InformitaNews

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Carillion

A total failure of risk management

The news in the UK has been full of the debacle of Carillion. There will be lots of people suggesting what went wrong and the media will land on the usual greedy bosses etc to explain what has happened. But the reality is that a litany of things have gone wrong. All this is consistent with one simple fact that has happened with the vast majority of previous major corporate collapses: Carillion went into liquidation because it ran out of cash. The construction and outsourcing market is very competitive and, as a result, margins have been falling in recent years. Carillion had been publishing profitability numbers over the years that were consistently ahead of their competitors and the markets loved it. But there were many opportunities to highlight their cash flow problems, either externally or internally, that were missed or ignored. The first point is that all their long term contracts should have had a cash flow plan attached. That would mean that if anything caused a delay in a particular contract then it should have been very easy to recalculate those cash flows and plug the problem either with additional cash or by taking management action to accelerate other projects. Carillion also got them selves into very dangerous territory when it came to their attitude to cash. They massively overextended themselves by tapping into sources of cash that were easily available. They deliberately under-funded their pension scheme for many years, they had £350 million in supply chain finance funding that was invisible to the balance sheet, their auditors and directors were either incompetent or unequipped to spot the signs of trouble. Suppliers were also very naïve. The standard payment term was 128 days. This is excessively long by any standard. Many suppliers would start work on a verbal contract only to find that the then need to get a purchase order that took 30 days to receive, adding to the 128 day term. So in the blind pursuit of greed everyone chose to ignore the obvious signals. Be aware of the risks your to business. That will be your best protection from such tragedies.

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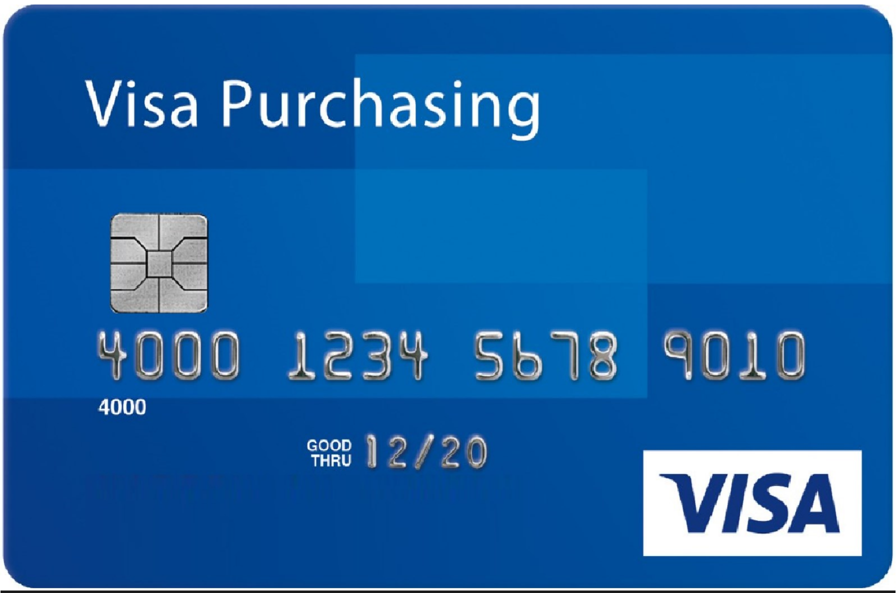

P-Cards in Europe

Still little traction

We have been getting questions in recent months from European clients that are getting curious about purchase cards. And with good reason. Many clients recognise they need an efficient and effective way to deal with small value suppliers. In North America, purchase cards continue to evolve. The quality and detail of reporting continues to improve and there are a number of purchase card providers now creating their own database of suppliers allowing smaller companies to reduce purchase cost. The advent of the virtual purchase card has also meant the potential for purchase fraud has been greatly reduced. Since the last time we looked at this subject in detail, not a huge amount has changed in Europe. There is still a problem with card acceptance in many parts of Europe. One thing that has not helped is that while merchant rates for consumers have come down to much more reasonable levels, the merchant charges for purchase cards in Europe still average about 1.5%. This discourages vendors from accepting purchase cards when there are other cheaper forms of finance. Reporting remains a problem for procurement professionals. It is still very difficult for banks to provide meaningful spend data to their clients, especially in those countries that are still unable to provide Level 3 data. The banks themselves have not been hugely helpful. There is a continuing pattern of the take up rates by suppliers is low and slow. Banks usually have limited resources to get suppliers to sign up for a purchase card scheme and they are usually dependent on the enthusiasm of the client's procurement department to gain momentum. But many procurement departments are also under-resourced and do not want resource to be focused on such low value spend where the potential for cost reductions is so low. So the result for many companies with purchase card schemes in operation is that they have not been unsuccessful, but neither have they been overwhelming successes. One South African product well worth a look is called Visa Procurement. It solves all the issues, but needs to be in Europe.

TermsCheck

2018 Update

Last year we told you that we had fully integrated the TermsCheck offering into Informita's analytical offering. After a busy year and our usual annual cull to eliminate all records more than 4 years old the net number of records has grown yet again to over 950,000. This represents a net growth rate of 12% in just one year. That reflects the continuing interest in working capital management from major corporates all around the world. We are also very grateful to all of our clients for using the service and helping to increase the size and coverage of the database. It continues to interest us how our clients are using the information. In one case a client wanted to extend terms with a major software supplier and used the data from TermsCheck as leverage to get 60 day payment terms. In another case, two businesses that were merging quite rightly wanted to move all their suppliers on to the longest term available fron the two companies. By using the TermsCheck data as well, they found the could extend more suppliers beyond what the original two companies had achieved. One of the biggest successes for us in 2017 was with a Fortune top 20 corporation who were surprised that we had matches for more than 25% of their supply base. Another surprise for us is that we have been approached by a number of consultancies who want to use TermsCheck data on behalf of their clients. So far we have had major consultancies in the UK, Germany and India use the data successfully. Of course, you can still come directly to our website (www.TermsCheck.com) to make contact and we will be very happy to help.

Blockchain

Coming to you?

We hear so much in the media about blockchain that you would think it had already happened. Companies in the international logistics space are proving to be the pioneers in this space. That should be no surprise given that without this kind of traceability data it would be very difficult to operate in the field of international shipping. And it is clear that there are potentially major benefits available to many other business sectors that operate on a global basis. With increasing pressure to ensure that the products we buy do not have supply chains infiltrated by child labour or slave labour, blockchain will become a useful tool to verify that best practices are being followed. But blockchain is not free. The early adopters are finding that implementation of blockchain technologies can be expensive and in a global market where margins are under increasing pressure that will slow down the broad uptake of blockchain technology. Another fundamental problem is that many companies are afraid to share their data. And this is an old problem. The very best technology is unlikely to change that mindset quickly. Blockchain remains a great supply chain innovation but the idea that it is going to be everywhere very quickly is a pipedream.

Iran: Ready for business?

Iran is a country with a long history but tends to hit the headlines for all the wrong reasons. But it can still be surprising how little is known about the country's economy and trading relationships. According to the United Nations Yearbook, Iran had a population of nearly 80 million people in 2016. Iran produced about 3 million barrels of oil a day but because of a large population and a huge number of people employed directly by the government or indirectly by various agencies supported by government that oil money can never make that much of a dent in peoples lives. So Iran needs to trade in order to prosper and that is where sanctions have hit so hard. There was an expectation that once sanctions were lifted that trade would increase dramatically, but that has not been the case. One of the most difficult things to do in Iran for a foreign company is to open a local bank account. There are no American banks in Iran and European banks won't operate there because of their fear of being fined by US authorities for some retrospective error. One US client did manage to open a bank account but they had to use a Japanese bank. So Iran might be technically open for business, but not ready.

Do you have the Bitcoin Blues?

Before Christmas a friend was extolling the virtues of Bitcoin and other crypto-currencies. He said that they are the future and that as a working capital firm we should be encouraging our clients to adopt this new way of working. Our view is that we are in favour of change but, like Warren Buffet, we are wary of things that are not fully understood. We are all for blockchain technology but that is not the same as Bitcoin. And for those of you that bought Bitcoin at $18,000, we hope you can sweat it out now that it has gone down to $8,000.

Cash Flow Falling

Is a downturn on its way?

A recent analysis done by SocGen suggests that the levels of net operating cash flow being generated by Americas top companies has been falling steadily, excluding oil companies and financials. Oil companies are doing well again based on the improved oil price and rising US interest rates are an opportunity for banks to increase their margins. But for other US companies things don't look quite so rosy. If the trend continues, according to SocGen, then an inverted yield curve will occur. Historically, when such an event occurs it usually predicts an economic slump. Other analysts have suggested that the US has never had an economic expansion that has lasted for more than 8-9 years continuously. Given that the current expansion has been going since 2010, it would suggest that we may be close to the end of this period of prosperity. And the most recent US GDP numbers would suggest that although things are still good, they may be starting to slow down. If such an economic disruption is about to happen, history would suggest that it is time to focus on the balance sheet. Great companies are the ones that can survive, innovate and proper during such downturns and not those that ride the positive wave in periods of expansion.

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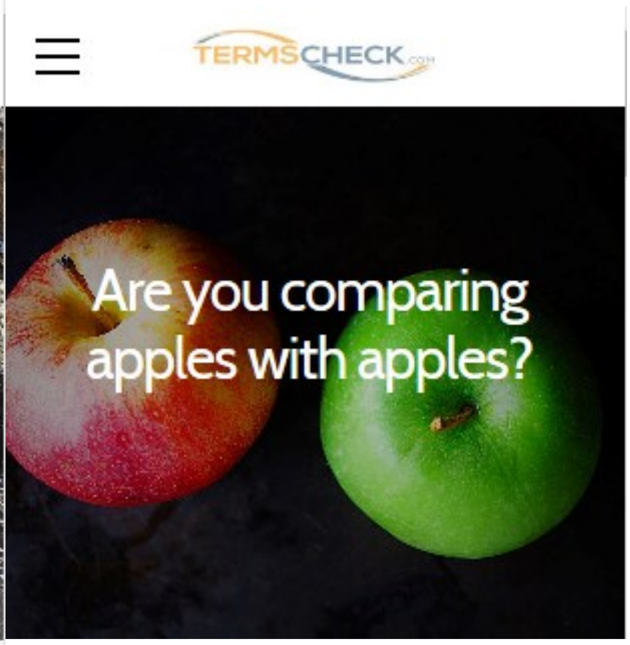

Website: www.informita.com

Twitter/Facebook: @informita

Email: brian.shanahan@informita.com
Phone: +44-7769-260-042