All tied up

Working capital management report 2016

EY
Building a better working world

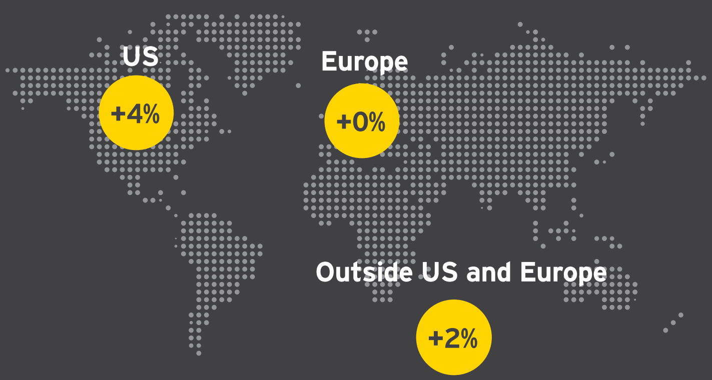
Foreword

All tied up 2016 is the ninth annual publication in a series of working capital (WC) management reports based on EY research, reviewing the WC performance of the world's largest companies.

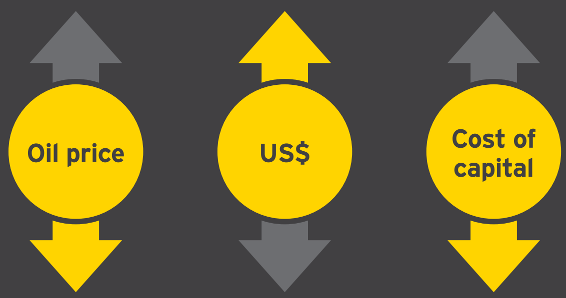
The survey focuses on the top 2,000 companies in the US and Europe, examining their WC performance at a company, regional, industry and country level. It also provides insights into the WC performance of another 2,000 companies in seven other regions and countries. In addition, this report sets out the findings of a review comparing the WC performance of small and medium-sized enterprises (SMEs) with that of large companies.

Key findings 2015 vs. 2014

Change in C2C:

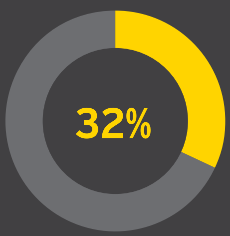


Prime WC drivers:



WC gap performance:

32% SMEs' C2C premium over large companies'



Cash opportunity:

US$1.2t excess WC for leading US and European companies

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Executive summary

A review of WC performance among the largest companies in the US and Europe reveals a deterioration in the US and a relative stability in Europe. For the US companies analyzed, C2C[1] increased by 4% from its 2014 level, after a decrease of 3% in the previous year. For Europe, this year's stable performance contrasts with the progress made the year before, when C2C fell by 2%.

However, if the oil & gas and metals and mining industries are excluded from our analysis, WC performance would have improved in both regions in 2015, with a reduction in C2C of 1% in the US and 2% in Europe.

Companies outside the US and Europe fared worse in 2015. Six out of seven regions and countries analyzed reported an improvement in WC performance, but only three showed better year-on-year results if we exclude the O&G and M&M industries.

Interestingly both SMEs and large companies performed similarly in 2015.

Overall, our research findings suggest that most companies continue to have huge opportunities to improve in many areas of WC. A high-level comparative analysis indicates that the leading 2,000 US and European companies may have as much as US$1.2 trillion in excess WC, over and above the level they require to operate their business model efficiently and meet all their operating requirements. This figure is equivalent to nearly 7% of their combined sales. In other words, for every US$1billion in sales, the opportunity for WC improvement is, on average, US$70m.

Yet while some benefits may still be available through relatively simpler steps, such as improving billing and cash collections or extending supplier payment terms, most companies seeking further gains will need to embrace more substantial and sustainable changes in the way they do business and manage their WC.

To achieve this, the changes required will include:

- Ensuring that WC remains a strategic focus throughout the year, with the whole business engaged and incentivized to drive improvement
- Ensuring that the organization is sufficiently responsive to change, with lean and agile manufacturing and supply chain solutions deployed for different products or market segments, as well as enhancing responsiveness through cross-functional cooperation and effective collaboration between participants in the extended enterprise
- Ensuring that supply chains are resilient, through robust risk management policies, alternative sourcing, and enhanced visibility across the end-to-end supply chain
- Ensuring that strong discipline in terms and transactions, internal controls over cash and WC, and appropriate performance measures are in place
- Ensuring that the complex and evolving trade-offs between cash, costs, delivery levels and the risks that each company must take are clearly understood and properly managed.

1 C2C: cash-to-cash

US and Europe

WC performance improvement in the US and Europe

A review of WC performance among the largest companies in the US and Europe reveals a deterioration in the US and a relative stability in Europe.

For the US companies analyzed, C2C increased by 4% from its 2014 level, after a decrease of 3% in the previous year. For Europe, this year's stable performance contrasts with the progress made the year before, when C2C fell by 2%.

However, if the oil & gas and metals and mining industries are excluded from our analysis, WC performance would have improved in both regions in 2015, with a reduction in C2C of 1% in the US and 2% in Europe.

Table 1. Change in WC metrics by region, 2014-2015

C2C change 15/14

	US	Europe
DSO	0%	-1%
DIO	+5%	+1%
DPO	+1%	0%
C2C	+4%	0%

C2C change 15/14 excl. O&G and M&M

	US	Europe
DSO	-2%	-2%
DIO	+1%	-1%
DPO	+1%	-2%
C2C	-1%	-2%

Source: EY analysis, based on publicly available annual financial statements

Note: DSO (days sales outstanding), DIO (days inventory outstanding), DPO (days payable outstanding) and C2C (cash-to-cash), with metrics calculated on a sales-weighted basis

For the US, each WC component contributed to the improvement in overall WC performance in 2015, with DSO and DIO down 2% and 1%, respectively, and DPO up 1%. Europe's better results came from a higher DPO (up 3%), partially offset by an increase in DIO and DSO (both up 1%).

For each region, a number of factors, some of them operating in conflict with one another, can explain these WC trends. They include:

Contrasting economic conditions: For both the US and Europe, WC results for 2015 have continued to be affected by the impact of contrasting economic conditions during the year, as well as by sharp variations in both exchange rates and commodity prices. Compared with 2014, overall sales growth for leading companies in the US was down 3%, while up by 1% for Europe.

Impact of commodity prices: The sharp fall in commodity prices during 2015 significantly influenced overall WC performance. The O&G and M&M industries account for 13% of total sales in Europe and 8% in the US.

Exchange rates movement: Movements in US dollar exchange rates also played some part in driving the industry's WC performance in 2015. For companies reporting in euros and in Swiss Francs, the weakness of those currencies against the US dollar compared with its average level during the year was a positive contributory factor. In contrast, for companies reporting in US dollars, the strength of the US dollar against all major currencies at the end of the year had a negative impact.

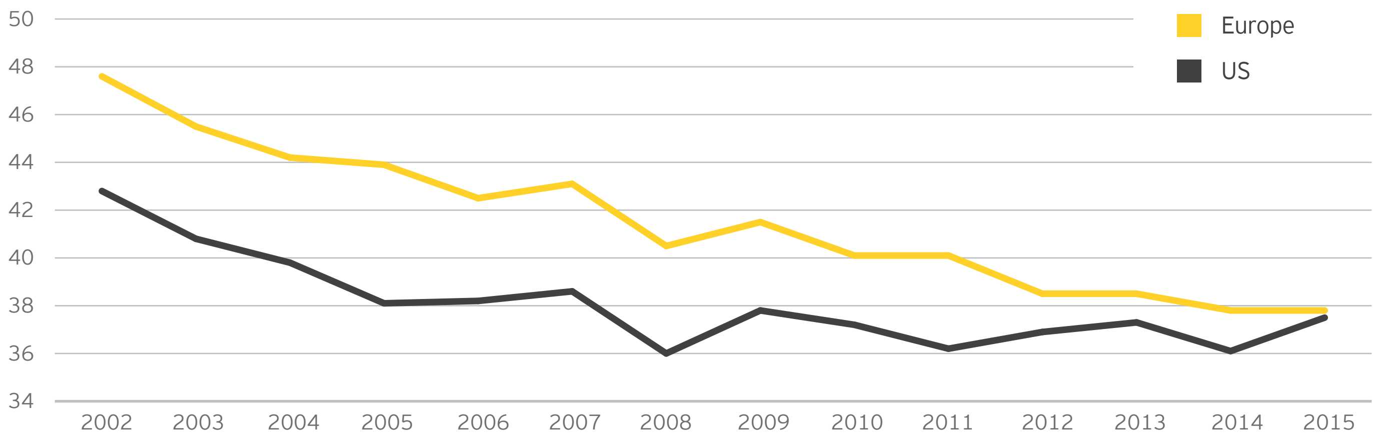
Continued attention to WC management: Many companies in the US and Europe have continued taking steps to drive cash and cost out of WC, in an effort to grow their returns on capital and increase cash returns to shareholders. In some cases, these activities have been prompted by increased pressure from shareholders, including some activists.

Initiatives have focused on streamlining manufacturing and supply chains, collaborating more closely with customers and suppliers, managing payment terms for customers more effectively and improving billing and cash collections. In addition, extending supplier payment terms and driving greater efficiency in procurement and payables processes, along with simplifying functions and processes have made a contribution to better management of WC.

Changes in trade-offs between cash, costs, delivery levels and risks: As carrying WC became much less costly during the year following the decrease in the cost of capital, a number of companies in the US and Europe may have also chosen in 2014 to trade off WC improvements against sales growth, margin expansion, or increased provision of financing solutions to their suppliers and customers.

Competing WC strategies: With many industries trading with each other, change in WC performance is also the net result of industries' competing and conflicting WC strategies. As one company is trying to collect its receivables, its customers are trying to stretch out their payment terms. As one tries to push back supplies, its suppliers are trying to sell and ship more products as fast as possible.

Table 2. WC performance for the US and Europe, 2002–2015



Source: EY analysis, based on publicly available annual financial statements

The results for 2015 bring the total reduction in C2C achieved since 2002 to 12% for the US and 21% for Europe. Each of the WC components contributed to this improved performance. In the US, DSO fell by 9%, while DPO rose by 7%. Conversely DIO was up 3%. In Europe, DSO and DIO dropped by 12% and 2%, respectively, while DPO was up 7%.

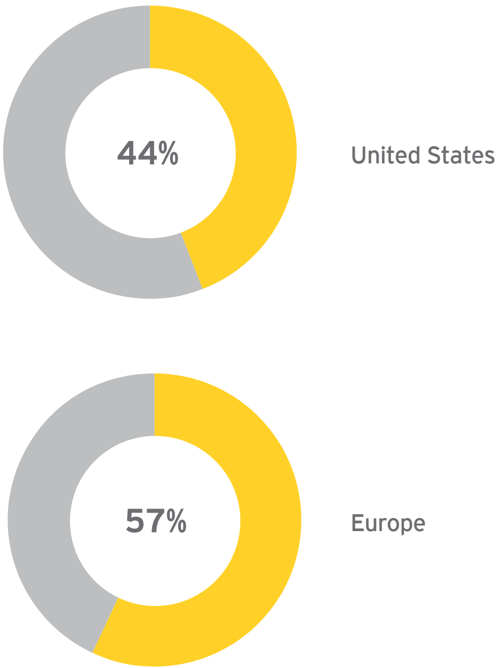
Company performance review

A majority of US companies reported a deterioration in WC performance, while a majority of those based in Europe showed an improvement.

In the US, only 44% of the companies included in our research reported an improvement in WC performance in 2015, compared with 2014. A high proportion of companies reported weaker performance in both inventory and payables in 2015 (57% and 53%, respectively). There was a similar number of companies showing a year-on-year increase or decrease in DSO.

In Europe, 57% of companies reported an improvement in WC performance in 2015 compared with 2014. As much as 62% and 58% of companies posted better results in receivables and inventory, respectively in 2015. These more than offset the number of those showing weaker payables performance (56%).

Table 3. Proportion of companies showing improved C2C performance, 2015 vs. 2014



Source: EY analysis, based on publicly available annual financial statements.

Industry performance review

In 2015, there were wide variations in the level and direction of changes in C2C between various industries across the US and Europe, partly reflecting the impact of contrasting economic growth patterns and movements in commodity prices and exchange rates during the year.

The O&G and M&M industries reported significant changes in C2C, largely as a result of falling commodity prices during 2015. In the US, C2C more than doubled from 7 days to 15 days on sales down 35%. In Europe, the increase in C2C was moderate at 2% on sales down 21%.

For the pharmaceutical industry, the results in 2015 show a deteriorating WC performance compared with 2014. Their C2C was up 2%, after dropping by 4% the year before. This weaker WC performance overall in 2015 was driven by a further deterioration in inventory performance, with DIO up 2%. Performance in receivables was also poorer, with DSO up 1%. The improvement in payables performance seen in previous years came to a halt.

For automotive suppliers, change in year-on-year C2C was mixed, with an increase of 10% for the companies based in the US but a decrease of 2% for those in Europe.

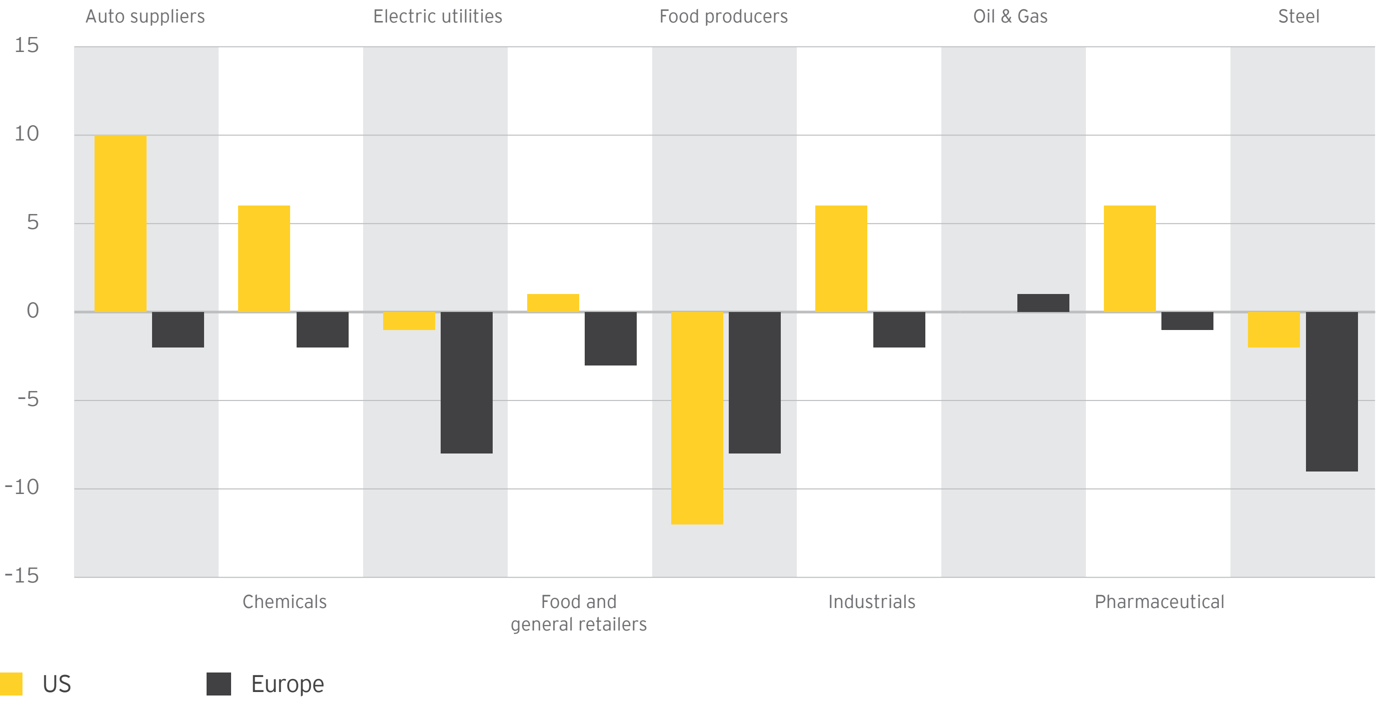
These variations in the degree of change in C2C between different regions reflect companies' different responses to challenges, including diverging regional automotive production patterns, continuing pricing pressures from OEMs, an ongoing shift in global demand towards rapidly-growing markets and volatility in commodity prices and exchange rates.

Food producers delivered a further significant improvement in WC performance in 2015, with C2C down 8% and 12%, respectively in the US and Europe from its levels of 2014. Progress came from better receivables and inventory performance in both regions. In addition, companies based in the US reported better results in payables, primarily driven by a further extension in payment terms, as well as by greater efficiency in procurement and payables processes.

For chemicals and industrials, WC results diverged between both regions. Performance deteriorated for companies in the US, but improved for those in Europe.

For electric utilities, WC performance in 2015 was heavily influenced by the impact of falling energy prices during the year. C2C decreased by 1% in the US and 8% in Europe.

Table 4. Most significant WC changes among major industries, 2015 vs. 2014



Source: EY analysis, based on publicly available annual financial statements

Regional and country performance review

US vs. Europe performance comparison

The WC performance gap between the two regions has narrowed significantly in 2015, partly due to the impact of commodity prices and exchange rate movements.

However, a degree of caution is required when comparing WC performances in the US and Europe. Since some of the business done by North American and European companies takes place outside their home regions, their WC results reflect global market conditions to some degree, as well as conditions in the regions where they are based.

The US exhibit slightly lower levels of WC compared with European-based companies. Overall C2C for the US in 2015 was only 0.4 days below that of Europe (0.6 days excluding the O&G and M&M industries). This was primarily due to a strong performance in inventory (with a DIO 2.7 days, or 10% below). The differential between receivables and payables cycles (DSO – DPO) across both regions was 2.3 days, with the effect of generally longer trade terms in Europe than in the US being mitigated at the net level. The wide variations in trade terms between Northern and Southern Europe should be noted, however.

There are many possible causes for the differences in WC metrics between the US and European regions: companies in Europe tend to have more SKUs (Stock Keeping Units) to serve different markets and customers in different currencies, while the US benefits from the absence of national borders and a unique trading currency. Transport also takes longer and logistics costs are higher in Europe than in the US.

Table 5. WC changes by European sub-region and country, 2015 vs. 2014

	US	Europe
DSO	38.2	49.3
DIO	31.4	34.1
DPO	32.1	45.6
C2C	37.4	37.8

Source: EY analysis, based on publicly available annual financial statements

European country performance comparisons

In Europe, each sub-region and country except the UK (and Southern European countries had the O&G been excluded from our calculation) reported an improvement in WC performance.

Of the seven main sub-regions and countries in Europe, the UK was the only one reporting worse WC results in 2015 compared with 2014. Its C2C increased by 6%, wiping out the entire gain registered in the year before when the country significantly outperformed its peers. Had the O&G been excluded from our calculations, the deterioration in performance would have been more limited (C2C up 3%). These weaker results came from a combination of higher DIO and DSO (up 6% and 4%, respectively), partly offset by higher DPO (up 4%).

In contrast, France and Germany managed to report a reduction of 2% in C2C. Both countries achieved progress in receivables, while performance was mixed in inventory and unchanged in payables. In France, electric utilities, industrial companies and telecommunications operators all reported an improvement in WC performance. In contrast, food producers scored poorly. In Germany, chemical, electric utilities, industrial companies and automotive suppliers all achieved strong progress. Conversely, industrial companies saw weaker results.

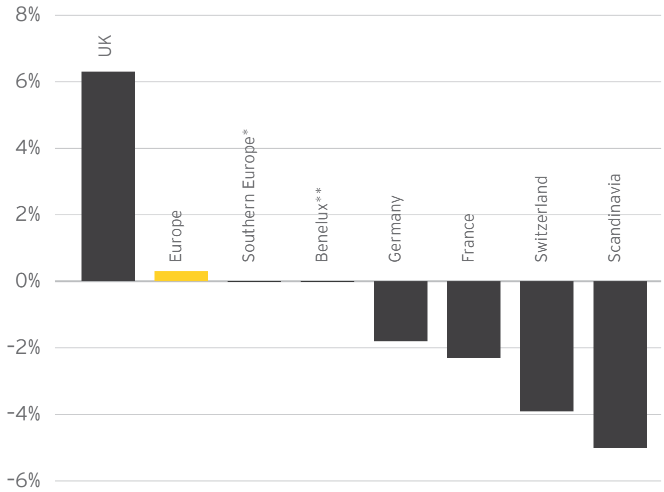
Benelux reported a flat WC performance in 2015, but a significant improvement had the O&G been excluded from our calculation. There was a strong showing from consumer products and food retailing.

For the Nordic countries, WC performance remains heavily skewed toward the performance of certain industries. For example, had the oil industry been excluded from our calculations, the reduction in C2C for this sub-region would have been limited to 2% instead of 7%. Strong results were achieved by telecommunications equipment and paper & forestry companies.

Switzerland reported a fall of 5% in C2C, benefiting from the strong performance of one major food company which accounted for one-quarter of the country's total sales. The two largest pharmaceutical companies reported diverging results.

For the Nordic and Southern European countries, WC performance continues to be heavily skewed toward the performance of certain industries. The Nordic countries reported good results (C2C down 5%), helped by the performance of electric utilities, and industrial and paper & forestry companies. In contrast, Southern European countries registered a flat performance, but a significant deterioration had the O&G been excluded from our calculation. Electric and gas utilities as well as telecommunications operators scored particularly poorly.

Table 6. WC changes by European sub-region and country, 2015 vs. 2014



Source: EY analysis, based on publicly available annual financial statements

* Greece, Italy, Portugal and Spain;
** Belgium, Luxemburg and Netherlands

Opportunity for improvement

The wide variations that our research reveals in WC performance between different companies in each regional industry point to significant potential for improvement — amounting to an aggregate of up to US$1.2 trillion of cash for the leading 2,000 US and European companies.

This range of cash opportunity is defined as the sum of the WC cash opportunity derived for each company. This has been calculated by comparing the 2014 performance of each of its WC components with that of the average (low estimate) and the upper quartile (high estimate) achieved by its industry peer group.

On this basis, the 1,000 US companies included in this research would have in total between US$375 billion and US$680 billion of cash unnecessarily tied up in WC. That is an amount equivalent to between 12% and 21% of their WC scope (defined as the sum of trade receivables, inventories and accounts payable) and between 3% and 6% of their aggregate sales.

The 1,000 European companies would have in total between €280 billion and €480 billion of cash unnecessarily tied up in WC, equivalent to between 11% and 19% of their WC scope and between 4% and 7% of their aggregate sales.

In total, the leading 2,000 US and European companies would have up to US$1.2 trillion of cash unnecessarily tied up in WC, equivalent to nearly 7% of their aggregate sales. This figure is similar to last year's.

Our "cash potential" analysis reveals that the opportunity is distributed across the various WC components, with 35% available from both receivables and payables and 30% from inventory.

The reported figures for the cash opportunity should be treated with a degree of caution, as they are based on an external view of each company's WC performance within its industry (based on public consolidated numbers). The top end of each range is likely to be ambitious, as it ignores differences in commercial strategies (impacting cash discounts and payment terms), customer base, supply, product mix, country sales exposure and local practices for payment terms, which can vary widely, especially across Europe. The consolidated figure would also be lower if intra-company benefits were excluded. On the other hand, the opportunity is calculated for each company's WC component by comparing its performance not against the best performer, but against the top quartile of its industry peer group.

Table 7. WC cash opportunity, 2015

Region	Cash opportunity					
	Value		% WC scope*		% sales	
	Average	Upper quartile	Average	Upper quartile	Average	Upper quartile
Europe	€280b	€480b	11%	19%	4%	7%
US	US$375b	US$680b	12%	21%	3%	6%

*WC scope = sum of trade receivables, inventories and accounts payable

Source: EY analysis, based on publicly available annual financial statements

Other regions and countries

Improvement in WC performance in 2015

Companies based in the other seven regions and countries (Asia; Australia & New Zealand — Aus/NZ; Canada; Central and Eastern Europe — CEE; India; Japan; and Latin America — LatAm) covered by our survey reported a deterioration in WC performance in 2015 compared to 2014, with C2C rising by 2%.

It is worth noting that if we exclude the oil & gas and metals & mining industries (O&G and M&M which accounted for 23% of total sales in 2015) from our calculations, C2C would have increased by 3%.

Last year's weaker WC performance was due to a poor showing in receivables (DSO up 2%), partly offset by better results in inventory (DIO down 1%). Performance in payables remained unchanged. Excluding the O&G and M&M industries, there was a deterioration in performance for both receivables and inventory (DSO and DIO up 2% each), partly offset by better results in payables (DPO up 1%).

In 2015, six out of seven regions and countries posted an improvement in WC performance compared with 2014. Only Japan scored worse. However, if we exclude the O&G and M&M industries, only three regions and countries showed better year-on-year results.

More specifically, within the Asian and LatAm regions, there were wide variations between countries in the degree of year-on-year change in C2C.

Table 8. Change in C2C, 2014–2015

Regions and countries	2015	Change 15/14
Asia	35	-1%
Aus/NZ	25	-5%
Canada	25	-2%
CEE	39	-1%
India	44	-1%
Japan	63	3%
LatAm	22	-13%
Other Regions	42	2%

Table 9. Change in C2C excluding the O&G and M&M industries, 2014–2015

Regions and countries	2015	Change 15/14
Asia	40	1%
Aus/NZ	25	-8%
Canada	30	-3%
CEE	44	1%
India	66	1%
Japan	64	3%
LatAm	25	-4%
Other Regions	48	3%

Table 10. Change in C2C per Asian country, 2015 and 2014

Asia	2015	Change 15/14
China	12	-20%
Indonesia	82	-5%
Malaysia	55	5%
Singapore	66	7%
South Korea	64	3%
Taiwan	38	9%
Thailand	21	-13%
C2C	35	-1%

Table 11. Change in C2C per Asian country excluding the O&G and M&M industries, 2015 and 2014

Asia	2015	Change 15/14
China	6	-35%
Indonesia	84	-5%
Malaysia	55	5%
Singapore	74	8%
South Korea	66	4%
Taiwan	38	11%
Thailand	32	-10%
C2C	40	1%

Source: EY analysis, based on publicly available annual financial statements

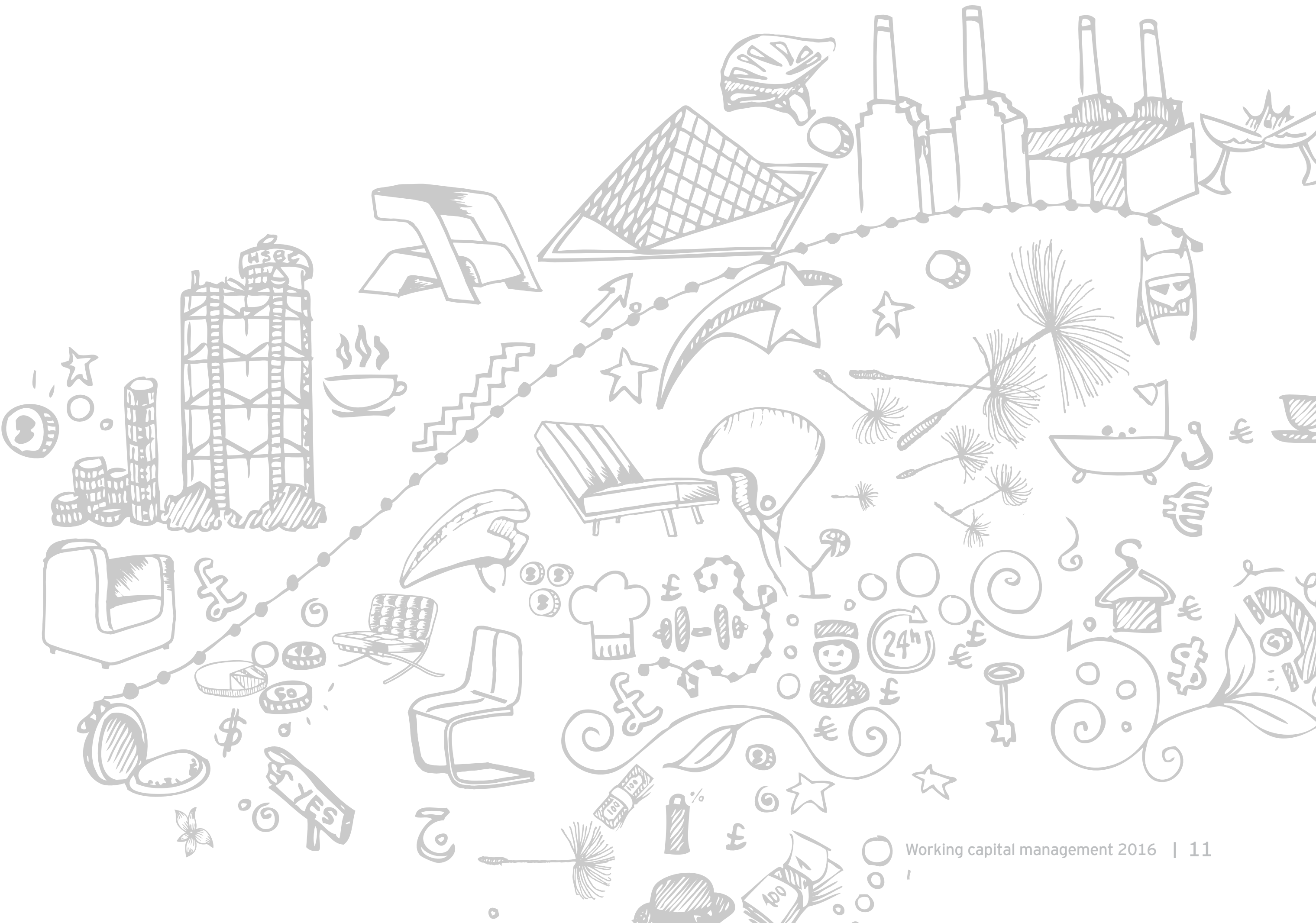
Table 12. Change in C2C per LatAm country, O&G and M&M industries, 2014–2015

LatAm	2015	Change 15/14
Argentina	6	-18%
Brazil	25	-9%
Chile	48	1%
Colombia	4	-69%
Mexico	8	-42%
C2C	23	-12%

Source: EY analysis, based on publicly available annual financial statements

Table 13. Change in C2C per LatAm country, excluding

LatAm	2015	Change 15/14
Argentina	11	22%
Brazil	24	1%
Chile	52	-1%
Colombia	11	60%
Mexico	14	-24%
C2C	26	-2%



Large distribution of WC performance

A review of the WC performance of the largest companies across other regions and countries reveals both significant variations overall and for each individual metric. These variations would have been even larger had the O&G and M&M industries been excluded from our calculations.

It is worth noting, however, that regional and country comparisons should be approached with a particular nuance in mind. Since some of the business carried out by top country-headquartered companies takes place outside their home regions, their WC results to some degree reflect global market conditions, as well as those in the regions where they are based.

Table 14. WC metrics by main region and country

	Asia	Aus/NZ	Canada	CEE	India	Japan	LatAm
DSO	44	39	39	46	47	69	35
DIO	36	37	31	34	45	42	32
DPO	44	43	44*	41	49	49	44
C2C	35	32	25	39	44	63	23
DSO – DPO	0	-4	nm	5	-2	20	-9

* includes accrued expenses

Table 15. WC metrics by main region and country, excluding the O&G and M&M industries

	Asia	Aus/NZ	Canada	CEE	India	Japan	LatAm
DSO	53	34	42	58	69	72	41
DIO	39	29	30	35	52	42	34
DPO	51	38	42*	50	54	50	49
C2C	40	25	30	44	66	64	26
DSO – DPO	2	-4	nm	8	15	22	-8

Table 16. WC metrics by Asian country

	China	Indonesia	Malaysia	Singapore	South Korea	Taiwan	Thailand
DSO	33	27	57	40	58	57	25
DIO	32	83	38	63	35	37	25
DPO	53	28	41	37	29	57	29
C2C	12	82	55	66	64	38	21
DSO – DPO	-20	-1	16	3	29	0	-4

Source: EY analysis, based on publicly available annual financial statements

Table 17. WC metrics by Asian country, excluding the O&G and M&M industries

	China	Indonesia	Malaysia	Singapore	South Korea	Taiwan	Thailand
DSO	53	26	57	43	61	58	29
DIO	36	86	38	70	35	37	37
DPO	83	27	41	39	30	58	34
C2C	6	84	55	74	66	38	32
DSO – DPO	-30	-1	16	4	31	0	-5

Table 18. WC metrics by LatAm country

	Argentina	Brazil	Chile	Colombia	Mexico
DSO	38	36	45	22	28
DIO	31	35	39	20	21
DPO	63	46	36	37	41
C2C	6	25	48	4	8
DSO – DPO	-25	-10	9	-15	-13

Table 19. WC metrics by LatAm country, excluding the O&G and M&M industries

	Argentina	Brazil	Chile	Colombia	Mexico
DSO	41	40	49	28	38
DIO	25	35	42	29	27
DPO	56	51	39	47	50
C2C	11	24	52	11	14
DSO – DPO	-15	-11	10	-19	-12

Source: EY analysis, based on publicly available annual financial statements

Looking at 2015 WC performance, India, Japan and CEE exhibit the highest C2C among these regions and countries, scoring particularly poorly in receivables and inventories. In contrast, Australia/New Zealand and LatAm carry the lowest C2C, thanks to strong results in receivables and inventories.

Japan also shows the highest differential between receivables and payables cycles (DSO vs. DPO), while Asia and Australia/New Zealand exhibit the lowest.

One point to note is that for Canada, DPO figures from a large number of companies are inflated (and therefore C2C deflated) by the inclusion of accrued expenses in the absence of detailed financial disclosure. Canada's DSO and DIO are among the lowest globally.

Factors behind the WC performance variations

Industry bias.
For some regions and countries, WC results are heavily influenced by the performance of certain industries. For example, the O&G and M&M industries represent as much as 44% and 42% of total sales of our sample of companies for India and CEE, respectively, but only 6% for Japan. Electric utilities and telecommunications services account for 16% of sales in Latin America, but for only 9% in Australia and New Zealand. Steel accounts for 8% and 5% of sales in India and Asia, respectively, but for only 1% in the US and 2% in Europe.

Payment practices.
Payment practices vary widely across and within regions and countries. Significant disparities in the length of payment delays and incidence of defaults can also be observed between regions and countries. While payment usage plays a role, these differences can also be explained by local behaviors, as well as by variations in the degree of effectiveness of credit management policies and legal enforcement procedures.

Logistics and distribution infrastructures.
The efficiency of logistics and distribution varies greatly across regions and countries, leading to significant differences in local supply chain costs, service levels and risks, as well as in WC performance.

According to the World Bank's 2014 ranking of logistics performance, developing countries have since 2007 been slowly catching up with the high-performers , but the logistics performance gap between the two groups remains wide. The US, most European countries and Japan are among the top 10 countries (out of 160), while the other Asian economies rank among the top quartile (with China being the 28th). Interestingly, India's position in the ranking has fallen in the past two years from being the 46th in 2012 to the 54th in 2014.

Focus on cash and effectiveness of WC management processes. There are fundamental differences in the intensity of management focus on cash and the effectiveness of WC management processes among these regions and countries. These variations partly reflect the commercial and industrial strategies deployed (with some businesses choosing to grow sales, increase investment or enhance service rather than improve WC performance for example), as well as differences in the degree of business and process maturity among companies.

WC comparisons among industries across regions and countries

An analysis of WC performance by industry across other regions and countries, and in comparison with the US and Europe, reveals substantial divergences, exacerbated by the impact of factors specific to each local industry.

For example, the WC performance of food producers in other regions is much weaker (with the notable exception of China and India) than in the US and Europe. As well as lacking the benefits of size, many of these companies deal with a dispersed customer base and operate comparatively inefficient supply chains.

The O&G industry also exhibits wide variations in WC performance between the different regions and countries, partly due to differences in business models, with companies operating at various points in the value chain. For example, O&G companies in Japan are mostly refiners, which carry much higher WC requirements than those involved in exploration & production.

Interestingly, machinery makers report high levels of WC across all regions and countries, reflecting the global nature of this industry.

Steel companies in both Asia and Australia/New Zealand carry the lowest levels of C2C, while their counterparts in CEE, LatAm and Japan display much higher levels.

In the case of telecommunications services, WC performance in individual regions and countries varies considerably, largely influenced by the distribution of revenues between fixed-line and mobile on one hand and between pre-paid and post-paid on the other hand, as well as by local payment practices, payment methods and levels of capital expenditure.

Table 20: WC metrics by industry across main regions and countries

C2C	Asia	Aus/NZ	Canada	CEE	India	Japan	LatAm	US	Europe
Automotive supplies	43	nm	33	78	50	64	59	40	55
Building materials	55	61	56	78	44	84	48	54	49
Chemicals	60	46	65	50	88	96	17	67	71
Electric utilities	32	20	10	48	57	25	18	33	24
Food producers	51	43	37*	49	59	67	36	34	28
Machinery makers	118	nm	120	nm	97	172	109	113	87
Oil and gas	17	23	-5*	27	6	43	12	11	20
Steel	60	54	79	127	40	85	85	72	69
Telecommunications	-54	41	2*	24	-43	52	0	12	-4

* includes accrued expenses

Source: EY analysis, based on publicly available annual financial statements

SMEs and large companies

The gap in WC performance between SMEs and large companies has remained stable in 2015, having widened in the previous year.

Compared with 2014, our 2015 study shows a similar increase of 2% in C2C for both SMEs and large companies. For SMEs, weaker WC results came entirely from a lower DPO (down 4%)., while both DSO and DIO remained unchanged. For large companies, the deterioration in WC performance was due to a higher DIO (up 3%), while both DSO and DPO remained unchanged.

Among both the SMEs and large companies included in our survey, there were a similar number of companies (57%) reporting increases in C2C. A majority of SMEs (53%) saw an improvement in receivables performance, but only a minority (47% and 43%, respectively) did so across both inventory and payables. Among large companies, there was a a similar number of companies reporting improvements and deteriorations in receivables performance, with a minority (47% and 42%, respectively) showing weaker performance in payables and inventory.

Table 21: Change in WC metrics for SMEs and large companies, 2014–15

C2C change 15/14

	SMEs	Large companies
DSO	0%	0%
DIO	0%	+3%
DPO	-4%	0%
C2C	+2%	+2%

Source: EY analysis, based on publicly available financial statements

SMEs have been only slightly closing the WC gap with large companies since 2005

A comparison between 2015 and 2005 shows SMEs reporting slightly higher C2C (+2%) over the intervening period, while large companies saw a bigger increase (+3%). This means that, since 2005, SMEs have been slightly closing the WC gap with large companies.

For SMEs, the deterioration in WC performance over the reviewed period has been the net result of a much lower DPO (down 12%) and a higher DSO (up 1%), more than offsetting a reduction in DIO (down 5%). For large companies, weaker results in C2C arose from much higher DIO (up 12%), partially offset by lower DSO (down 4%) and higher DPO (up 3%).
A variety of factors may help to explain these contrasting patterns of WC performance:

- Large companies have reported stronger receivables performance, benefiting from progress to improve billing and cash collections. For SMEs, a higher DSO probably reflects ongoing pressure from large customers to extract better payment terms.
- Large companies have managed to drive improvement in their payables performance, taking action to leverage spend and extend payment terms. In contrast, the payables results for SMEs have been much weaker since 2005. This may have been partly due to changing strategies and tactics, with a higher proportion of companies responding to more challenging credit conditions by paying more quickly, in return for enhanced cash discounts.
- With regards to inventory performance, large companies have seen a significant deterioration, as their supply chains become more complex and extended, buying and selling goods and services from and to more countries. In contrast, SMEs registered a significant improvement in inventory performance.

Much higher current C2C for SMEs than for large companies

Performance by company

SMEs continue to exhibit much higher C2C than large companies. In 2015, SMEs' C2C was 31% (equivalent to 15 days) higher than that of large companies on a sales-weighted basis.

Compared with SMEs, large companies enjoy superior performance in both receivables and payables, reaffirming the view that scale provides greater opportunities to negotiate favorable payment terms with customers and suppliers. SMEs scored slightly better than their larger counterparts in inventory management. Several factors may explain the difference in performance. For example, SMEs may have simpler product offerings and supply chains. Large companies are also more likely than smaller companies to sell outside their home regions, potentially giving rise to longer lead times and excess safety stocks. On the other hand, lean practices and vendor-managed inventory arrangements are more widespread among large companies. Increased use of outsourcing may have also played a significant role in driving inventory performance.

While these results confirm that size matters in WC, it remains unclear how much of the WC performance gap between SMEs and large companies is due to SME's reluctance to engage more openly with other participants in the value chain.

Table 22: WC metrics differential between SMEs and large companies, 2015

		%	days
DSO	SMEs worse by	21%	9
DIO	SMEs worse by	(5)%	(2)
DPO	SMEs worse by	(28%)	(8)
C2C	SMEs worse by	31%	(15)

Source: EY analysis, based on publicly available financial statements

Performance by industry

Comparing the relative WC performance of large companies and SMEs in the same industry highlights that SMEs in almost two-thirds of industries have higher C2C than large companies. In 2015, the median C2C differential figure at an industry level between SMEs and large companies was twelve days (median being used as a more appropriate measure in this case, given the uneven distribution of companies by industry).

The most meaningful variations at a C2C level for major industries are reported in the table below. Among electrical components, software and communications technology, for example, SMEs' C2C is 47%, 35% and 28%, respectively, above that of large companies. For diversified industrial companies, the corresponding figure is 12%. In contrast, SMEs in the aerospace & defence and oil equipment industries display lower C2C (-15% and -40%, respectively) than their larger peers.

Table 23: C2C differential by industry between SMEs and large companies, 2015

	C2C differential	
	%	days
Electrical components	47%	27
Software	35%	17
Communications technology	28%	16
Semiconductors	20%	12
Diversified industrial	12%	9
Chemical	5%	3
Aerospace and defense	-15%	-16
Oil equipment	-40%	-40

Source: EY analysis, based on publicly available financial statements

How EY can help

EY's global network of dedicated working capital professionals helps clients to identify, evaluate and prioritize actionable improvements to liberate significant cash from WC through sustainable changes to commercial and operational policies, processes, metrics and procedure adherence.SMEs continue to exhibit much higher C2C than large companies. In 2015, SMEs' C2C was 31% (equivalent to 15 days) higher than that of large companies on a sales-weighted basis.

We can assist organizations in their transition to a cash-focused culture and help implement the relevant metrics. We can also identify areas for improvement in cash flow forecasting practices and then assist in implementing processes to improve forecasting and create the frameworks to sustain those improvements.

WC improvement initiatives often create value. In addition to increased levels of cash, significant cost benefits may also arise from productivity improvements, reduced transactional and operational costs and from lower levels of bad and doubtful debts and inventory obsolescence. Improved processes also increase the quality of services both internally and externally. Wherever you do business, our WC professionals are there to help.

Methodology

The report contains the findings of a review of the WC performance of the largest 4,000 companies (by sales) headquartered in the US (consisting of 1,000 companies), Europe (1,000) and seven other main regions and countries - Asia (600); Australia & New Zealand (100); Canada (300); Central and Eastern Europe (150); India (400); Japan (230); and Latin America (270).

This report also sets out the findings of a review comparing the WC performance of SMEs with that of large companies. Using sales as the indicator of each company's size, SMEs have been defined in this report as companies with sales under US$1 billion, while large companies are those with sales exceeding US$1 billion. A total of 1,000 companies (all domiciled in the US for comparison purposes) were analyzed, evenly divided between the two sub-groups.

- The overall analysis draws on companies' latest fiscal 2014 reports. Performance comparisons have been made with 2013 and with the previous eleven years in the case of the US and Europe, and eight years for SMEs and large companies.
- The review on which the report is based is segmented by region, country, industry and company. It uses metrics to provide a clear picture of overall WC management and to identify the resulting levels of cash opportunity.
- Each of the companies analyzed in this research has been allocated to an industry and to a region or country. Reported global, regional and country numbers are sales-weighted.
- The overall review excludes financial institutions. The auto manufacturing industry (OEMs) is also excluded due to the difficulty of assessing its "true" WC performance, given the intertwined nature of its industrial and financial activities.
- The performance trends at the country and industry level need to be treated with a degree of caution: the approach is based on consolidated numbers in the absence of further local details, with each company being allocated to the location of its headquarters.
- Because of differences in industry weightings and in the level of international activity within each economy, an analysis of the WC performance gap across countries in Europe would not have been useful or meaningful.
- The WC performance metrics are calculated from the latest publicly available company annual financial statements. In order to make the figures as comparable and consistent as possible, adjustments (see glossary) have been made to the data to reflect the impact of acquisitions and disposals and off-balance sheet arrangements.

Glossary

- DSO (days sales outstanding): year-end trade receivables net of provisions, including VAT and adding back securitized and current financial receivables, divided by full-year pro forma sales and multiplied by 365 (expressed as a number of days of sales, unless stated otherwise)
- DIO (days inventory outstanding): year-end inventories net of provisions, divided by full-year pro forma sales and multiplied by 365 (expressed as a number of days of sales, unless stated otherwise)
- DPO (days payable outstanding): year-end trade payables, including VAT and adding back trade-accrued expenses, divided by full-year pro forma sales and multiplied by 365 (expressed as a number of days of sales, unless stated otherwise)
- C2C (cash-to-cash): equals DSO, plus DIO, minus DPO (expressed as a number of days of sales, unless stated otherwise)
- Pro forma sales: reported sales net of VAT and adjusted for acquisitions and disposals when this information is available

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