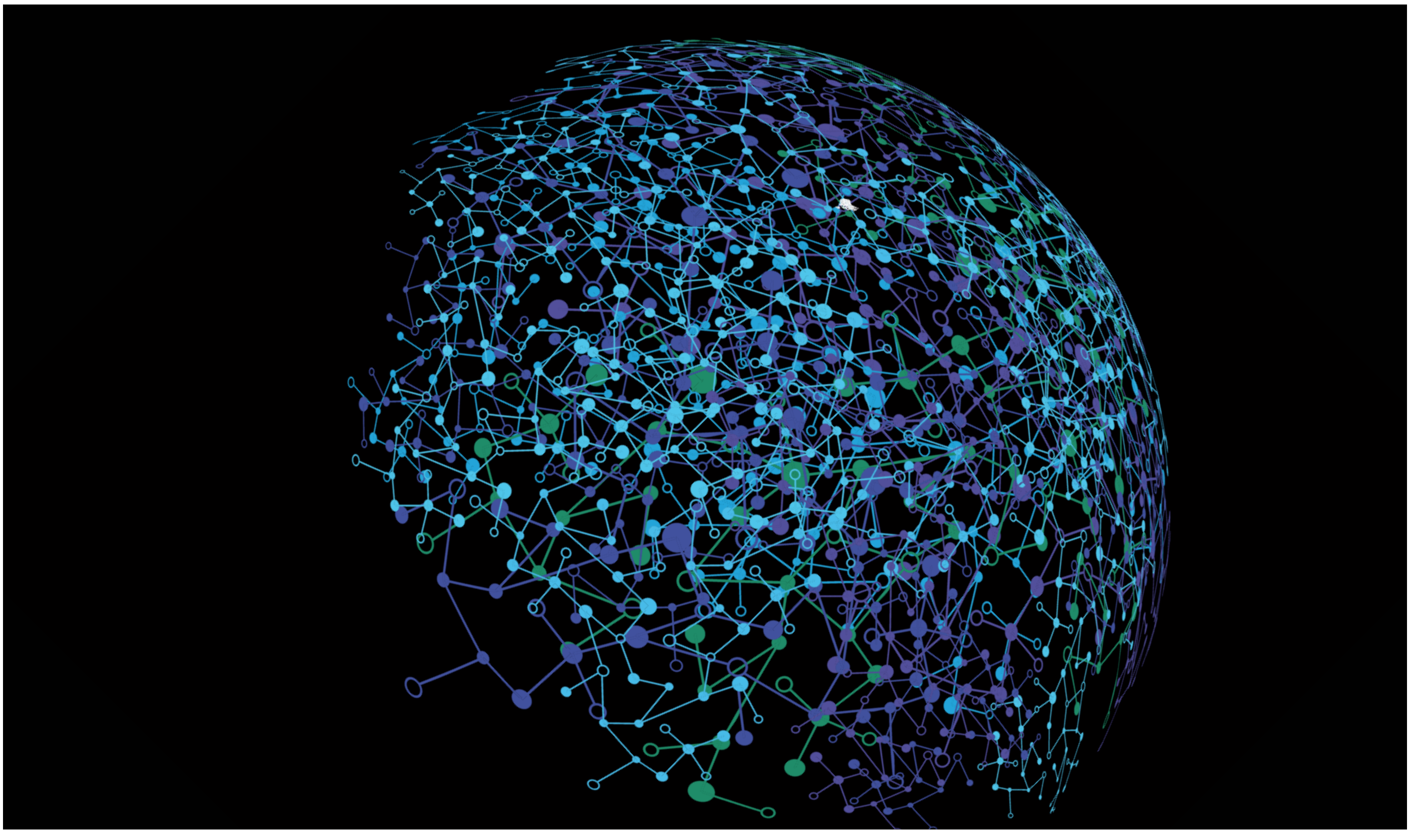
Deloitte.

April 2020



Managing Cash flow during a period of crisis - Part 2

COVID-19

The outbreak of the Novel Coronavirus (Covid-19) pandemic continues to have economic and financial ramifications with uncertainties on full global recovery. The number of infections have increased rapidly over the past few weeks, with more than 1.5 million confirmed cases and more than 80,000 deaths as beginning of April. The United States of America (USA) has become the next epicenter of the pandemic, recording more than 350,000 cases and Italy reports world's highest number of deaths- over 15,000 deaths since the start of the pandemic.

Ghana has equally seen a rapid surge in the number cases, adding more than 150 cases in a week, and taking the nationwide total to 287 cases, 31 recoveries and 5 deaths as at the beginning of April.

In view of this, the Government of Ghana has imposed a partial lockdown in the Greater Accra Metropolitan Area and the Greater Kumasi Metropolitan Area for a period of two (2) weeks, effective March 30 to limit and contain the spread. In addition, the Government plans to undertake the following initiatives:

- release of a minimum of GH¢1 billion to households and businesses;
- make available a GH¢3 billion facility to support the pharmaceutical, hospitality, service and manufacturing sectors;
- get banks to roll out a six-month moratorium of principal repayments to entities in the airline and hospitality sectors;
- absorption of water bills for all citizens for the next three (3) months; and
- tax exemptions for all health workers for the next three months and an additional allowance of 50% of basic salaries for frontline health workers.

As some parts of the country go on partial lockdown, a sharp decline in demand is expected as consumers stay at home and stop spending. Business activities will slow down considerably and companies risk being unable to manage the disruptions.

This article which is part 2 in the series, will suggest more ways organisations can mitigate damages to their business during this volatile event.

Businesses that will be hit the hardest

Tourism and hospitality

- Job losses given the low patronage.
- In Ghana, 16 hotels spread across 3 regions have reported total revenue loss of about GHS63m due to cancelations of room bookings and conferences scheduled for March and April.
- Full Recovery expected in 10 months.

Aviation

- A projected 20% decline in revenue in Ghana's aviation sector.
- Pace of recovery for domestic travel is expected to be faster than international travel.

Oil and Gas

- The cash flow of oil and gas companies in Ghana have been threatened given the plunge in global crude oil prices in recent times.
- Recovery is dependent on resumption of consumer demand.

Financial Services

- Risk of loan default as incomes of businesses and individuals are adversely impacted by COVID-19.
- Pressure on banks to restructure loan facilities with possibility of granting moratorium on loan repayment and reduction of interest rate.

Retail/ Consumer products

- Shortage of some basic consumer goods imported from China have led to price spikes.
- Overall decline in consumption.

Information and Communication Technology (ICT)

- Revenues of telecom companies (telcos) and internet service providers (ISPs) will be boosted as demand for voice and data services increases
- Pressure on telcos and ISPs to invest in expansion of infrastructure and improve service quality

Highest Impact — Estimated degree of impact in terms of duration — Lowest Impact

Responding to the immediate challenge

1. Extend payables, intelligently.

One way to preserve working capital is to take longer to pay your suppliers. Some companies may unilaterally decide to delay their payments and force the extension on their suppliers, especially when stuck with inventory they cannot deliver into impacted margins. Of course, such an approach is likely to damage your supply relationships. Even worse, it might deprive supply chain partners of the cash they need to maintain their operations, which could lead to late deliveries and quality problems, never mind the added strain to supply relationships. We recommend working with suppliers to establish an agreement that both of you can live with. There might even be situations where you need to accelerate payables for a critical supplier that is on the brink of failure in order to preserve the integrity of your supply chain and prevent a critical disruption.

2. Manage and expedite receivables.

Companies tend to get lax about receivables when the economy is booming, interest rates are relatively low, and cash flow is not a concern. But, as supply chains are affected and managing cash flow becomes more important, it is worth taking a hard look at how your receivables are being managed. In the point above, we mention the strategy of delaying payments to your suppliers; don't be surprised if your customers are thinking about doing the same thing to you. That is why it is important to improve the rigour of your collection processes. Focus on customer-specific payment performance and identify companies that may be changing their payment practices. Also, get the basics right, such as timely and accurate invoicing. Any errors in your billing process can lead to costly delays in receiving payment.

3. Consider alternate supply chain financing options.

Depending on what your cash flow scenario planning reveals, you may also need to consider tactics to generate faster cash flow from your receivables. Aggressive techniques such as factoring your receivables, although relatively expensive, may be your best option to improve cash flow quickly. You may also consider working with your customers to offer dynamic discounting solutions for those that are able to pay more quickly (e.g., discount terms can be defined in advance, and the customer calculates the appropriate discount based on a defined payment schedule). With this technique, you are essentially paying customers to provide you with short-term financing. But the cost may be substantial: a conventional "2% net 10" early payment discount translates into a 36% APR. However, if government loans or bank credits are not available, this might be one of your only options. There are also a number of other supply chain financing possibilities that can be implemented in the short to medium term, such as collaborating with your key trading partners to optimize cash flow across the extended supply chain.

4. Audit payable and receivable transactions.

Make sure you are paying the right amount for the goods and services you procure and collecting the right amount for goods and services you sell. On the payables side, double-check that you are not overpaying duties and taxes on purchases, especially as alternate international supply locations are used to keep supply chains running. Also, if you have the cash flow to support it, make sure you are taking full advantage of all available discounts. On the receivables side, look for situations where unearned discounts were applied and then aggressively pursue the proper payment. Once the audits have been completed, look for longer-term policy and process improvements that can prevent new problems from cropping up. Consider using robotic process automation for your audits, which will reduce the burden on headcount.

5. Understand your business interruption insurance.

Companies should understand existing business insurance policies and the coverage they have in the event of a significant business disruption. Such insurance generally covers losses arising from disruptions to a business's customers or suppliers. However, the breadth of coverage can vary significantly by insurer policy, industry sector, and geography. In addition, due to the insurance losses from the SARS epidemic, some insurers have included specific exclusions for losses arising from epidemics and pandemics, which you'll need to understand if this is the case in your policy.

6. Consider alternate or non-traditional revenue streams.

If your scenario planning is showing pressure on your continued revenue streams, consider ways you could temporarily or maybe even permanently replace that revenue. For example, if your primary markets are international, how might you pivot to domestic markets (especially if your inventory is perishable)? If you have assets you use to generate revenue, how could you think differently about how those assets are used to generate alternate revenue sources? Not only could this reduce some of your top line pressures, it could also mean not having to reduce your cost lines as significantly (not to mention a potentially more diversified revenue mix in the longer term).

7. Convert fixed to variable costs, where possible.

Companies in times of uncertainty, it is generally a good idea to swap fixed costs for variable costs wherever you can preserving your core business while increasing your flexibility on the fringes. Selling assets and then leasing them back is one way to raise emergency cash. You might also want to consider expanding your use of practices such as contract manufacturing, transportation fleet leasing, and third-party warehousing. This is not likely a quick-hit measure for most companies, but may be important to longer-term cash flow management, depending on how long demand and supply chains are disrupted by COVID-19.

8. Think beyond your four walls.

To maximize working capital, you cannot only focus on your own operations and inventory levels: you need to think about your entire ecosystem and supply chain. Squeezing inventory out of your operation may not do much good– and could in fact introduce significant risk–if it just shifts the burden to a supplier or customer. The same is true for payables and receivables. It is important to carefully consider the upstream and downstream impact of your actions. High-level financial risk assessments should be conducted on any critical, sole-source suppliers to identify issues before they become problems. In extreme cases, if a critical supplier is at risk, you might even need to buy a stake in the company or acquire the business outright to protect your supply chain and keep your goods and services flowing.

What's next: Recovering and returning to normal business operations

Cash flow management needs to be an integral element of a company's overall COVID-19 risk assessment and action planning in the near term. Even for companies that have not yet been adversely affected, we recommend management teams with concerns about COVID-19 actively evaluate their cash flow requirements, develop appropriate actions under various scenarios, and assess potential risks in and to their customer base and supplier network.

How can Deloitte help?

Financial restructuring

Helping companies deal with urgency when appropriate. Together with management, we prepare and review turnaround business plans, highlight key sensitivities and determine the cash needs.

Business modelling

Scenario modelling to help assess the impact of COVID-19 on budgets and forecasts. We assist companies in the preparation of forecasts and set-up a comprehensive reporting system that allows them to assess the cash generation of their operations.

Debt advisory and restructuring

We prepare debt restructuring plans and advice on optimal capital structures for businesses. We assess serviceable debt and covenants obligations. We support companies to negotiate with financing parties and to obtain new debt funding.

Cyber

Cyber risk assessment along with recommended solutions given the onslaught of “work from home” that is occurring globally.

Contacts

Charles Larbi-Odam
Country Managing Executive
Deloitte Ghana
clarbi-odam@deloitte.com.gh
+233 307 086 330

Kofi Awuah
Partner
Risk Advisory
kawuah@deloitte.com.gh
+233 501 648 111

Yaw Lartey
Leader
Financial Advisory
ylartey@deloitte.com.gh
+233 244 158 377