InformitaNews

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Feeling Lucky?

Or is your luck about to run out?

The number 8 is considered to be a very lucky number in Chinese culture. Having an apartment on the 8th floor of a building is considered very auspicious. In one case in Hong Kong, a person paid HK$ 5 million for the number 8 as their car registration plate. This edition of our newsletter also coincides with Informita's 8th year in business. Have we survived and succeeded because of luck or strategy? Everyone needs some good luck along the way, but our business model has proven successful for all those clients that we have had the privilege to help since 2012. We are very grateful for their support and look forward to many more years of helping companies improve working capital and procurement. We call 2020 the year of survival. But there are winners as well as losers. In the UK, Tesco increased sales by more that 8% as the hospitality industry went to zero. Many bricks and mortar shopping chains have gone to the wall while on-line shopping has gathered pace. Oil companies are suffering from low demand for fuel as more people work from home, while the number of Zoom users has jumped from 10 million to more than 300 million. But what will 2021 be like? Will Zoom turn out to be the latest tech unicorn as everyone goes back to the office? Will the supermarkets find that they are spending all their additional profits of extra labour cost and PPE? In short, are we seeing a short term change that will revert to the old norm or are we in the middle of setting the new norm? The answer is that nobody really knows. In the area of working capital, there has never been such a huge cash pile with major corporations across the world. And its been building steadily since the last recession. The only constant is that if you have enough cash you will always have choices. Please make good choices.

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Supply Chain Finance

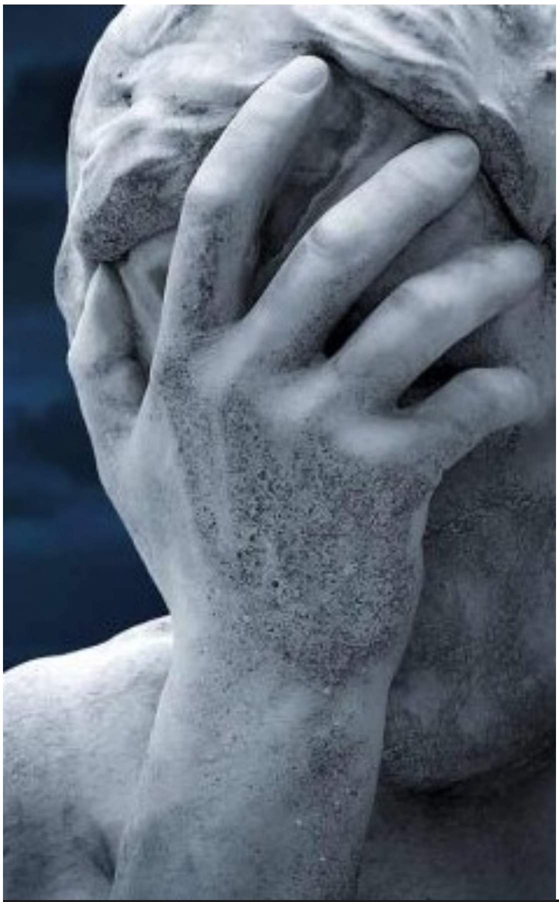
Is there a liquidity issue?

Bankers have been keen to reassure us all that there will be no bank liquidity crisis since their balance sheets are so much stronger than in 2008/9 and because the Fed and the ECB have been pumping liquidity into the market. So you would think everything is okay. On the surface, yes. But behaviours that have been observed in recent months would suggest otherwise. We know that many companies, thankfully not all, are suffering from some kind of cash flow turbulence and that many others took the opportunity back in March to draw down their bank facilities to maximise their cash holdings. That should be no surprise to anyone. But the supply chain finance market seems to be behaving weirdly. It is a fact that the demand for supply chain finance from both buyers and suppliers has rocketed in 2020. But the cost of funding to many buyers has gone up. We have even seen funders withdraw from bidding opportunities at the slightest hint of risk. In one instance in Europe where we were trying to set up a supply chain finance programme, we were advised that the only way to get cheap funding was to use funding banks from countries such as Japan where low rates of return for banks are the norm. Elsewhere we were told that many buyers are deliberately not using their house banks to fund supply chain programmes so that they don't draw down their banking facilities. All this does not suggest that everything is about to crash on the floor, but does indicate that there is a lot of nervous people in the banking community. They are probably right to be nervous about what might happen and are rightly being more risk averse than we have seen for several years. For many corporates, expect that setting up a supply chain facility will take longer than you planned.

Payables

How much will you pay next week?

This seems like a simple question to answer. Intuitively, payables is a process that is under your control since you decide when you pay invoices. The reality is much more complicated. The first problem are invoices on insanely short payment terms. Invariably they will need to be paid immediately once the payables department receives the invoice. The second reason will be invoices that are authorised too slowly. Many invoices will arrive in payables after they were due and need to paid in the next payment run. The third problem is that the supplier has not yet sent the invoice. This particularly true with paper invoices. These normally take between 11 and 14 days to get to the customer's payables department. A small part of this is due to postage delay, but the main problem is that invoices are often posted in weekly batches. These three issues mean that there can be a very large number of invoices that will be paid next week that are not in the accounting system this week. Every payables department has these issues, but the proportion will be different in each case. All this makes it very difficult to forecast next week's cash requirement especially if the patterns of behaviour are erratic from one week to the next.



Supplier Sourcing

Who let you down lately?

The supply chain disruption over the last few months has caused a number of dilemmas for suppliers of manufactured goods that have seen surges in demand as a result of the pandemic. If demand vastly outstrips supply there is a temptation to jack the price up and make a killing. This kind of price gouging is great for short term profits but terrible for the commercial relationship. The customer may accept the increased price in the short run, but will almost certainly re-source the supply at the first opportunity. This will also happen if supply is being rationed. The customers who get the product will be very happy, as long as there was no price gouging. The customer who didn't get the product is forced to finding new sources of supply immediately. Letting people down sticks in the memory.

Ethiopia: On the Up?

Ethiopia is a country with a very long and sometimes tragic history. Most people remember the wars and the famines that ravaged the country in the 1980s. Ethiopia now has one of the fastest growing economies in Africa, but still has one of the lowest GDP per capita in the world. But there are signs of progress. The country has the largest water reserves in Africa, a large pool of low cost labour, is close to many expanding markets in both East Africa and the Middle East and has easy access to international shipping routes. Much of the growth of recent years has been due to public investment and a rise in domestic consumption. And they have just built the largest hydro-electic dam in Africa. That should mean a secure electricity supply in the years to come. But there are still big issues to be confronted. The private sector is quite small and lacks the capital for large scale investment. While things are politically stable now, the country has a history of ethnic tensions at many different levels that in the past have spilled over into violence. But if stability remains the norm, Ethiopia has the potential to become an economic powerhouse in Africa. Recent moves to reconfigure supply chains away from China may also help. There are many positive signs, but there is a long journey ahead.

Brexit: Not done yet

When one or other party employs brinkmanship to get their way, it's a sure sign that they are not interested in a mutually beneficial realtionship. It follows that if an agreement comes out of such a high stakes negotiation it is likely to be focused on short term financials rather than longer term goals. An example would be buying or selling property, where it is likely that the parties have no need for an ongoing relationship so tough price negotiations are quite common. Trade negotiations are rarely like this since the whole point of a trade agreement is to set the parameters for a future long term arrangement. There is also a lot of detail to be covered. Many have the impression that it is simply about agreeing a series of tariffs and that's it. Unfortunately, there are many other things to be agreed. An example would be documentation requirements for exporting goods. Right now in the EU there are none. The extreme will be the documentation requirements of WTO terms. But its all being left very late. From a business perspective, this means that you must assume that there will be a no-deal Brexit and hope that it will be something better. It could be a very expensive game of chicken.

Payment Behaviour

How are things changing?

If you believed everything you read in the press, you might expect that payments are being made later as a result of the pandemic. The real answer is much more complex. There certainly have been cases where some companies have taken unilateral action to either delay payments or to stop payments altogether until they have a better view of their cash flows. There have also been others, like major supermarkets, who have taken action to pay many smaller suppliers more quickly than before the crisis. But there have been some more nuanced responses as well. In one example we have seen a supplier to the restaurant industry extend their payment terms from 30 to 75 days, but actual payment days have stretched from 32 days to 72 days. So they are paying 3 days before the new term. In another example in the same industry the same payment term change happened, but payment days are now 51 days. In both cases, it suggests that payment processes are not fully responding to change in payment terms that each of these companies desired. But in the majority of cases we have seen no changes in payment terms or payment behaviours. This suggests that there are pockets of the economy who are being stretched to the limit, while many others seem to have the liquidity to weather the storm. Let's hope that situation continues.

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