
Bridging the gap

2016 Singapore working capital study



Foreword

Welcome to the inaugural 2016 issue of our annual working capital study for Singapore. We believe this is the first working capital study to focus on Singapore and we hope you will find our local perspectives relevant and insightful.

Working capital is the lifeblood of any business and most companies can release significant amounts of cash from their balance sheet by managing working capital more actively.

In these times of economic uncertainty, reduced access to credit and interest rates that cannot go any lower, working capital management offers the cheapest source of funds and is available to most businesses.

Initiatives to release working capital and increase liquidity can fuel strategic investments and allow the reduction of debt. In addition, profitability can be enhanced due to efficiency improvements and a reduction in the cost of capital. Considering all of these effects, improving working capital inevitably leads to a sustainable increase on Economic Profit/Return of Capital Employed (ROCE), and therefore to a higher corporate value.

Our study shows that companies focusing on working capital not only see a better cash position and improved working capital but also benefit from a higher EBITDA margin and higher investment rates.

Managing working capital efficiently and optimally can be challenging. However, with the right skills and support, in our experience there is usually scope for working capital improvements in most businesses.



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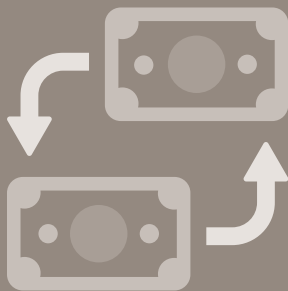
Key highlights



70% of sectors studied have seen their working capital performance deteriorate YoY



Cash on hand fell 26% YoY



S\$6 bn of NWC across companies studied



S\$2.4 bn of additional cash tied up in FY15



Top performers show 40% higher EBITDA



Top performers show 30% higher investment rate

Why working capital matters

The analysis from our 2016 Singapore working capital study shows an average Net Working Capital (NWC) employed of 18% (of sales) across 136 listed companies; with a combined total of S\$ 26 billion of NWC.

Our study also shows a year-on-year (YoY) deterioration in working capital performance across 9 out of 13 industries studied in Singapore. The results suggest a lack of a cash management culture and signpost the scope for further focus on the processes and discipline that can support cash release.

The traditional working capital levers remain the bedrock of any systematic effort to control cash:

- Procurement strategy and payment processes
- Order management and invoicing & collection processes
- Inventory planning and sourcing & delivery

The importance of working capital is more critical in today's volatile economic environment, where in addition to declining revenue and longer cash cycles, we are also seeing decreasing levels of cash on hand. Companies will therefore need to be pro-active about releasing cash from their balance sheets, which they can then leverage to sustain their business.

Our study shows an overall declining working capital performance YoY with:

- a decline in sales
- a longer cash cycle
- and decreasing cash on hand

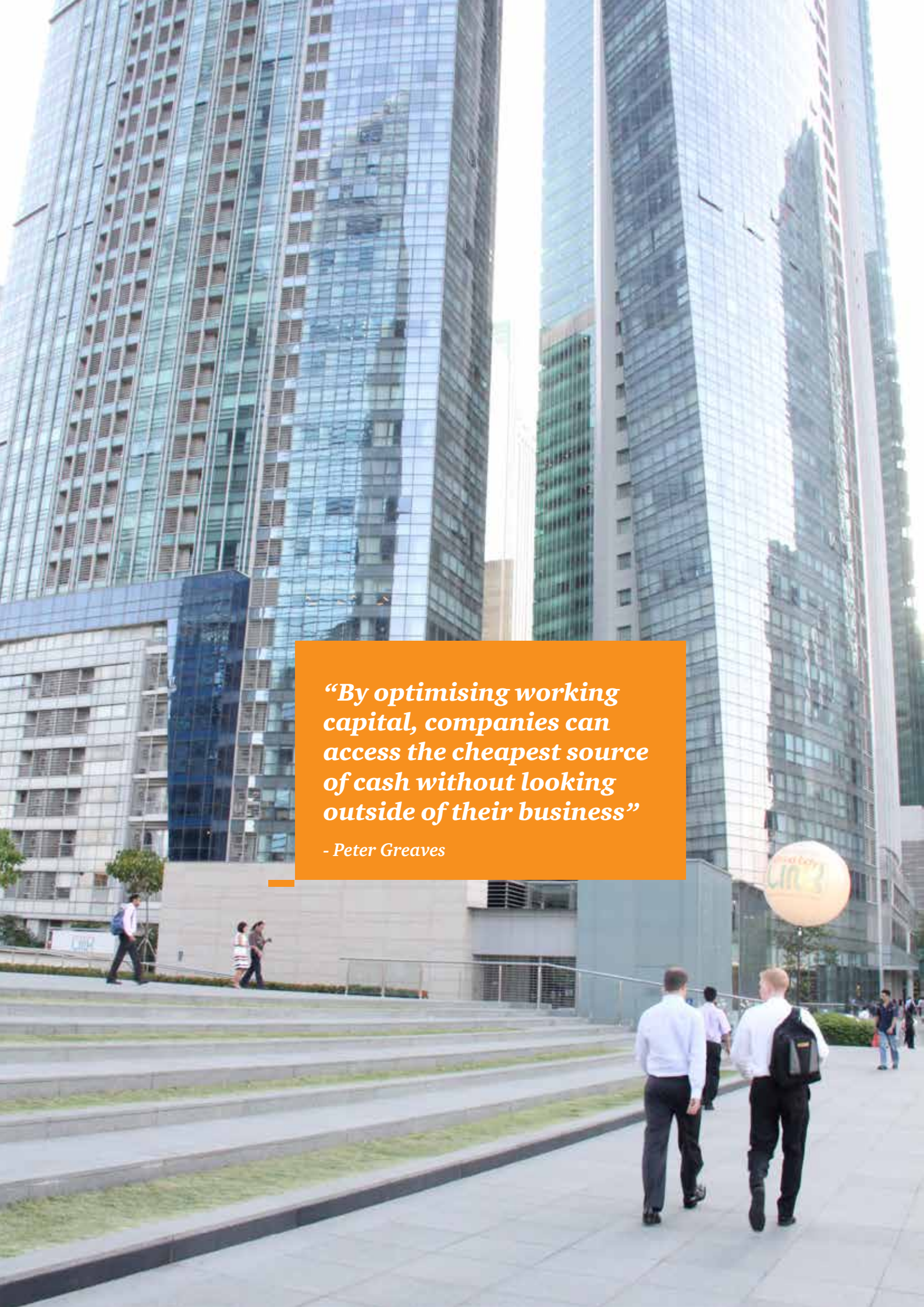
Given that interest rates are unlikely to fall below current levels, a 1 point increase from say 5%, would result in a 21% increase in interest costs.

There is clear evidence that much can be done to optimise the working capital performance of a business and gain strategic benefits (Figure 1).

In fact, our study shows that top working capital performers lead the way and show the benefits of a cash culture, recording higher investment rate and EBITDA margin.

Figure 1: Strategic benefits of working capital



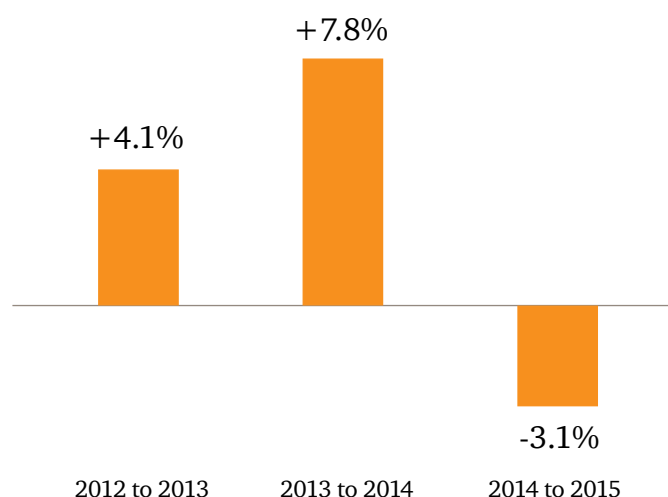


“By optimising working capital, companies can access the cheapest source of cash without looking outside of their business”

- Peter Greaves

Singapore working capital at a glance

Figure 2: Change in annual revenue



S\$2.4 bn of additional cash tied up in FY15

Our study of 136 companies in Singapore shows a revenue drop of 3.1% (Figure 2) from the prior year. This is in part due to global economic headwinds (e.g. lacklustre growth and currency volatility), but some industries such as the metals sector, construction & engineering, as well as transportation & logistics have been more hard-hit than others.

We note a 4.1 days deterioration in NWC in the FY15 cash cycle YoY (Figure 3). This deterioration is strongly driven by a 4.5 days average increase in debtor days to pay (Figure 5a). In cash terms, this translates into some S\$ 2.4 bn of additional cash tied up.

Cash on hand in 2015 has fallen 26% YoY and sharply from 2012 and 2013 levels (Figure 4). Companies planning to invest over the next 2 years that are also working to improve their working capital performance will stand to benefit from a self-funding advantage.

Figure 3: NWC days

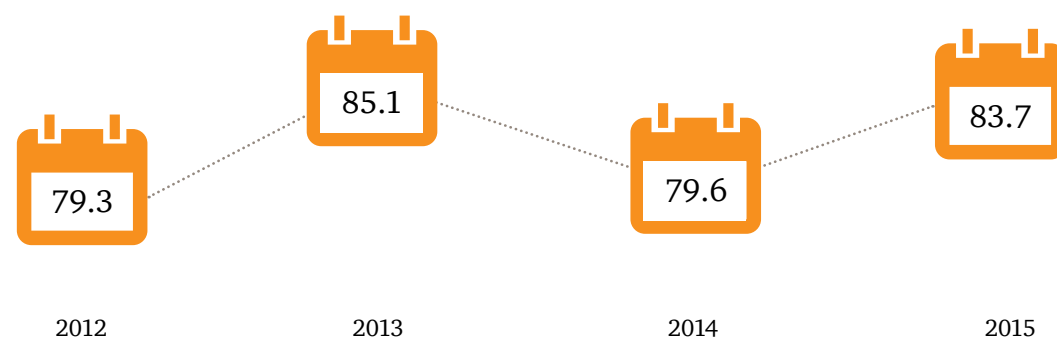
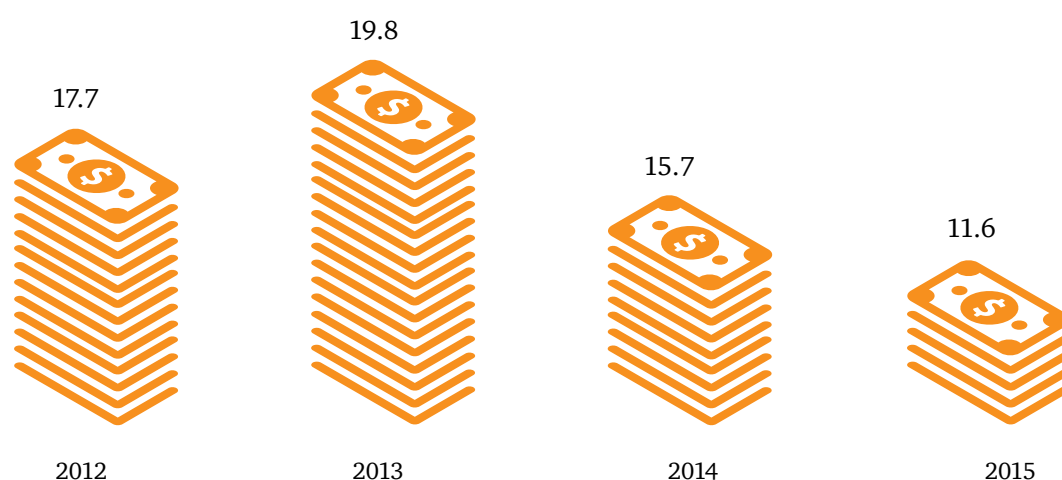


Figure 4: Cash on hand (S\$ bn)

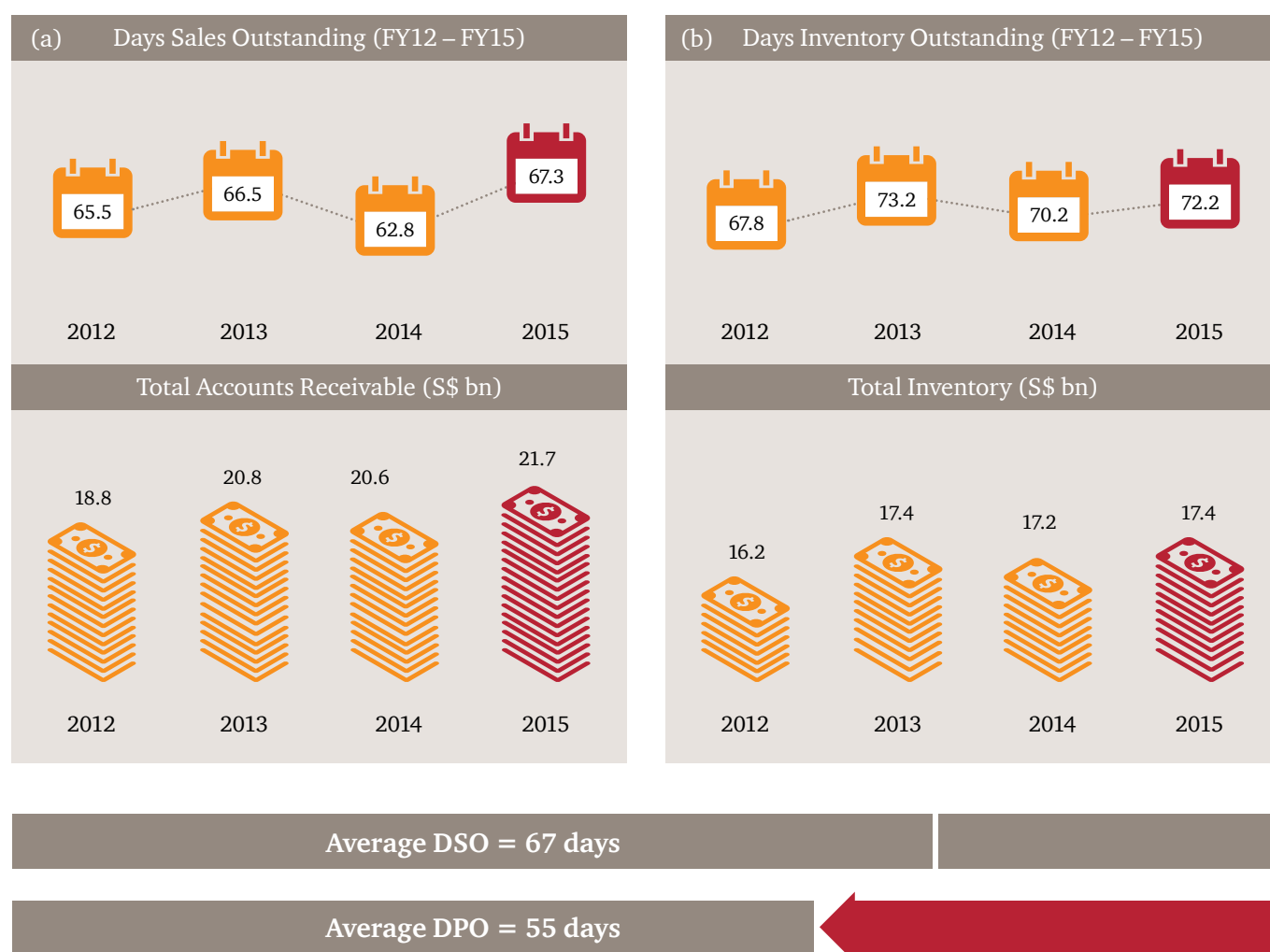


Working capital KPI's overview

The improvement shown in days payables outstanding (DPO) has partially off-set the deterioration in both days sales outstanding (DSO) and days inventory outstanding (DIO) (Figure 5). However, there is a strong imbalance between DSO and DPO which highlights a need for further improvement in payables and further focus on collections.

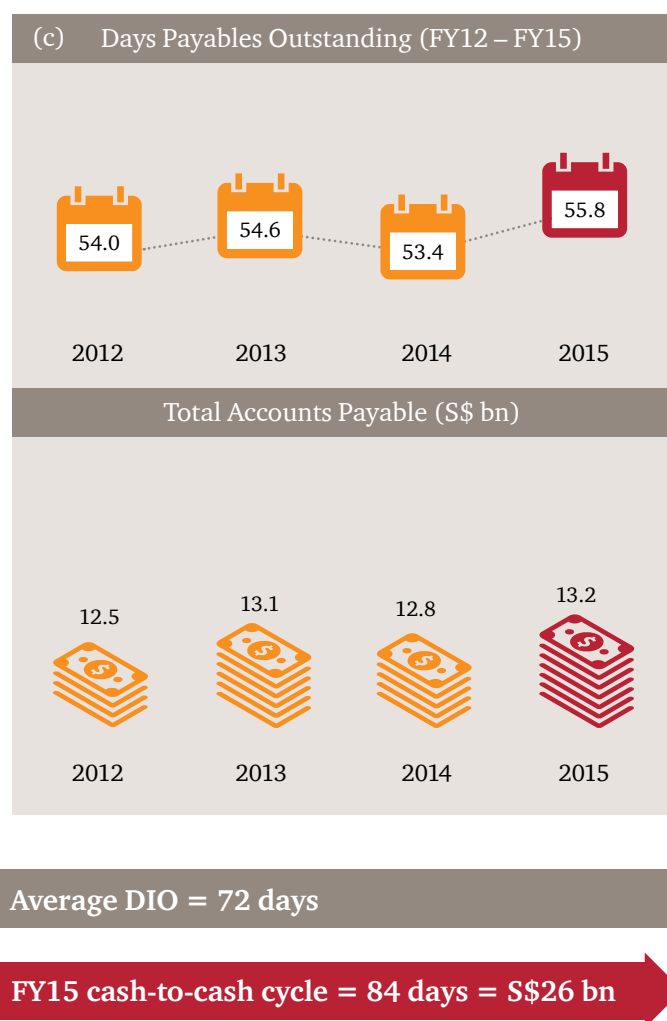
The average time to collect from debtors has increased by 4.5 days compared to 2014 (Figure 5a) – a negative impact to the overall NWC performance. For some companies, this could be the effect of late payments from debtors, or a short term strategy in granting longer payment terms to “boost” sales.

Figure 5: Working capital KPI performance breakdown



DIO performance has worsened by 4.4 days since 2012, with 2014 improvements cancelled out by an increase of DIO to 72.2 in 2015. It appears that there is scope for a greater focus on inventory management going forward (Figure 5b).

Looking at the average performance across sectors, companies are 2.4 days slower in paying their suppliers compared to 2014 (Figure 5c). For some companies, this could be the result of tightening liquidity, but for others, it may demonstrate a focus on creditors' terms and processes.



Working capital performance

Our study analyses working capital trends in Singapore based on three main factors that impact and drive its performance:

Industry

Some sectors require more working capital than others. However, our analysis shows that there can be a wide gap between the bottom and top performers within each industry. This indicates that some companies are more efficient at managing their processes across the working capital cycle.

Company size

Larger companies tend to be better at managing their working capital. Meanwhile, smaller businesses often have less sophisticated working processes, systems and functional expertise even though they may have a greater need for cash to finance their growth.

Management and financial performance

The importance placed by management on cash and working capital will dictate their ability to manage working capital and benefit from a strong and reliable cash flow to run their day-to-day operations. Too often management turns to banks or investors to fund their working capital rather than finding ways of generating more free cash flow themselves or reducing the funding requirements by becoming more working capital efficient. This need for cash goes far beyond working capital funding, with businesses under competing pressures to pay dividends and invest in growth.

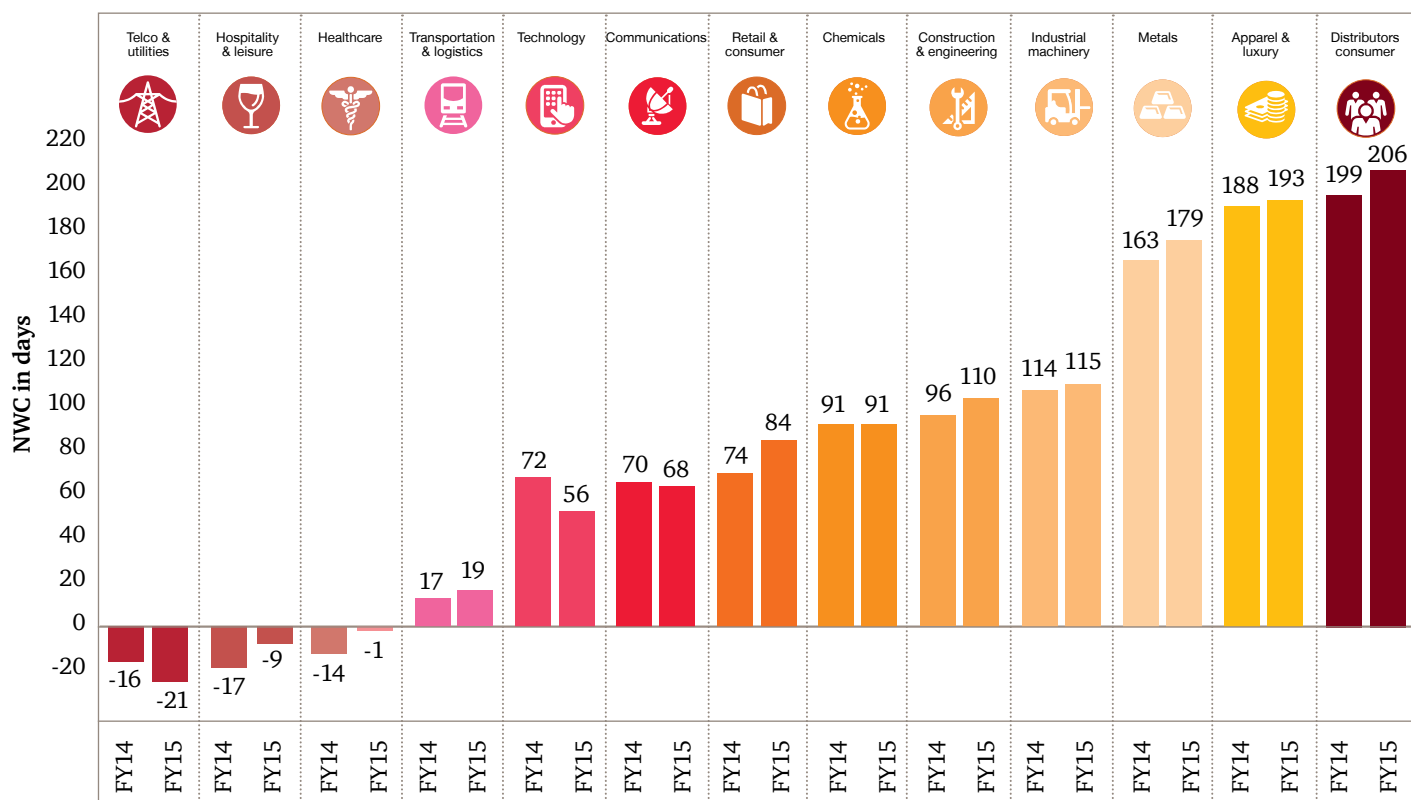




Analysis by industry

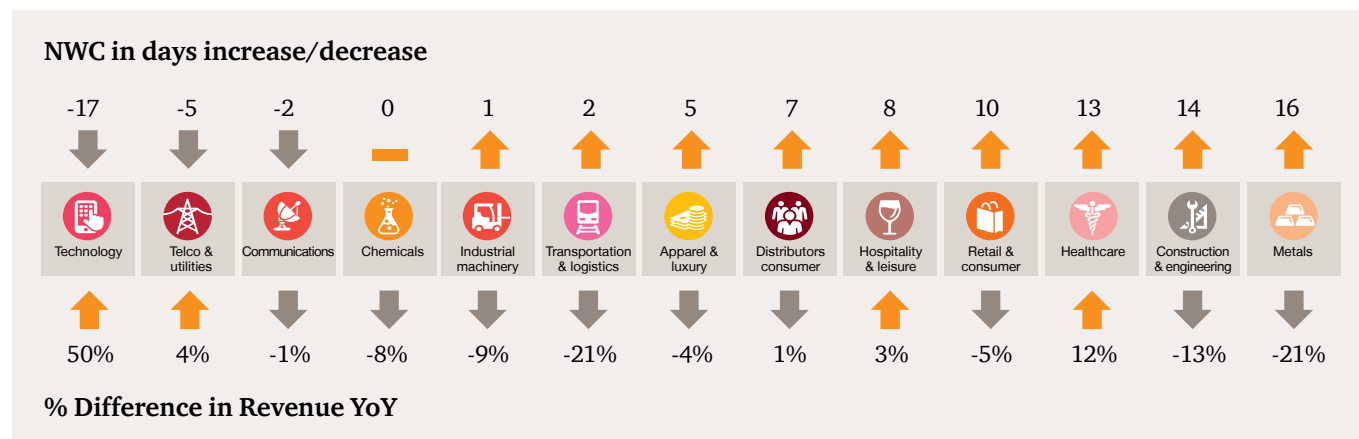
While the levels of working capital required vary between different industries, the majority of the industries studied saw their working capital performance decline from the previous year.

Figure 6: NWD by sector, FY 2014 – FY 2015



Detailed performance by sector

Figure 7: Breakdown of YOY increase/decrease in NWC and revenue



9 out of 13 sectors deteriorated in FY15

Our study shows 9 out of 13 industries studied in Singapore experienced a deterioration of their working capital performance YoY, and the majority also saw their revenue declining in the same period. The three sectors that registered improvements (i.e. decreases) in their NWC in days (NWD) are technology, telco & utilities, and communications (Figure 7).

Improvement most significant in the technology sector

The technology sector displays the largest improvement with a 17 days decrease in NWD, driven by a lower DSO and DIO, coupled with a 50% increase in revenue, reflecting the growth trend experienced by the technology industry. However, 33% of the technology companies studied failed to improve their performance, potentially from a lack of focus on working capital, but the resounding success of the majority shows the opportunity for improvement exists and can be rewarding.

Retail & consumer

In addition to a 13% increase to its NWD corresponding to a 10 days deterioration, this sector saw all 3 streams of working capital performance decline: DSO has increased by 1 day on average, and both DIO and DPO have deteriorated by 5 days and 3 days respectively. As the sector deals with a slowing economy, it also has to face an increase in the number of outlets, creating the need for strong control of inventories and strict management of procurement constraints.

Substantial deterioration in healthcare

The healthcare sector saw the highest increase in NWD with +13 days (93% increase) YoY. This deterioration was mainly driven by a sharp increase in DSO, reflecting a significant shift towards corporate agreements and extension of “cashless” schemes.

That being said, Healthcare remains among the best performing sectors, running with negative working capital days at -1 day.

Construction & engineering

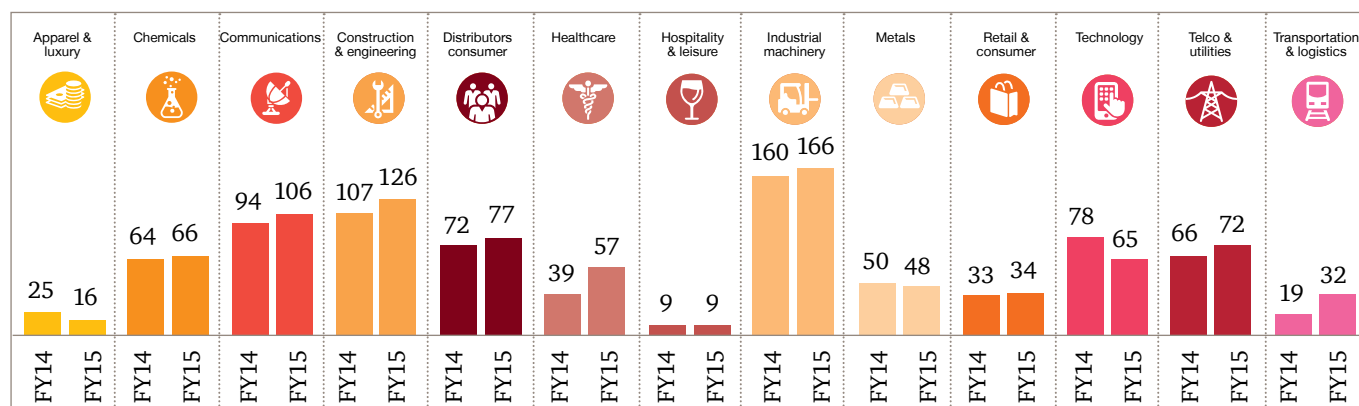
The sector saw a 14% increase in NWD (second highest among 13 sectors studied). While DPO improved by 9 days YoY, it was not sufficient to off-set the substantial increase in DSO (+19 days) and DIO (+4 days). An escalation in delayed payments from debtors, with a consequent partial impact on creditors, are indicative of challenges experienced by the industry.

Metals

Despite seeing a 16-day increase in NWD (Figure 7), it is worth noting that the majority of the companies within the sector improved their performance between 2014 and 2015 (Figure 9, page 14).

Figure 8: Breakdown of sector performance by DSO, DIO and DPO

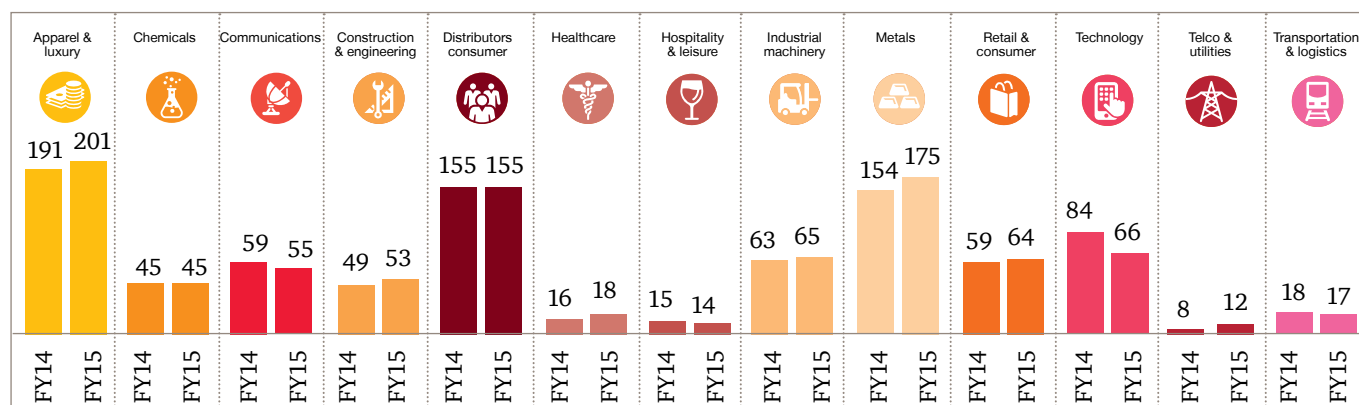
Days Sales Outstanding



The majority of the sector in our study (10/13) failed to improve or maintain their DSO with the exception of apparel & luxury, metals and technology.

The transportation & logistics and healthcare industries both show an exceptionally high surge YoY. Both these sectors have challenges and it is even more important they monitor closely their cash flow.

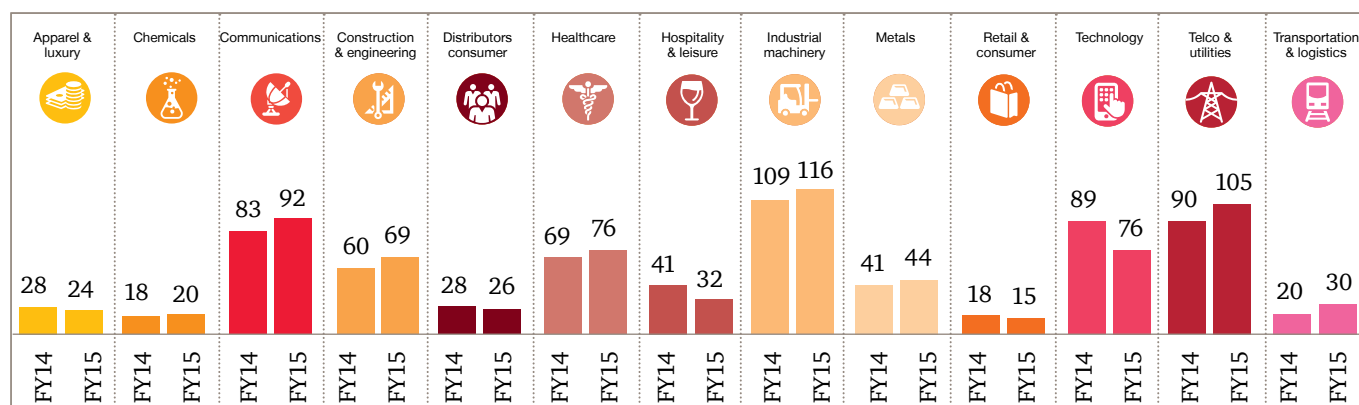
Days Inventory Outstanding



More than half the industries show a deterioration in their DIO.

Whilst the technology sector improves its performance by 18 days reduction YoY, the apparel & luxury sector shows a 10 days increase in DIO reflecting the slowing pace of growth.

Days Payables Outstanding

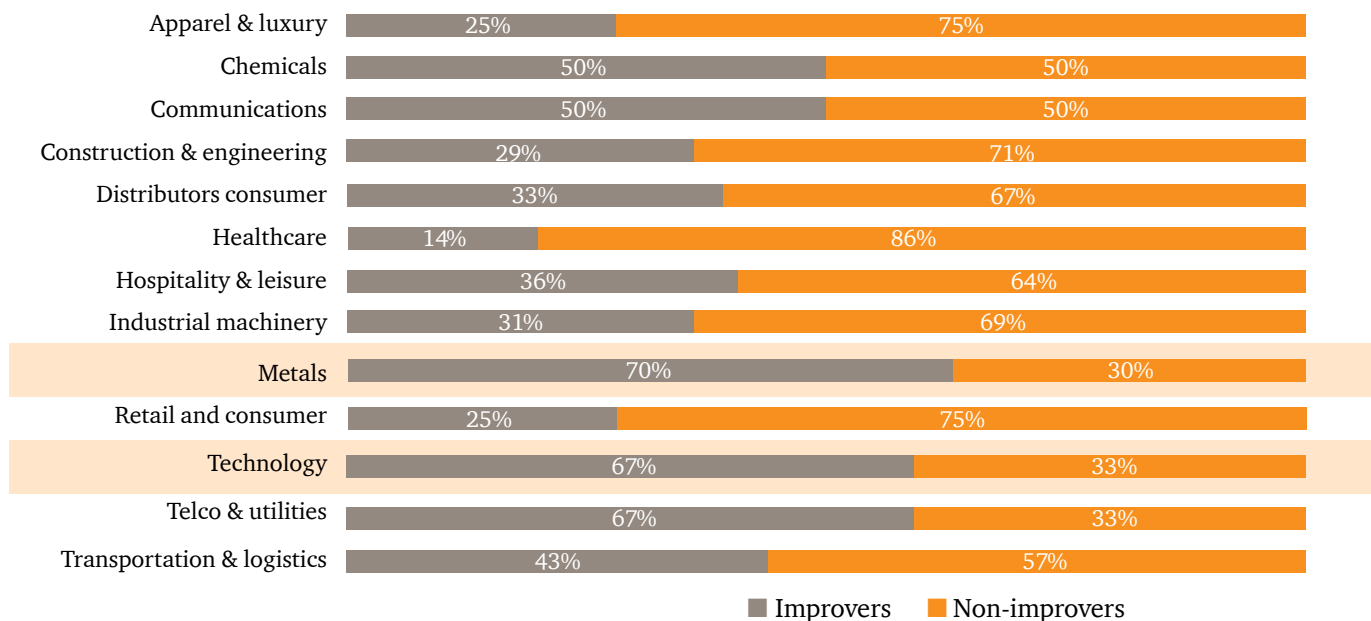


Seven sectors have been able to improve their performance and two have managed to maintain it.

Healthcare has managed to partially off-set its poor performance in DSO and DIO with a 10% increase YoY.

Technology, instead, has not been able to maintain its overall excellent performance in payables as well, recording 13 days retrogression.

Figure 9: Breakdown of NWD improvers by sectors



Despite a deterioration in NWC days, the metal industry saw 7 out of 10 companies improve their performance between 2014 and 2015. The technology industry saw a dramatic improvement in overall NWC days (-17 days); however, 33% of the companies failed to improve their performance.

Analysis by company size

Size matters

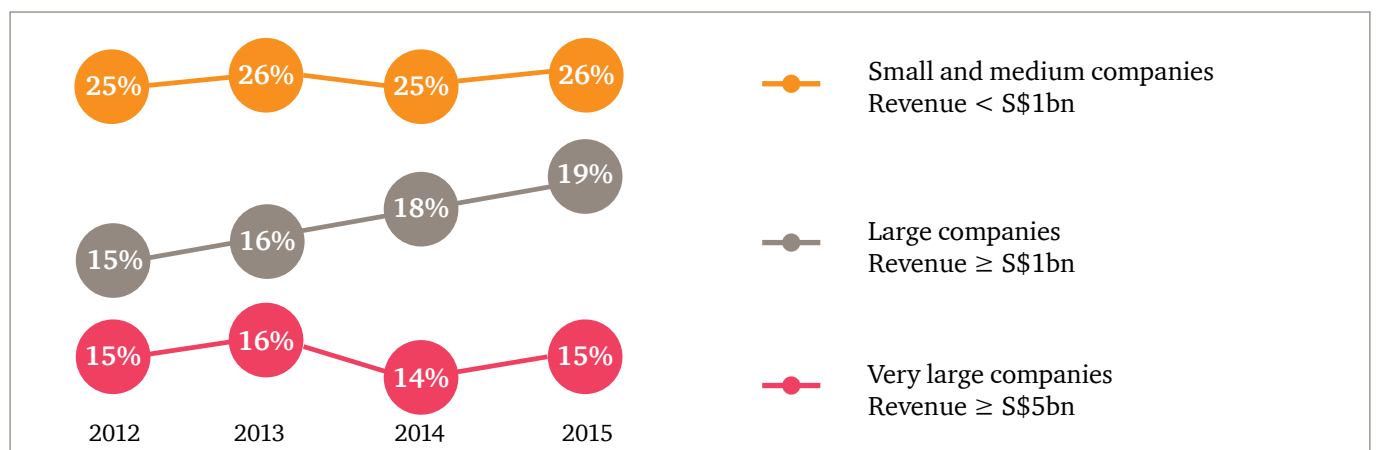
Large companies saw their NWC % increase YoY from 2012 (Figure 10). Very large companies' performance has been quite flat over the past four years although they saw a 1% increase in their working capital as percentage of sales in 2015. Both large and very large companies still maintain a much healthier NWC performance compared to the SMEs.

Overall, large and very large companies are performing better than the small and medium sized ones. This is in part due to larger businesses having easier access to

alternative sources of capital and stronger negotiating power. In addition, their management tend to have a stronger focus on potential free cash flow, finding ways to unlock their cash for self-funding purposes.

Typically, smaller companies strive for cash while struggling to obtain funding. From our study, we can see NWC as percentage of sales for SME's is 27% to 42% higher than the large and very large companies. Unlocking cash from excess working capital could be a good alternative source of capital.

Figure 10: Working capital as % of sales





Analysis by management and financial performance

Top performers have 108% more cash on hand than bottom performers

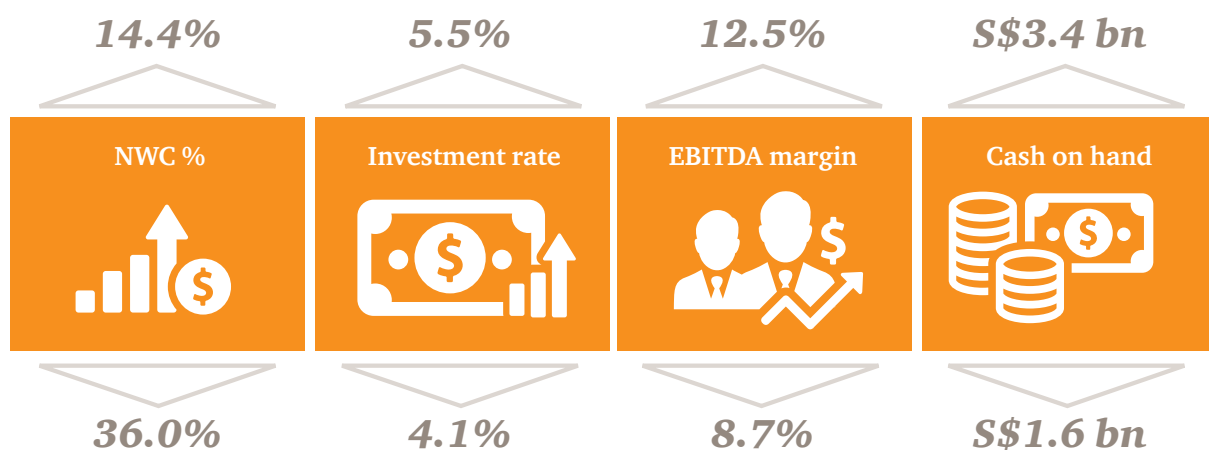
Cash is a growth driver. It enables businesses to invest, acquire, pay dividends, refinance and reduce covenant risk.

Top performing companies in working capital (the upper quartile) demonstrate better financial performance with a 40% higher EBITDA margin and a 30% higher investment rate than the bottom performers (Figure 11).

Industry leaders continue to focus on generating cash to maintain their lead and reap the benefits of high performing working capital management (WCM). With the rising cost of capital likely to impact return on investment, it is becoming crucial to plan ahead and use working capital as a tool to ensure businesses are best positioned for the future.

Figure 11: Top and bottom performers

Top performers (upper quartile)



Bottom performers (lower quartile)

Next steps forward

The PwC approach

Improving working capital performance requires the analysis and understanding of the full cash-cycle and to identify opportunities that are driven by four key components:

1. Commercial terms

- Understand all terms in place
- Match terms with size and nature of contracts
- Establish methodology based on internal and external best practices
- For production industries, also consider logistical terms

2. Process optimisation

- Understand each process and its review cycle
- Develop process optimisation methodology, including trade-off tools
- Challenge individual steps of process with aim of optimising full process with regard to WCM

3. Compliance & monitoring

- Analyse and measure compliance with terms
- Understand root causes and key drivers for non-compliance
- Evaluate cash and overall business impact
- Develop relevant KPIs for high WCM visibility and monitoring

4. Cash culture & management

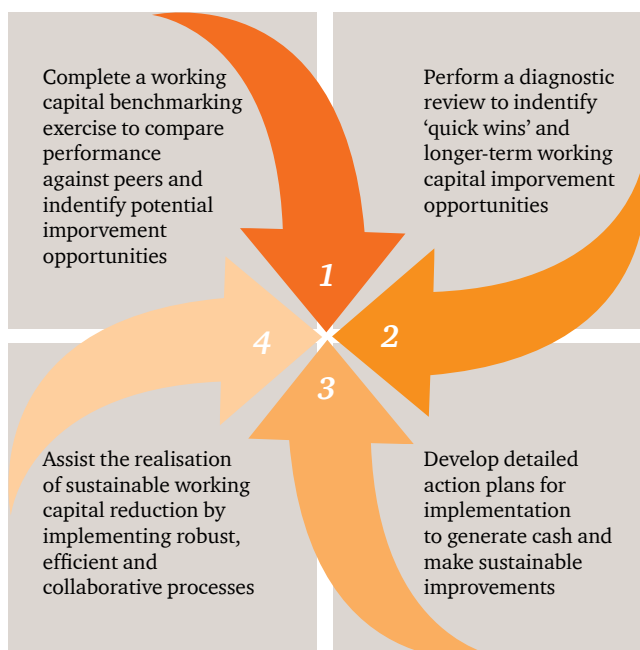
- Ensure that cash and working capital become part of performance measurement
- Define accountability and responsibility for WCM performance and management
- Involve top management (from a monitoring perspective)





How we can support you

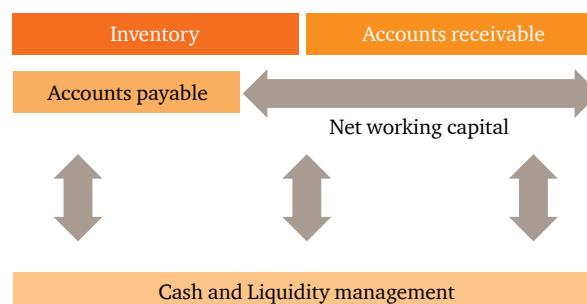
Phases in the journey



Addressing the key levers

- Identification, harmonisation and improvement of commercial terms
- Process optimisation throughout the end-to-end working capital cycles
- Process compliance and monitoring
- Creating and embedding a 'cash culture' within the organisation, optimising the trade-offs between cash, cost and services

Components we tackle



Methodology

This study provides a view of working capital performance based on data sourced through S&P Capital IQ, selecting 136 listed companies in Singapore (based on the location of their headquarters). As the research is based on publicly available information, all figures are financial year end figures.

It should be noted that underlying working capital requirements within reporting periods may be higher than shown due to the impact of efforts to improve working capital performance towards year end. Also, off balance sheet financing or the affect of assets securitisation have not been taken into account.

Metrics	Overview	Basis for calculation
DSO (Days sales outstanding)	DSO is a measure of the average number of days that a company takes to collect cash after the sale of goods or services have been delivered.	Accounts receivable/sales x 365
DIO (Days inventories on hand)	DIO gives an idea of how long it takes for a company to convert its inventory into sales. Generally, the lower (shorter) the DIO, the better.	Inventories/cost of goods sold x 365
DPO (Days payables outstanding)	DPO is an indicator of how long a company takes to pay its trade creditors.	Accounts payable/cost of goods sold x 365
NWD/NWC days (net working capital in days)	NWC days indicates the length of time it takes a company to convert resource inputs into cash. This is commonly referred to as the Cash Conversion Cycle (CCC).	DSO + DIO – DPO
NWC % (net working capital %)	NWC % measures working capital requirements relative to the size of the company.	(Accounts receivable + inventories – accounts payable)/sales
Investment rate	Investment rate measures the amount of investment relative to the revenues of a company.	Capital expenditure/sales
EBITDA margin	EBITDA margin is an indicator of a company's profitability level as a proportion of its revenue.	EBITDA/sales

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