting), KPMG can help complete the forecasting assessment as key to liquidity management. KPMG has proven methodologies to assess and improve working capital during times of stress. This is part of our service to help clients through downturns and recoveries (*See KPMG framework for stabilization and value creation*).

KPMG framework for stabilization and value creation

At the heart of a turn-around is stabilization and value recovery. Our range of capabilities allows us to provide a comprehensive solution.



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