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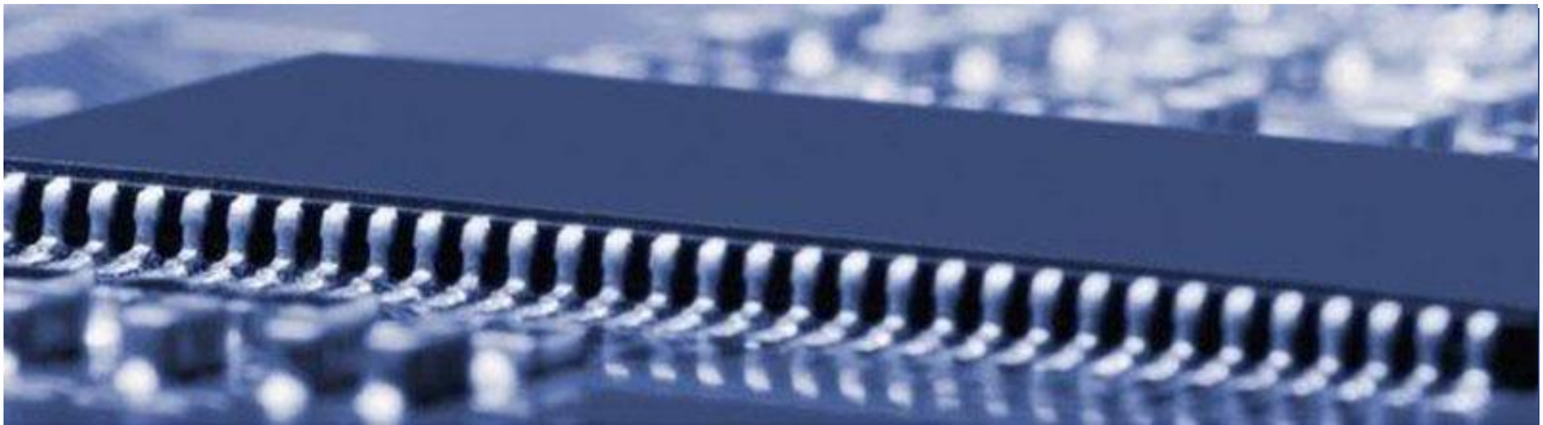
EU Payment Terms – an update

We’re nearly at the final hurdle for directive 2011/7/EU. The deadline for implementation is 16 March 2013 and so far most countries look to be transposing the directive exactly in the form suggested by the EU Commission and EU Parliament. But there have been some exceptions. For example, in the UK it has been decided that the maximum payment term for all public authorities (including healthcare) will be 30 days and the fines per invoice will start at £40 per invoice rather than the directive’s flat rate fine of €40. In Denmark, if the term is more than 30 days it must be agreed in writing. In Italy the maximum term will be 60 days on all contracts from 1 January 2013. The key point that we expected was that the directive is not retrospective, i.e. for contracts enacted before the legislation has become active the payment term can still be in excess of 60 days. So it might take a while before we see any real effects of the legislation for those suppliers that must endure excessive payment terms. One of the most surprising points is that our estimates suggest that if all of Europe’s top 800 companies had maximum receivables days of 60 and maximum payables days of 60 then the largest companies would stand to gain up to €78 billion in cash flow. That does not seem to be what was intended.



On-shoring

What are the implications for cost and working capital?

We were told that all our manufacturing would re-locate to low cost countries due to the low wage costs of these sites. If original predictions had been true the developed nations of the world would be almost entirely service economies at this point. But it hasn't happened that way. For those companies with highly automated manufacturing processes there proved to be almost no benefit in off-shoring. In fact, many companies are now starting to bring back manufacturing capability to their home markets. This is because either the perceived benefits of off-shoring have proved illusory or that the cost differential has narrowed sharply. The primary reason for off-shoring used to be labour arbitrage. But in China wage rates in industrial cities are rising at phenomenal rates. Matched with a massive property bubble and vastly increased transportation costs means that Lenovo predict that the cost of making computers in the USA versus China will be the same by 2015. Although there are many other low cost countries such as Thailand, Vietnam, Myanmar and so on, most of these countries available workforces are either too small or lack the right skills to support modern manufacturing methods. One of the bigger issues that many off-shoring manufacturers experienced was a lack of responsiveness to changes in customer demand and the necessity to produce in large quantities to achieve economies of scale causing inventory hoarding. This has been evident in the high technology sector where products like mobile phone handsets and laptops can have a very short product life. It has also affected those manufacturers with large numbers of demand volatile products in their range. With the cost differential gone or going, the impact of off-shoring can be increases in unwanted and often expensive inventory. So what should we be expecting to see in the future? Firstly, increasing the level of manufacturing automation will be seen as a much more important route to sustained unit cost reduction. We should see much more flexibility in production capacity as companies can more quickly respond to changes in market demand. And we should expect dramatic reductions in the level of finished goods inventories and the supply chain becomes considerably shorter. Will this happen for all companies. Probably not. But the world's leading companies will lead the charge and use the pace of change as a force for market advantage and increasing the value that their businesses create.

Business Intelligence Software

You can't manage what you don't measure. While there is nothing new about that phrase, there are still many companies out there that are still trying to make decisions based on intuition. The advent of ERP systems for the vast majority of companies across the world has produced a deluge of data to support business decisions, but the number of companies that use the technology effectively is still a minority. Even many of the largest and most profitable global firms do not possess these capabilities. This suggests that the opportunities for efficiencies are massive. There is even a good case to say how this kind of information could create a competitive advantage for those with the right vision.

Why consolidate when there isn't much in spend savings?

From an accounts payable perspective, anything that reduces the number of transactions that need to be physically touched can only be a good thing. But to achieve this will mean implementing solutions that eliminate or automate transaction volumes where the scope for spend saving may be very small. Most procurement functions are focused on those large areas of spend that are vital to company profitability and are often not incentivised on reducing transaction volumes. If this is the case, there is the possibility of causing frustration across the organisational silos. Accounts payable cannot reduce transaction volumes with the cooperation of procurement and the design and implementation of solutions that will have the desired effect require the time and dedication of procurement personnel. Even the simplest solutions require expert configuration by people who understand the business need and the technology involved. This is true for all the major solutions available such as EDI, purchase cards, supplier catalogues, self billing, evaluated receipts, workflow and purchase order design. The successful purchase is not only determined by the price and quality of the goods or service, but by the transactional choices available at the point of demand. All too often this point is missed with the result being larger volumes of requisitions, purchase orders and invoices that otherwise would have been required. It also has the potential for delaying payment because processes can be unnecessarily complex. So there might not be much in spend savings to be had from these solutions, but they will have the effect of improving internal efficiency and your relationships with your suppliers.

Invoice Scanning

There was a time when we all believed that invoice scanning would be the panacea to make all those paper invoices go away. Unfortunately that has proved to be a lofty expectation. There are broadly three types of scanning in play: imaging, OCR and intelligent OCR. Imaging only takes an image of the invoice for archiving and storage purposes, OCR will pick up on preformatted invoices and post them to the ledger and intelligent OCR will find certain strings (e.g. VAT numbers) and determine the key fields to complete the invoice record in your system. But even intelligent OCR will have a first time scan rate of no more than 80-85%. This is not a criticism of the technology, but just a realistic expectation of success. In that light, invoice scanning has an important plan to play in increasing the efficiency of invoice processing, but must be part of a broader transactional strategy throughout the end-to-end purchase to pay process.

Ireland: A mixed bag

What a roller coaster that Ireland has been through. The late 70's brought stagnation and crippling debt. The 80's brought unemployment and emigration. And then the Celtic Tiger arrived. People never had it so good and it was meant to go on forever. We all know that it didn't and the shock to the Irish economy has been enormous. The only solace is that Ireland has the experience of the 80's and that is helping to guide the country out of the fiscal mess. For 2013, Ireland is one of the few Euro zone countries that are not predicted to be in recession. But recovery has been patchy. Exporters of goods and services are growing at very respectable rates. There are now labour shortages in the IT sector for skilled programmers. Rates of inward investment are still quite high compared to other European countries. Ireland's largest companies are very heavily export orientated and this has cushioned many from the downturn of recent years. But Irish domestic demand is flat and it is still very difficult for small business to get funding from still recovering banks.

Demand Sensing

The end of volatile inventories?

Most text books tell us that to manage inventory levels properly that we need to have as much history of historical demand as possible, run large models to understand safety stock, lead times and batch sizes, decide on replenishment strategies and that should be it. But there are certain large industries where using all these techniques are not enough. One example of this is consumer packaged goods companies. Lead times are often very short and there is likelihood that sales are heavily influenced by promotions. For example, in the UK having beer on an end of aisle display at a promotional price can lift demand by a factor of ten. There are similar comparisons for ice cream sales on a summer's day or cough medicine in cold weather. So it becomes more likely for these companies that their best selling items have very volatile demand profiles. Many companies have tried to get around this by getting the retailer to share real-time demand data with them. This means that manufacturers can respond to sudden changes in demand much more quickly than before. Some multinationals have claimed that finished goods inventories have been reduced by up to 30% as a result, so this is clearly an effective strategy. But to make such a strategy effective requires more than access to retail data. You will need a relatively short manufacturing process and the capability to deliver produce very quickly to market. So for those with the data, the capability and the geographical footprint the benefits of such techniques are truly dramatic. For the rest of us, we will have to plough on with the demand planning techniques we already have.

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