

Cash for Growth

Working Capital in the Manufacturing Sector

Sector Analysis, 2014



Foreword



Joel Segal
Partner –
Industrial Products and
Services Leader

Welcome to PwC's Working Capital Survey of the manufacturing sector.

Working capital is the life blood of every company and is a barometer for how freely cash flows. In efficiently run businesses, cash runs freely; in others, cash gets trapped in working capital, restricting the company's ability to grow. This is particularly true for manufacturing companies, as these are capital intensive and more sensitive to economic swings.

In this survey we look at how companies have performed and what the key trends are around the globe and across sectors. We are working with many companies to help them optimise their working capital and achieve sustainable performance improvements.

This study shows that working capital continues to present a significant opportunity for releasing cash and should therefore receive special attention as companies seek to take full advantage of the global economic upturn.





Executive summary

Working capital can deliver cash today, for growth tomorrow



Daniel Windaus
Partner – Working
Capital Management

Globally, the largest companies within the manufacturing sector have experienced a challenging trading environment over the past two years, which has been highlighted by declining revenues.

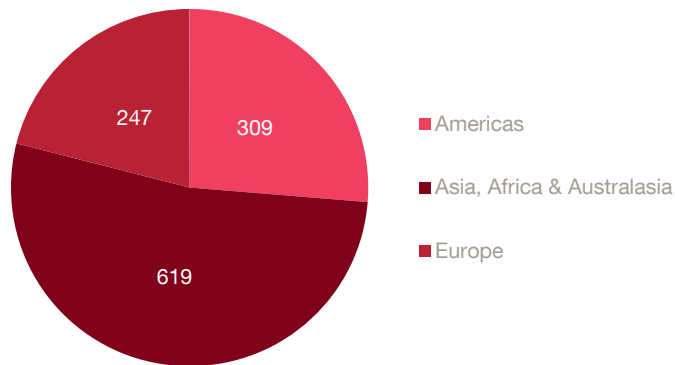
This recent trend has put pressure on companies to proactively manage their cash position, causing ‘cash management’ to feature further up the corporate agenda for the first time since the economic recession.

This increased focus has already translated into working capital improvements, with the first decrease in days working capital since 2009. Improved inventory management has been the key driver of this trend. However, working capital performance varies widely across the industry, with good performers getting better and bad performers getting worse.

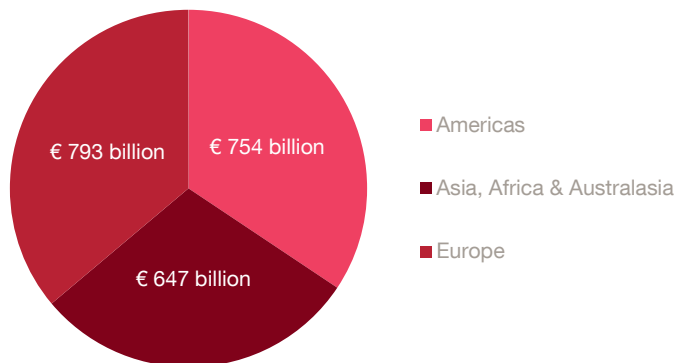
To return to the levels of revenue growth achieved in 2010 and 2011, companies need to invest in their future, which will require significant extra cash over the next few years. Our survey shows that if companies were to move to the next performance quartile, they would generate a total of €100bn of cash, while moving to upper quartile performance would release €162bn of cash. Cash is at your finger-tips.

Whilst revenue growth has stalled in recent years...

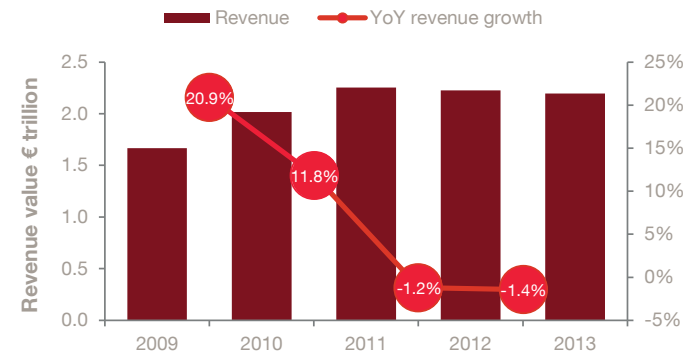
Number of companies in the study



Number of companies in the study



Total global revenue in the manufacturing sector



Sales for the largest 1,175 companies in the manufacturing sector grew by 32% over the past four years equivalent to a Compound Annual Growth Rate (CAGR) of 7%. This was achieved in 2010 and 2011 following the start of the financial crisis. However, over the past 2 years revenue has decreased with a CAGR of -1.3% since 2011.



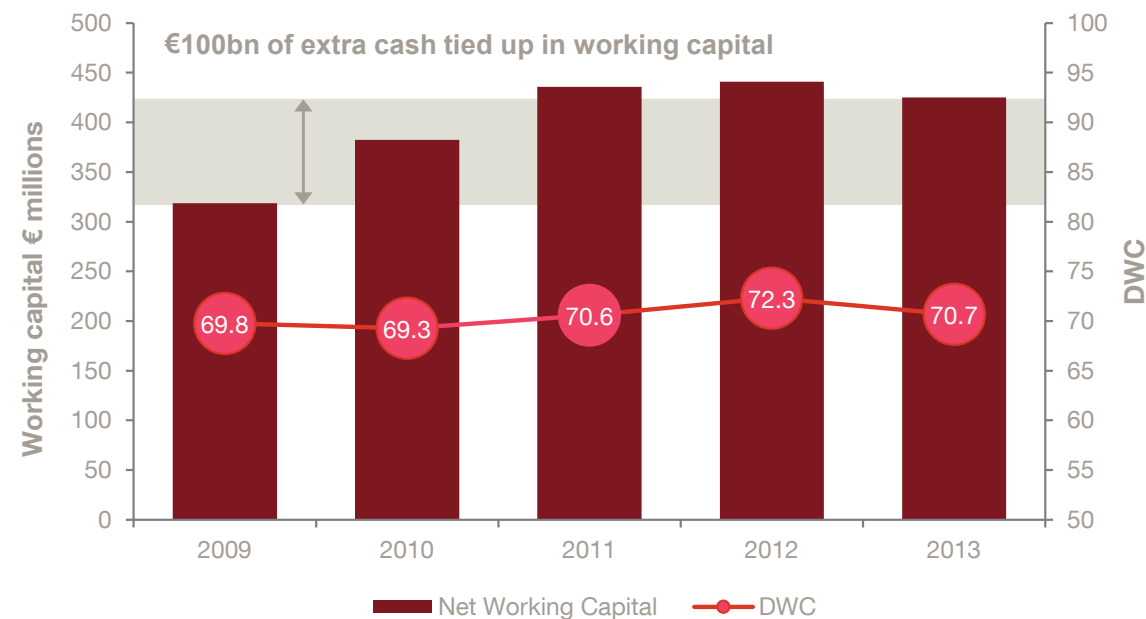
... companies have focused on improving working capital performance as a source of cash

Working capital performance across the sector has improved by 2.2% during the past year. Despite this, an additional €100bn has been trapped in working capital across the industry compared to 2009.

Since 2010, working capital performance has steadily deteriorated with first signs of improvement becoming visible over the past year. This suggests that cash is returning to the fore-front of companies' agendas once again.



Manufacturing sector working capital trend



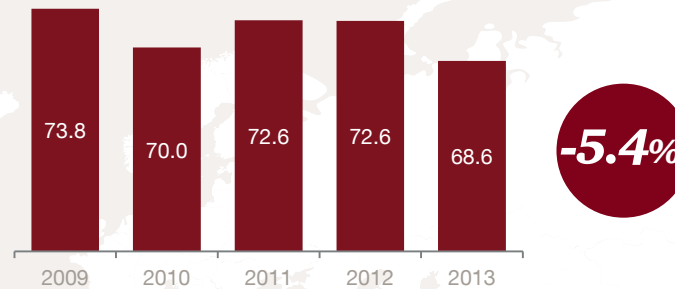
€100bn
increased
working capital

2.2%

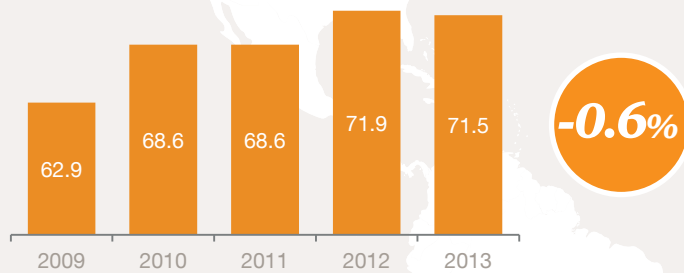
decrease in days
working capital
between 2012 and
2013

Working capital performance has improved in all regions, with Europe achieving the greatest development

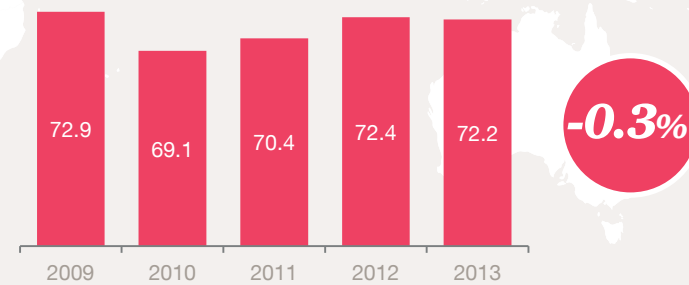
Europe



Americas



Asia, Africa & Australia

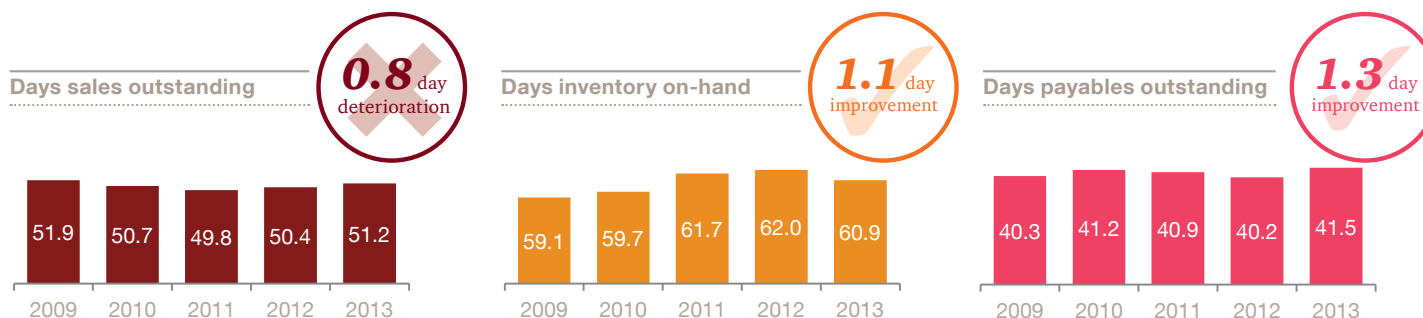


Key

- Days of working capital
- Percentage change between 2012 and 2013

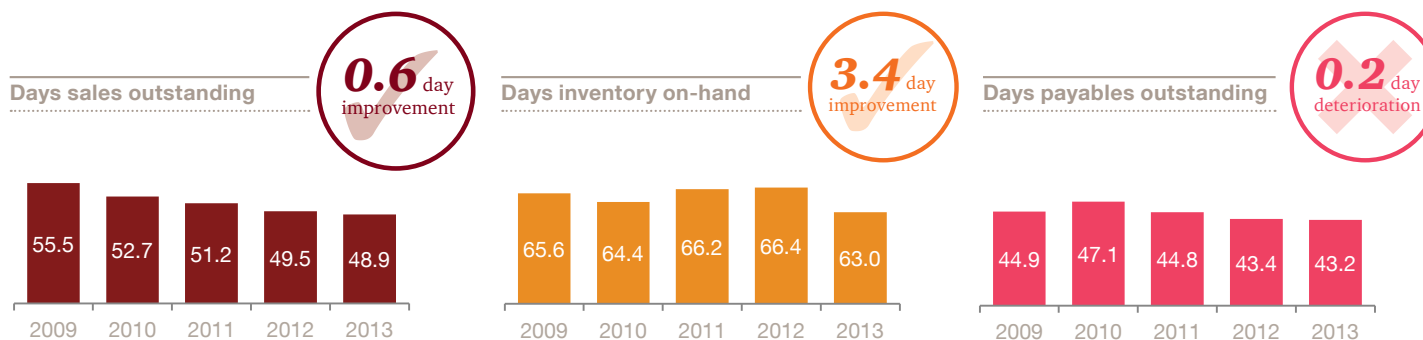
Inventory has been a key driver of improvement, particularly in Europe

Global working capital performance



Working capital performance has improved by 1.6 days globally between 2012 and 2013. The primary drivers of the trend are improvements within the inventory and payables cycles.

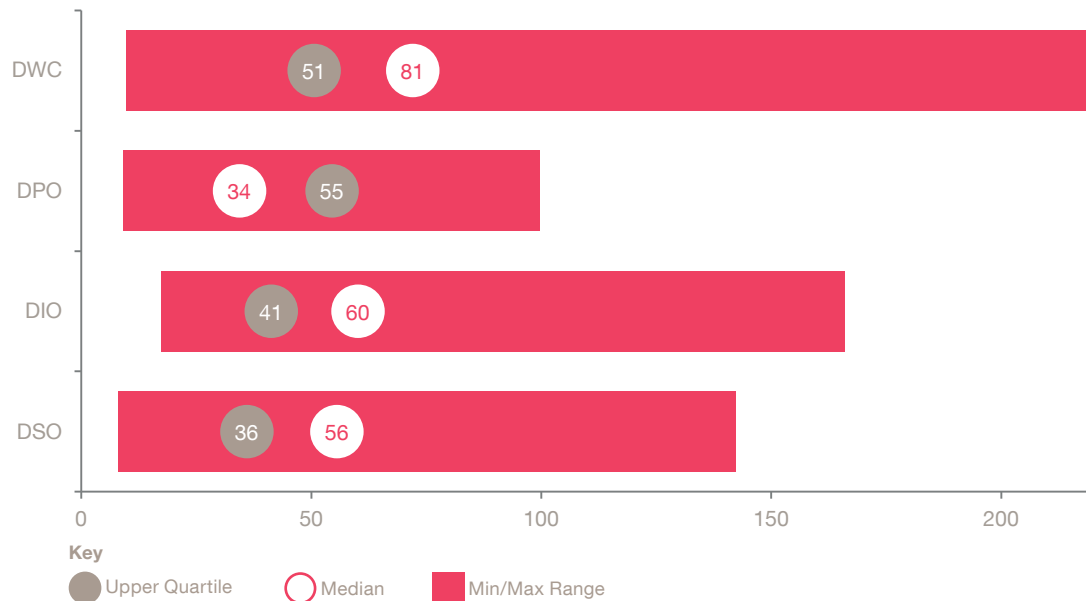
European working capital performance



European companies have achieved an even more notable improvement of 3.8 days over the past year. Enhanced inventory performance was the key driver of the trend. Payables performance has deteriorated, showing a 4-year declining trend.

Performance varies widely within the industry...

Working capital performance range



Working capital performance ranges widely across the manufacturing sector, with a median of 81 days.

Notably, the variance between days payables outstanding and days sales outstanding is low, which causes a relatively high level of cash to be trapped in working capital across the industry.

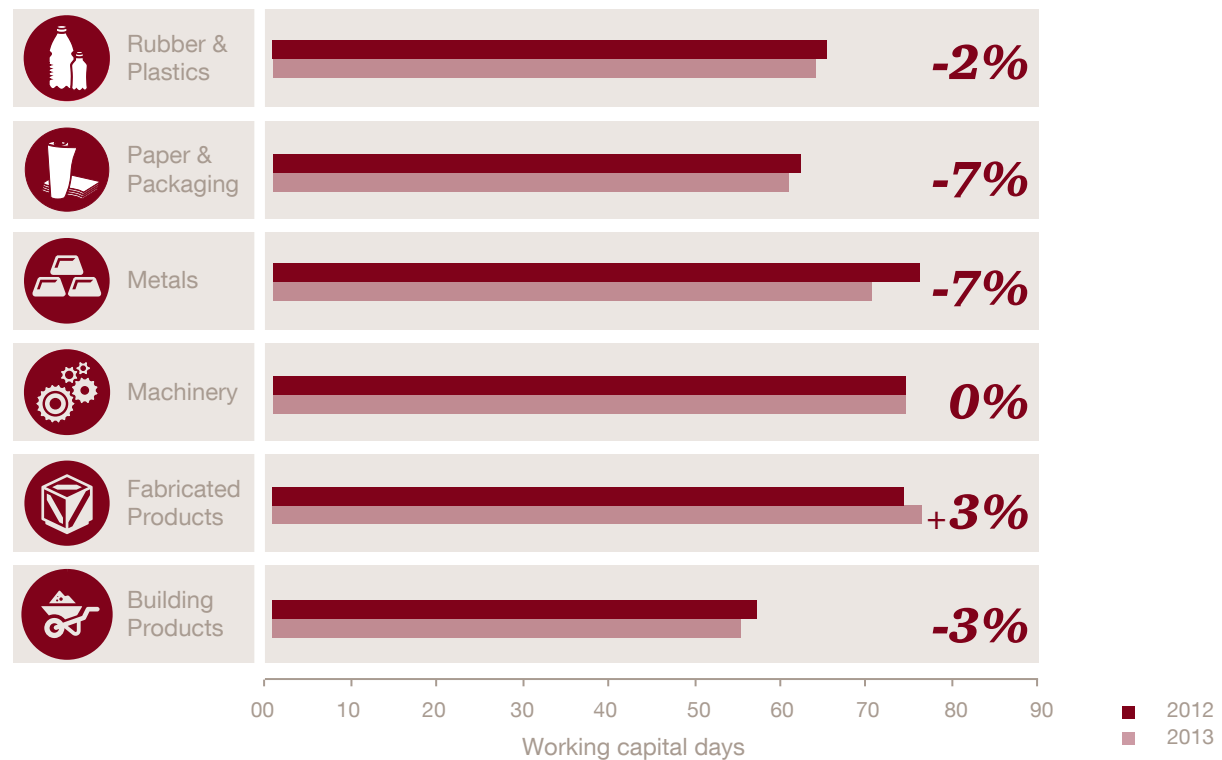
As highlighted by the top performers in each cycle, there is room for improvement across the sector.



... which is partly caused by the mix of sub-sectors



Change in days working capital between 2012 and 2013



Varying working capital performance across sub-sectors is one of the drivers of the wide performance gap in working capital cycles.

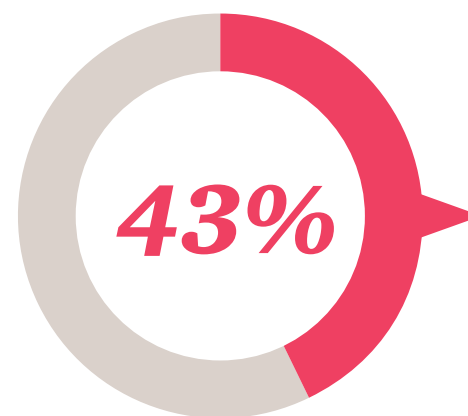
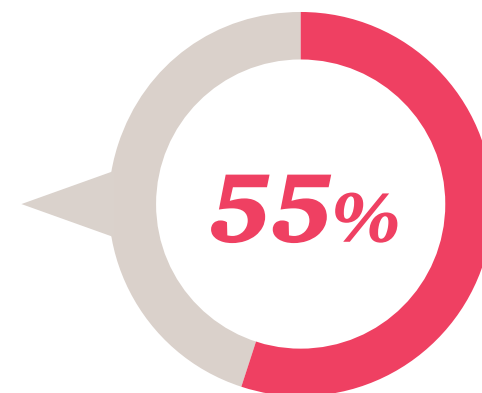
The Metals and Paper & Packaging sectors have achieved the greatest improvement over the past year, whilst Building products remains the best performing sub-sector within the industry.

The good getting better, and the bad getting worse



The leaders

55% of companies with days working capital above the industry median have improved their performance over the past year.



The laggards

Only 43% of those performing below the median improved.

In addition, 10% of companies operating below the industry median deteriorated by more than 40 days, whilst this was only 2% for those operating above the industry median.

Globally, €100bn to €162bn of cash could be released from working capital in the manufacturing sector



How can we support you?

1. Complete a working capital benchmarking exercise to compare performance against peers and identify potential improvement opportunities.

2. Perform a diagnostic review to identify 'quick wins' and longer-term working capital improvement opportunities.

3. Develop detailed action plans for implementation to generate cash and make sustainable improvements.

4. Assist the realisation of sustainable working capital reduction by implementing robust, efficient and collaborative processes.

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 service.



Examples of areas where PwC could help you to release cash from working capital

Cash culture & visibility – The aim is to create a culture whereby cash is important & performance is clearly visible

Key cash driver focus areas:

- Cash related management incentives
- Top management sponsorship
- Clear roles & accountability's
- Corporate Working capital framework
- Defined targets per division / country
- Working capital reporting dashboards by division / country

Accounts receivable

- Credit risk policies
- Billing timeliness and quality
- Systems-based dispute resolution
- Dispute root cause elimination
- Good contract management (for large scale project type businesses)
- Aligned and optimised customer payment terms across global customer base
- Timely order entry & order processing
- Formalised collections strategy with tailored and proactive collections approach
- Dispute management process to avoid/minimise queries resulting from complex products, variants portfolio, and payment delays

Accounts payable

- “Centre Led” procurement
- Consolidated spending
- Supply Chain Finance
- Purchasing channels (to avoid contract leakage)
- Payment method and frequency
- Early payment prevention
- Supplier payment terms standardisation and optimisation programmes across global supplier base
- Improved visibility of cash/cost trade offs across the supplier base to enable conscious optimal decision making
- Assistance with establishment and optimisation of supply chain finance programmes (through an association with an independent finance provider)

Inventory

- Balanced cash, cost and services
- Lean and agile supply chain strategies
- Global manufacturing footprint
- Sales and operations planning (S&OP)
- Demand management and forecasting techniques
- Production planning and batch size optimisation
- Accurate tracking of inventory quantities
- Differentiated inventory segmentation per product group
- Standardisation of components
- Extended supply chain integration
- Collaborative replenishment strategies
- Transport and installation lead time compression
- Maintenance, repair and overhaul inventory optimisation

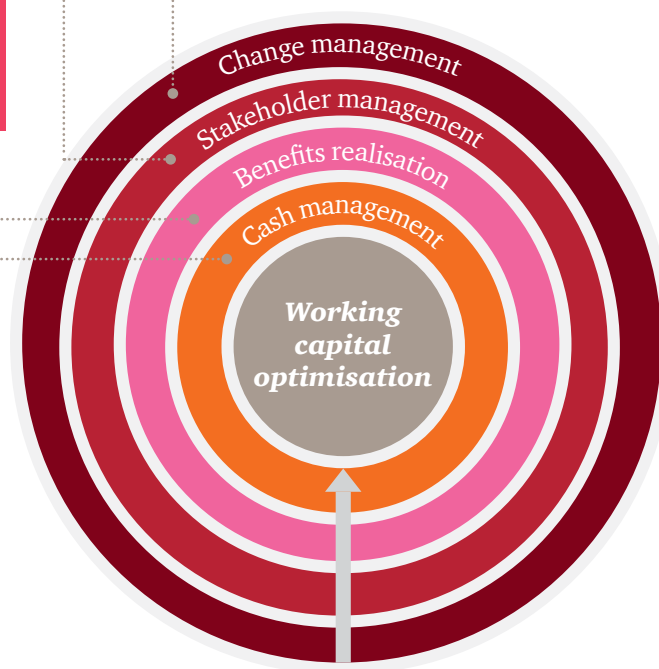
Our approach to sustainable working capital

Change management – Establish a more cash focused culture that is able to sustain the higher levels of performance and drive continuous improvement.

Stakeholder management – Ensure that key stakeholders remain engaged during the project.

Benefits realisation – Ensure that cash generation objectives are achieved and maintained.

Cash management – Ensure effective utilisation and forecasting of cash.



We supplement our working capital and cash management methodologies with core consulting approaches to make sure that improvements are tangible and sustainable.

Case study: Operational working capital improvement programme for a wind turbine group

The key issue

The company was struggling to cope with lower demand and increased competition in their industry. They were facing mounting debts and a profit warning saw the company's share price drop sharply. As a consequence, the company were facing severe liquidity problems.

How we helped

After a restructure, we identified that cash targets were missing. Our team worked with the company to assess their working capital improvement potential and to investigate how the introduction of a cash-focussed culture could be elevated on the agenda.

We performed a total working capital diagnostic review, including procure to pay (creditors), forecast to fulfil (inventories) and order to cash (debtors). This identified c €1bn of benefit potential.

Our fast pace approach was essential to raise organisational awareness to poor cash performance and raise receptiveness to change behaviours.

This comprehensive six month programme was sponsored by the executive board, with a focus on the core markets across Europe and North America, with the objective to realise €1bn of working capital improvement and deliver the cash benefits over a period of three to six months.

The result

We identified and delivered net working capital cash benefits close to €1bn.

Over a 6 months period the benefits were realised by improving procure-to-pay (creditors), improving order-to-cash (debtors) and reducing inventories.

Financial results for Q2 2013, as a consequence of the project, delivered negative working capital, and the announcement coincided with the company's share price rising sharply over six months.



PwC's Working Capital Management Group brings together experienced practitioners from across the world. Our people have many years of experience at delivering world class working capital performance both as consultants and from time spent in industry.

To find out more, please go to www.pwc.com/workingcapital

For other sector-specific working capital studies, please contact Daniel Windaus.

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