Cashing in on uncertain times is more than just a quick fix

TRUST IN Resilience

BY VICTOR SAW AND GANESH GUNARATNAM

"No winter lasts forever, no spring skips its turn." — Hal Borland

Seasons change and difficult times too shall pass, as American author Hal Borland's quote suggests. A sense of optimism can be felt as the Malaysian economy gradually reopens on the back of increasing vaccination rates.

Fitch Ratings also recently projected a 6.3% GDP growth rate for Malaysia in 2022. While this is encouraging, the local business community needs to press on with caution to find its footing post-pandemic. The nearly 3,000 bankruptcy cases reported by the Malaysian Department of Insolvency in the first four months of 2021 are a clear reminder that businesses are not out of the woods yet.

There is also the risk that stimulus packages — while helpful as a buffer for businesses to help refinance and restructure debt — may not be sufficient to help them tide over this subdued climate. Also, if and when policy support is withdrawn, will this result in a liquidity crisis or lead to further cases of bankruptcy? Given these uncertainties, companies need to take charge of their recovery response to stay competitive in the new normal.

Liquidity is taking centre stage

Profitability has traditionally been the central metric for evaluating companies. But as the pandemic hit and revenue streams dried up, many companies that were once profitable are now finding themselves in distress. This calls for a fresh outlook towards business performance.

It is timely for companies to refocus and pay attention to a usually overlooked aspect of business — cash flow. PwC's 2021 Act Now to Recover survey on business recovery among Malaysian business leaders and owners highlighted that 50% of the surveyed companies have not used a formal short-term cash-flow forecasting process. Only 30% have carried out contingency planning on the viability of supply chain stakeholders and only 24% have used a digital working capital management dashboard in the last 12 months.

This shows that while companies are recognising the importance of liquidity in their business, they also face challenges in identifying leading symptoms of an approaching cash crunch, isolating problem areas and deploying effective counter-measures.

While tracking financial metrics on liquidity is always helpful, early symptoms of a cash crunch may get overlooked by company leadership as it is concealed within day-to-day operations. In distressed times, companies should track markers such as repeated default on creditor payment terms, persistent difficulties in servicing loans and inability to invest in growth opportunities due to cash-flow pressures. Other indicators of an impending cash crunch include forced scaling down of marketing promotions and continuous lowering of customer service levels due to lack of investment.

These could be seen as alarm bells for companies to rethink how they manage their liquidity. If unchecked for long periods, these symptoms may manifest in a more complex form, making recovery that much more difficult. On the other hand, rectifying the problem sooner ensures business continuity. Hence, it is clear that a company's options for recovery will reduce over time.

A sharper look at cash flow

The first action for any company is to have a comprehensive understanding of their cash-flow position. Typically, organisations develop annual cash-flow forecasts; however, with the current economic uncertainties, continuous and scenario-based cash-flow forecasting is crucial.

Companies are recommended to set up a cross-functional cash management office to draft a 13-week rolling cash-flow forecast. This will go a long way in highlighting on-ground situations to management, giving them an opportunity to put strategic and operational interventions into action. These forecasts enable companies to focus on critical cash inflows and outflows while de-prioritising any expense that is not business critical. It also shows the extent of the company's cash runway, giving leadership the time it needs to act before it is too late.

The impact of Covid-19 has varied from industry to industry. While businesses in essential services and technology sectors have thrived, many others are facing challenges in staying afloat. Depending on size, operating models and supply chain dependencies, companies will need to adapt their approach of doing business based on their unique circumstances.

Dash for cash in the short term

In the short term, companies should look for immediate impact options to get an increase in cash flow. Working capital optimisation could be an option. Bolstering working capital can be performed strategically in different ways. This includes expediting receivables by reducing time to invoice, and running early payment discounting schemes and targeted follow-ups. Other options are to rationalise inventory levels by aligning sales and operations planning processes, containing early payments, and renegotiating payment terms with creditors.

In distressed times, companies may also consider liquidating their non-core assets to infuse additional liquidity. Restructuring debt to more favourable terms can help organisations align business proceeds to debt repayments at more equitable interest rates. Apart from all these, stimulus packages could be a fallback option to buffer the impact of the pandemic on businesses, but these measures need to be accompanied by liquidity management initiatives driven by the companies themselves.

These short-term measures focus on ensuring healthy liquidity for companies to wade through this current crisis. However, cash optimisation is not a one-off activity; it is a mindset, to be pursued consistently and across the organisational hierarchy. Businesses that focus on cash flow during buoyant periods are in a better position to deploy cash reserves on strategic investments during downturns, giving them a competitive advantage.

Sustained focus on operational excellence, better tax management and effective treasury operations will help in releasing trapped cash in the system. A differentiator also lies in proactively focusing on financing strategies as a part of the regular business planning process. Tying up the business strategy and future growth plans with associated investment requirements can help companies plan for fundraising ahead of time.

During recent times, investors are increasingly relying on non-financial markers such as environmental, social and governance (ESG) considerations to make funding decisions. In parallel, there is also growing regulatory and legislative momentum towards ESG. Thus companies that proactively recognise ESG risks and holistically address them will stay in favour of investors.

Nurturing a cash culture

Cash is evidently pivotal in building a strong support base for companies to avoid distress while also fuelling future growth. Building a "cash-first culture" in an organisation is key. What are some ways to inculcate this culture?

Considering the cash impact in every key management decision is a good starting point. This can be operationalised through various initiatives across the business such as setting objective cash performance targets at the departmental level, incentivising cash performance, and maintaining good operational and financial controls over liquidity.

Digital advancements will also serve as a key enabler in driving this culture in organisations. This will help enhance visibility across organisational silos, expediting real-time information flow and helping companies predict eventualities before they occur.

Advantages of this culture shift are far-reaching. It promotes proactive inputs from all stakeholders, leading to improved forecasts, and facilitates buy-in from different parts of the business on critical expenditures. This can then lead to a coordinated response to liquidity pressures and, by extension, to the prevalent business challenges.

In conclusion, uncertainties will be part and parcel of growing and charting a path forward beyond the pandemic. However, amid the uncertainties lie the biggest opportunity for businesses. Companies that are prepared to act sooner will present themselves with the best chance to stabilise their cash-flow position and maximise their options to grow. E

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