WORKING CAPITAL MANAGEMENT

Unlocking Cash in a Challenging World

Boosting Modern Working Capital Strategies

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When the trading world seems set for a future of uncertainty, the best strategy is to ensure access to liquidity is unhindered. It sounds simple but for many it is not. Johannes Wehrmann, Managing Director, Corporate Solutions, FIS Supply Chain Finance, directs the way to easier working capital access.

As a set of impactful macroeconomic factors, interest rates, investment strategies, and trade tensions run high on the agenda for many treasurers. How each is tackled, and the degree of success of that effort, has much to do with the adoption of a robust liquidity strategy.

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Interest rate volatility over the past few years has seen higher rates make their presence felt, and Wehrmann notes rate instability "feels like it will continue to be a treasury topic for some time to come".

Indeed, for the FIS Supply Chain Finance business, where the transactional focus is largely on USD, euro and GBP, the world is one now in which the conversation about elevated interest rates often concerns a new normal of 'slightly higher for longer' rates.

The element of uncertainty across these major currencies – albeit they are all more even-tempered than they were a few years ago – is not only playing out on the interest rate side but also on the global trade side, comments Wehrmann. The obvious trade tensions of the past year continue to have a significant impact across the global supply chain. Inventory management is a challenge when it comes to levels and locations, for instance. "And we see rising concern on the corporate side in dealing with their overall working capital positions too," he notes.

Indeed, questions now abound on how best to mitigate the impacts of all current trade challenges. For Wehrmann, it suggests that a robust approach is needed on matters such as hedging, insurance, or receivables finance, and in addressing emergent issues around liquidity, inventory, and payables. "It looks like all aspects of working capital are subject to scrutiny and possible revision. And from a financing perspective in particular, establishing an ample liquidity cushion in these uncertain times looks like a good choice."

Building blocks of success

However, responding with a robust working capital strategy is not necessarily straightforward, cautions Wehrmann. Depending on the company and its geographic footprint, he advises initially taking "a very broad but deep look" at DSO, DPO and DIO, and then considering the relative value in this context of partnerships, including FIs, advisers, and platform vendors. "Having a holistic view over different levers of liquidity and working capital right now, and being open to the full spectrum of solutions, makes a lot of sense."

With investment by various providers across the working capital market having increased, certainly in the last decade, Wehrmann reports that deployment effort and costs for clients are decreasing. "It's true, there has been notable change in the industry as new players enter and others retreat. For a treasurer, spending the time to explore and understand the new market landscape really is worthwhile."

One of the key beneficiaries of this industry effort could be sponsor-owned businesses. Private equity and venture capital companies in particular are often highly leveraged (and obviously they are in leveraged buyout scenarios). These businesses are naturally more susceptible to higher interest rates, and all tend to be pushed by owners to optimise their overall cash positioning, observes Wehrmann. In circumstances where incurring further leverage in these firms is undesirable, off balance-sheet working capital structures may be more interesting.

Another potentially beneficial situation is where an asset-light business model has been adopted. Firms in service industries, for example, may be driven by current macroeconomic uncertainties to seek additional liquidity. "Here, working capital on the receivables and payables side can be an appropriate means of supporting the overall financing structure of the company," he explains.

Raising awareness and understanding

While the advantages of certain working capital solutions may be readily apparent to many, deployment may not be obvious to all. "To some, it's just an issue of awareness," suggests Wehrmann. In other companies, their relatively easy access to mainstream debt facilities may preclude them even looking at working capital solutions. For an AAA-rated company, for instance, issuing commercial paper may be seen as the most convenient way to refinance its short-term liquidity needs.

"It's certainly not a solution for every company," Wehrmann acknowledges. Indeed, some business models are not as suitable as others in this space. "For a retail business, monetising consumer receivables will not be as effective as a B2B firm seeking to unlock working capital by using its receivables as securitisation for a large commodity trade."

It can be the case, too, that working capital solutions are perceived as being overly complex to set up from operational and reporting perspectives. "Especially on the private equity side, companies tending to grow inorganically through an active M&A approach are often faced with a plurality of ERP systems and data points within the group. Making sense of data flows to structure an efficient transaction may ramp up the complexity of even a straightforward transaction."

With a number of potential pain points to address, tackling awareness issues for working capital solutions can be a challenge, admits Wehrmann. "It sometimes has to be a multiyear journey with continuous messaging," he explains. "Our industry must be cognisant of, and ready to address, some of the less favourable mainstream media headlines of recent years where certain products had been misused. As an industry, we must highlight the many positive applications and implications of working capital solutions. We should be demonstrating how to set up these transactions properly and ensuring a proper level of understanding and awareness across all stakeholders."

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New players, more options

While many companies may know only about the traditional working capital market, there have been new entrants – including fintechs, private credit, and institutional investors – opening up options and access for many more potential SCF users.

"It's a very positive development because now companies seeking finance can find a wide range of providers with different solutions," comments Wehrmann. "There are plenty of providers now, with different solutions across inventory, receivables or payables finance, even hybrid structures," he notes. Of course, he advises choosing a provider carefully. "Treasury should maintain an open mind, and be ready to use different sources to acquire the fullest understanding of the market."

Nonetheless, from a corporate treasurer's perspective, having more working capital financing options is a positive development for liquidity management, not least because it means no longer having to rely wholly on a small group of relationship banks. Indeed, the arrival of new and different providers in this space has presented companies of different structures and sizes with increased access to capital, where 15 or 20 years ago it was simply not available.

An easier way

Specialist technology plays a key role in opening up this market. At its core, it enables corporates, funders, intermediaries, and other stakeholders to transact more efficiently. "What is possible nowadays in terms of process automation is a huge advance on what was possible just a decade ago," comments Wehrmann.

The removal of paper-driven processes has facilitated increased automation and reliability in terms of data consistency, he notes. This enables greater integration across data sources, including ERPs and TMSs, providing for a far smoother experience. The bottom line is that it is now possible to process a significantly higher number of supplier transactions with little or no manual intervention.

"The FIS platform, for example, is capable of extracting and consolidating data streams from multiple data sources," reveals Wehrmann. "This serves to harmonise and automate data flows, achieving a very high degree of report accuracy, irrespective of the complexity of those sources."

Where previously some facilities were labour-intensive from a data provision and reconciliation perspective, he explains that the time required now to run transactions is considerably lessened. "Treasurers really don't have to concern themselves too much with operational aspects of a programme."

A new baseline

It may be argued that becoming entangled in the intricacies of a technology project when treasury should be focused on managing liquidity in the current environment, is an unnecessary diversion. But while many IT projects will absorb some time and resources, Wehrmann explains that the introduction of technology, at least from the FIS perspective, should in fact decrease overall complexity.

"Technology can be the root of more informed decisions in the treasury world," he states. "It is fast becoming the baseline. We will soon reach a position where a well-thought-out technology stack will not just be a simple hygiene factor, but the basis for the proper running of the treasury function."

In a challenging trading environment, where robust working capital strategies demand easier access to liquidity for buyers and suppliers alike, the right tools could indeed become the new baseline.

While funding providers will always need to assess and underwrite counterparty risk – and supply chain finance will always suit some sectors better than others – Wehrmann believes that with the right technology and partners in place, unlocking cash in a challenging world is now well within the scope of many more companies.

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