Informita News

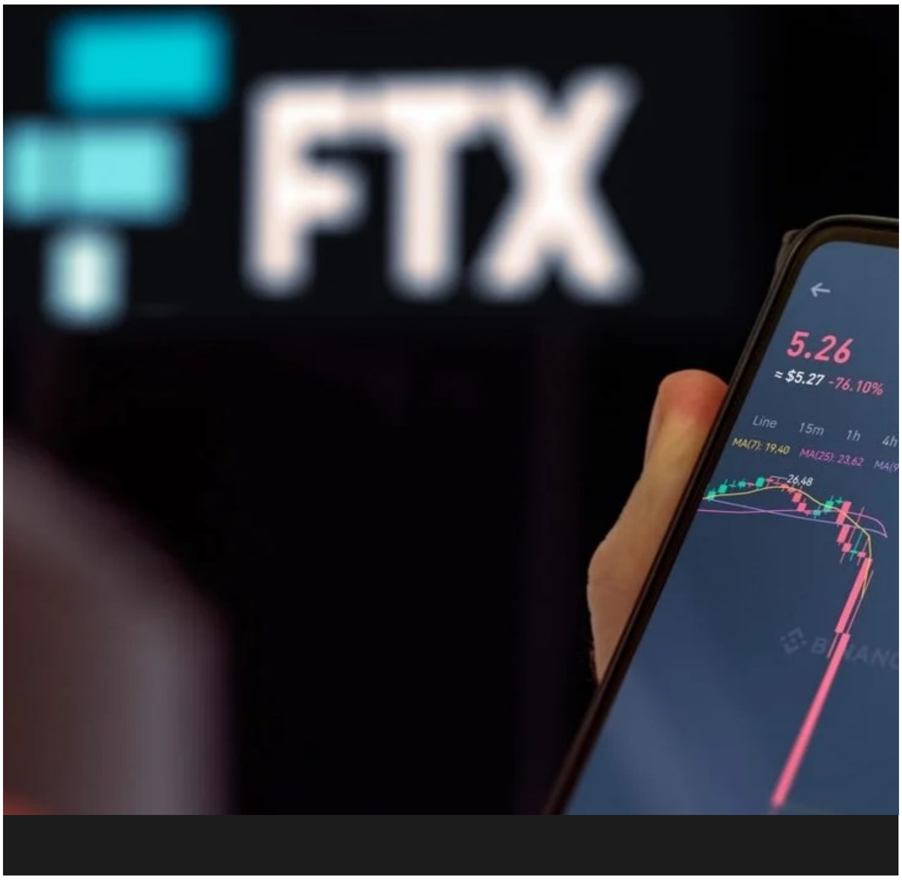
Issue 42 December 2022

About to snap

Most of us are now out of our comfort zone

This year of 2022 will be remembered as one of the biggest rollercoasters in business history. We ended the year with high fuel prices, surging inflation on all fronts, increasing interest rates and continuing supply chain disruptions going on around the world. The only bright spots right now is that ocean freight rates have fallen from their peak and that inflation is not even higher in most OECD countries than it already is, with the exception of Turkey where inflation is running at 85%. The biggest change this year are the long list of multinational CEOs who are refusing to give any guidance as to their expected performance in 2023. The idea that a CEO has no idea what the short term future looks like would be a reason for dismissal in the past. This also means that all those carefully honed business strategies have all had to be thrown out the window as companies roll with the punches. And we don't know when this will all end or how bad it might get. One large restructuring practice in the UK expects 75% of it 2023 clients to enter administration or be liquidated. Many perfectly healthy business that survived the pandemic are now finding that the additional pressures are driving their businesses over the edge. But there is a common thing that all these companies have not done right and that is working capital. The man (or woman) with cash will always have choices. Many organisations that were feeling comfortable did not do enough in the good times. Most of these organisations are not in trouble yet, but the longer the economic crisis continues, they more likely they will be caught in a dangerous trap. Banks are raising margins and rates of interest. Credit insurers are scaling back coverage limits. These are all signs that financial institutions are expecting things to get much worse before they get better. But there is much that can be done before coming anywhere near these danger points. Now is the time to tighten up on working capital controls, get the message out to the organisation that this is not a joke and that everyone needs to play their part. Many businesses will not survive, but the ones with spare cash will survive and thrive.

In This Issue



Is Crypto Currency Safe?

The lessons from FTX

In decades now long ago it regularly happened that banks engaged in risky lending went bust and the depositors and investors lost everything. Since then most countries have various regulations, run by central banks, that protect depositors with guarantee schemes and try to limit the riskier endeavours of banks. Do some banks still go bust? Yes, on occasion. But at least depositors are usually protected and the regulators are often able to save the bank in question. This is exactly the kind of safety net that does not exist for crypto currencies and their associated exchanges. While fans of crypto rightly say that this lack of regulation means that these forms of monetary exchange reflect the market as it develops, either positively or negatively, the lack of regulation means that the failures continue (FTX is by no means the first) and the reasons for failure are usually the same - a lack of liquidity caused by poor financing decisions. In the banking world, heavy regulation started after the Wall Street Crash in 1929. Many complained that it quickly became over-regulation, but at least it was there. The difficultly for crypto is that it evades all the usual national structures. No one central bank has jurisdiction over the assets of any of the players. We don't even really know where the assets are being held and finding out the ultimate owners of crypto it is more difficult than finding the owner of a Swiss bank account. The only viable means might be that the crypto exchanges develop some form of self-regulation that would protect asset holders. But this is like putting the fox in the hen-house. Expect that the fans of crypto will carry on regardless, some people will lose their shirts again as more exchanges fail in the future and the vast majority of the public will continue to ignore crypto as a result.

Supply Chain Compliance

New German law

On the 1 January 2023 a new German law comes into force. It called "Gesetz über die unternehmerischen "Sorgfaltspflichten zur Vermeidung von Menschenrechtsverletzungen in Lieferketten" or LkSG for short. It embodies new rules to ensure companies doing business in Germany meet the standards set out in United Nations (UN) Guiding Principles on Business and Human Rights and the OECD Guidelines for Multinational Enterprises. Similar laws are coming across the European Union. The main problem for many large companies is that there is an assumption that large companies have a good knowledge of their supply chains. In reality, most procurement departments have little idea of their supply base past the major ones on their spend list. In future this will mean a company could be liable to large fines. So it might be a good time to learn about tail suppliers.

Military Logistics

Lessons for us all

The general who proves to be the master strategist or tactician tends to become famous in history. Even today we can be fixated by the number of soldiers, tanks, aircraft and weapons that an army has. But none of that counts for very much if that same army cannot be supplied. Good modern armies employ serious logistical experts to make sure that the troops are fed and watered and that the right materiel is supplied to the front line. That has led to the modern techniques of supply chain planning and many tools that are in everyday business use. Some of the best examples are the forklift truck and the humble pallet. Although not invented by the US Army, in World War II they expanded their use dramatically and since then have become ubiquitous across the world.

Puerto Rico: Not all bad news

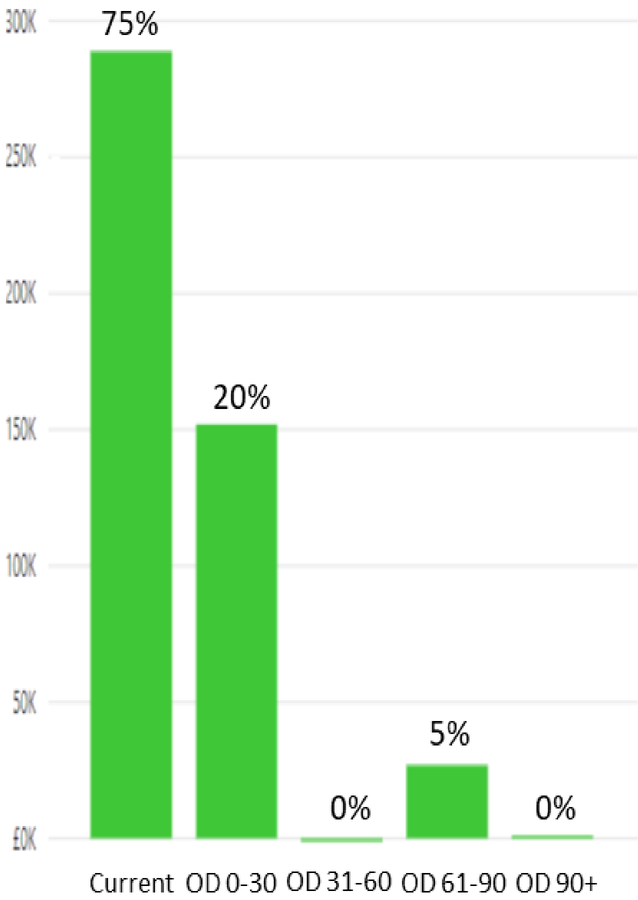
It is considered the most competitive economy in Latin America by the World Economic Forum and ranks highly on the Human Development Index. As an unincorporated territory of the Unites States, citizens of Puerto Rico enjoy freedom of movement throughout the United States without having to pay federal taxes. The economy is mainly driven by pharmaceuticals, textiles, petrochemicals, finance, insurance, real estate and tourism. Agriculture only accounts for 1% of GDP. Like most islands, it is highly dependent on imports for food and other consumer items. But there are three things that Puerto Rico has become known for in recent years. The first is the vibrant debate about the island’s political status. Should it remain as it is, become a US state or become independent? That debate still rages. The second is the enormous debt of the Commonwealth government that has resulted in underinvestment in public services and a near collapse of the public healthcare system. And finally for hurricane damage. The most recent hurricane knocked out all power on the island. While nature cannot be resisted, the power grid has suffered from underinvestment over many years. But its not all doom and gloom. The island is known for its scenery and beautiful beaches and is a much safer place to be than other Latin American countries. There are always plenty of wonderful places to relax and enjoy.

Dollar Inflation

The US Dollar remains the main reserve currency of the world and that means that many commodities, such as oil and metals are priced in US Dollars. In recent times that has been terrible for Europe, since it costs more Euros and Pounds to buy commodities and imports from the Far East that are usually priced in US Dollars. But this insulates the United States from inflation to an extent since it means that US imports can actually go down in price since the mighty dollar can buy so much more in other currencies as the dollar continues to strengthen. Given that US GDP is 70% driven by consumer spending, this would suggest that US inflation has been driven by an overheating economy. The Federal Reserve has been raising interest rates and while that will eventually calm inflation it also makes the US Dollar even stronger. That would suggest that apart form the effects of various supply chain disruptions across the world in the last years, we are probably going to have wait for the US to gets its inflation under control before the Fed starts to easing off on interest rates, making the US Dollar weaker. It is normal to have up to a 12 month time lag between interest rate decisions and seeing any effect on consumer demand. So it could be quite a time before we see US inflation settle down. That would further suggest that companies in Europe need to be prepared for at least another year of increasing prices and wage demands.

Is your aged debt report fooling you?

We recently encountered two separate instances where an aged debt report was giving a very misleading picture of the level of overdue accounts receivables. Many years ago it used to be that many systems would produce a standard report that was aged to invoice date and not to due date. That problem has largely been solved. The big unsolved problem are the terms used to calculate the due dates. In the first instance, there were a number of customers paying via a supply chain finance facility. The official payment term was 90 days from invoice, but anyone who uses these programmes knows that you should be expecting paying immediately once the invoice has been authorised. That should usually take 8-12 days from invoice date but it was actually taking 23 days. That might not be technically overdue, but that is a major cash opportunity. In the second instance, a customer has an option to pay in 45 days with a settlement discount or pay in 90 days without a discount. They always took the discount and paid in 51 days. So they were paying 6 days after due date and taking an unearned discount. That is the double whammy of an overdue position and lost margin. These issues are solvable but accurate reporting is vital. It is one of the reasons we never rely on an aged debt report to spot cash flow opportunities and discover opportunities using transactional data.



Visit our websites and listen to our podcast

(click on the logos to find out more)

Informita

PLÉSONA
BUSINESS ADVISORS

TERMSCHECK.COM

THE WORKING CAPITALIST$ PODCAST

Website: www.informita.com

Twitter/Facebook/LinkedIn: @informita

Email: brian.shanahan@informita.com
Phone: +351-911556662