

Professional Supply Management 1

Erik Hofmann
Daniel Maucher
Sabrina Piesker
Philipp Richter

Ways Out of the Working Capital Trap

Empowering Self-Financing
Growth Through
Modern Supply Management

Professional Supply Management

Series Editors:

Gerd Kerkhoff
Erik Hofmann
Wolfgang Stölzle

For further volumes:
<http://www.springer.com/series/10063>

Erik Hofmann · Daniel Maucher · Sabrina Piesker ·
Philipp Richter

Ways Out of the Working Capital Trap

Empowering Self-Financing Growth Through
Modern Supply Management

 Springer



Dr. Erik Hofmann
Universität St. Gallen
Kerkhoff Competence Center
of Supply Chain Management
Lehrstuhl für Logistikmanagement
Dufourstr. 40 a
9000 St. Gallen
Switzerland
erik.hofmann@unisg.ch

Daniel Maucher
Universität St. Gallen
Kerkhoff Competence Center
of Supply Chain Management
Lehrstuhl für Logistikmanagement
Dufourstr. 40
9000 St. Gallen
Switzerland
daniel.maucher@unisg.ch

Sabrina Piesker
Kerkhoff Consulting GmbH
Grafenberger Allee 125
40237 Düsseldorf
Germany
s.piesker@kerkhoff-consulting.com

Philipp Richter
Kerkhoff Consulting GmbH
Grafenberger Allee 125
40237 Düsseldorf
Germany
p.richter@kerkhoff-consulting.com

ISBN 978-3-642-17270-0
DOI 10.1007/978-3-642-17271-7
Springer Heidelberg Dordrecht London New York

e-ISBN 978-3-642-17271-7

Library of Congress Control Number: 2011921254

© Springer-Verlag Berlin Heidelberg 2011

This work is subject to copyright. All rights are reserved, whether the whole or part of the material is concerned, specifically the rights of translation, reprinting, reuse of illustrations, recitation, broadcasting, reproduction on microfilm or in any other way, and storage in data banks. Duplication of this publication or parts thereof is permitted only under the provisions of the German Copyright Law of September 9, 1965, in its current version, and permission for use must always be obtained from Springer. Violations are liable to prosecution under the German Copyright Law.

The use of general descriptive names, registered names, trademarks, etc. in this publication does not imply, even in the absence of a specific statement, that such names are exempt from the relevant protective laws and regulations and therefore free for general use.

Cover design: eStudio Calamar S.L., Heidelberg

Printed on acid-free paper

Springer is part of Springer Science+Business Media (www.springer.com)

Series Preface

The trend towards globalization and the increasing division of labor as well as the rapid development of information and communication technology have led to worldwide value networks associated by material flows, information flows, and cash flows. These global supply chains pose major challenges for the stakeholders involved because of their complexity and cross-national major structure.

Therefore, supply chain management deals with the task of planning and directing efficient value creation networks taking economic, environmental and social aspects into account.

A professional advanced purchasing comprises the integrated management of all processes to supply a company with the required goods from sources outside the company. Thereby, the foremost target is to contribute to the achievement of competitive advantages of one's own company. By linking the procurement with the supply chain management, company-wide improvements may be achieved and strengthened in a sustainable matter.

Nowadays, procurement and supply chain management are part of the key management disciplines and in many companies they are already anchored at the top management level. Procurement and supply chain managers are not longer focused solely on reducing costs, because of this relevance, but contribute to the differentiation of companies and value networks. The confrontation with issues such as risk management, financing, sustainability in the supply chain, and product innovation will increase in the following years due to changing political conditions, oligopolies in supplier markets and further shrinking resources.

Despite the great practical relevance of procurement issues, the future challenges mentioned appear not to be adequately addressed from a scientific point of view so far. Furthermore, the connection between procurement and supply chain management has not been explored extensively. The series "Advanced Purchasing & Supply Chain Management" aims to contribute to closing these gaps. The intention is to generate benefits both in respect of sciences and practical matters.

The realization of this objective is supported by the "Kerkhoff Competence Center of Supply Chain Management" (KCC) – a jointly initiated platform of excellence by Kerkhoff Consulting and the University of St. Gallen. The goal of the KCC is to create an interface between science and practice. Therefore, trends and challenges in purchasing, procurement and supply chain management are to be analyzed

and recommendations to be derived for practical issues. Meanwhile, a practice-relevant cognitive process is strived for in terms of procurement and supply chain management.

The contributions of the series deal with current issues as well as innovation and excellence approaches in the management of value networks and link theoretical concepts with practical applications. Relevant themes are inter alia the purchase of capital goods, performance measurement in supply chain management and procurement, performance contracting or procurement in the public sector. The authors are researchers from the University of St. Gallen, researchers of other leading international research institutions with a focus on procurement and supply chain management, consultants from Kerkhoff Consulting as well as practical experts. By forming mixed writing teams from academia and industry, a close integration of these areas is ensured. This combination takes the application-oriented aspect of business management into account.

The present volume “Ways out of the working capital-trap” opens the series “Advanced Purchasing & Supply Chain Management”. Based on the situation of an increased demand for capital during a period of restrained granting of credit by banks, approaches to identify and strengthen internal financial power are presented from a company’s and a supply chain’s point of view. With the first volume, the authors show the close integration between procurement and supply chain management and their impact on the financing capabilities of companies. Furthermore, specific recommendations for purchasing managers and supply chain managers are given to enhance the financial competitiveness of their company and of partners along the value chain.

The authors of the series hope that all readers may enjoy this first volume and receive a number of specific impulses to pursue possible “paths out of the working capital-trap”. We are convinced that the approaches and tools presented make a valuable contribution to this effort.

Düsseldorf, Germany
St. Gallen, Switzerland
St. Gallen, Switzerland
September 2010

Gerd Kerkhoff
Erik Hofmann
Wolfgang Stölzle

Foreword

In recent years increasing competition has led to a continuous focus on core competences within companies. They reduce their own value-added and buy more from outside. With this increase in buying, the impact of purchase on the company's results rises. Therefore, the purchasing function is playing an increasingly crucial role in a company. As one of the new hubs to ensure the company profits, the purchase has to make use of all levers available and start to operate professionally outside the "traditional" purchasing areas.

A continuous outflow of cash results from the company because of the payment of the procured raw materials, goods and services. There is a time gap within most companies between the payment made by customers and the payment for the raw materials. As a consequence, the purchase of raw materials, goods and services has to be financed. The cover of this time gap results in financing costs. The financing for companies has become increasingly difficult due to the 2008/2009 financial crisis and the previously enacted Basel II. As a result of this situation, a disproportionate demand in the first phase of recovery may result in the so-called "working capital-trap".

The focus of this book is on the impact of the purchase and its levers available to control liquidity. Therefore, the issues of different financing options and optimization on the debtor's side are not dealt with in depth.

As part of the work on this book, four areas were identified to influence liquidity in the supply chain, whereby each of them has to be optimized individually:

- Timing and method of payment to the supplier: many companies work with an extension of payment terms. Thereby, it is often overlooked that different financing costs within the supply chain have to be taken into account.
- The amount and date of the transfer of goods from suppliers into the company's own value-added. In this context, the issues of size of delivery, way of delivery, and thus the stock height are mainly concerned.
- Optimization of the financing costs in terms of cash flows given to the suppliers: there is a need to create a balance between internal and external financing costs and align with new payment tools.
- Reducing purchasing costs: this topic relates to the classical understanding of the activities in purchasing.

Directly depending on the business objectives, a comprehensive optimum has to be found for these four areas.

The purchaser is faced with a continuous increase in complexity. In order to provide the adequate value contribution in this environment, the purchaser has to leave the beaten track and make use of integrated approaches to a complete procurement optimization. This book aims to provide food for thought on this issue and also constitute a guide.

The joint work on these issues has repeatedly shown us that by dropping traditional attitudes and approaches the purchase influence can be expanded significantly. In this regard, our special thanks go to Mr Gerd Kerkhoff, the Chairman of the Board of Kerkhoff Consulting, who has provided us and the authors with many new ideas. Furthermore, we would like to thank the authors who have succeeded in describing the various levers of purchase and have thus created a guide for purchasing departments.

Vienna, Austria
Düsseldorf, Germany
September 2010

Tobias Némét
Oliver Kreienbrink

Contents

1 Call for Action: From Financial and Economic Crisis to Working Capital Trap	1
1.1 Effects of the Financial Crisis on the Real Economy	1
1.2 Looming Credit Squeeze as an Obstacle to Growth	3
1.3 The Working Capital Trap as a Challenge	4
2 Determination of the Internal Financing Power of Corporate Growth via the Self-Financeable Growth Rate	7
2.1 Limits of Growth and Growth Financing of Companies	7
2.2 Financial Growth Potential According to the Self-Financeable Growth Rate Approach	8
2.3 Possibilities for the Optimization of the Self-Financeable Growth Rate	12
3 Strengthening Internal Financing Power Using Cash-to-Cash Cycle Optimization	13
3.1 Presentation of the Cash-to-Cash Cycle	13
3.2 Influence of the Cash-to-Cash Cycle on Corporate Value	16
3.3 Possibilities for the Optimization of the Cash-to-Cash Cycle from the Corporate Viewpoint	17
3.4 Interdependencies of the Cash-to-Cash Cycle from a Supply Chain Viewpoint	20
4 Measures for Strengthening Internal Financing Power from a Corporate Viewpoint	21
4.1 Management of Payment Terms	21
4.2 Inventory Management	31
4.3 Product Group Management and Supplier Management	41
5 Measures for Strengthening Internal Financing Power from a Supply Chain Viewpoint	55
5.1 Finance-Oriented Supply Chain Sourcing	56
5.2 Supply Chain-Oriented Supplier Financing	59
5.2.1 Reverse Factoring	59
5.2.2 Cross-Company Financing of Capital Goods	61

- 5.3 Collaborative Cash-to-Cash Management 62
 - 5.3.1 Collaborative Cash-to-Cash Management with Varying Inventory Carrying Rates 63
 - 5.3.2 Collaborative Cash-to-Cash Management with Varying Capital Cost Rates 64
- 5.4 Collaborative Cash Pooling and Netting 64
 - 5.4.1 Cash Pooling and Netting in the Corporate Group as a Starting Point 65
 - 5.4.2 Cash Pooling and Netting in the Supply Chain 68
- 5.5 Supply Chain Financing Platforms 70
- 6 Case Study: Increasing Internal Financing Power of a Supplier in the Automotive Industry 75**
 - 6.1 Company’s Starting Situation 75
 - 6.2 Presentation of Measures 76
 - 6.3 Performance Measurement Using a Working Capital Management Analysis Tool 77
- 7 Measuring Procurement Contribution to Corporate Performance using the “Procurement Value Added” 81**
 - 7.1 Measuring Procurement Contribution to Corporate Performance 81
 - 7.2 Presentation of the Procurement Value Added 81
 - 7.3 Exemplary Calculation of the Procurement Value Added 84
- 8 Conclusion 87**
 - 8.1 Summary 87
 - 8.2 Outlook 88
- Literature 91**