European firms could improve working capital by almost €900 billion, research finds

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An increasing number of businesses are making use of supply chain financing (SCF) which is having a "positive effect on the overall health of supply chains".

These comments from Jonas Schoefer, a director at working capital specialist REL, follow research that showed an increased focus on working capital as costs and debt start to decrease and cash on hand and free cash flow increase.

But he added there is still a total improvement opportunity - the money that could be released if all the companies were to fully optimise their working capital operations in respect of payables, receivables and inventories - of nearly €900 billion (£720 billion).

"This is made up of a €300 billion (£240 billion) improvement opportunity in payables, a further €296 billion (£237 billion) in inventory and €293 billion (£235 billion) in receivables," REL's *16th annual European Working Capital Survey* explained.

It added the best companies – those with "well-optimised processes" – pay suppliers two-and-a-half weeks later and operate with nearly 70 per cent less inventory. The research revealed that sustaining working capital improvements still remains a major challenge. "Only 14 per cent of companies in the REL study improved days working capital (the days it will take a company to convert its working capital into revenue) for three consecutive years," it said.

Schoefer believes companies are paying suppliers later because "more companies are using SCF". He said: "This would extend payables on the balance sheet, but actually mean that suppliers can access payments earlier. This would also explain why we can see a like-for-like trend in receivables – companies receive payments earlier on the whole.

"SCF is increasingly popular because we are almost at the point of last resort for some companies – in general, terms are pushed as far as they will go. We quite often encounter clients who might be on 60 or 90 day terms with suppliers but don't want to extend any further on ethical grounds. But with SCF you can push terms out while keeping everyone happy.

"This is having a positive effect on the overall health of supply chains. Simply extending supplier terms without a flanking measure like SCF would directly increase supply chain risk. I think there's an acknowledgment that supply chains, particularly ones that are stretched across the globe, are increasingly fragile so there's low incentive to place further strain on them considering

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there are only marginal gains to be made."

Schoefer also said that companies' financial situations were "probably the biggest threat to supply chains". He said: "Financial situations, particularly given that we might face another burst bubble, are probably the biggest threat to supply chains.

"While REL wouldn't advocate giving away any benefits [such as ceding beneficial terms in negotiations with suppliers], there are solutions that can be win-win for buyer and supplier; for procurement and finance. Supply chain finance (SCF) is one of those solutions but so is, if you're a cash rich buyer, negotiating a price discount linked to shorter payment terms. With interest rates what they are, investing in your supply chain is probably more valuable than simply having more cash."

The research examined published accounts of Europe's largest listed companies.

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