

Business Recovery Services

Cash for Growth

Working Capital in the Retail Sector – 2016 Study

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and Confidential*

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pwc

Foreword



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Welcome to PwC's 2016 working capital study of the top 40 retailers within Germany, Switzerland and Austria.

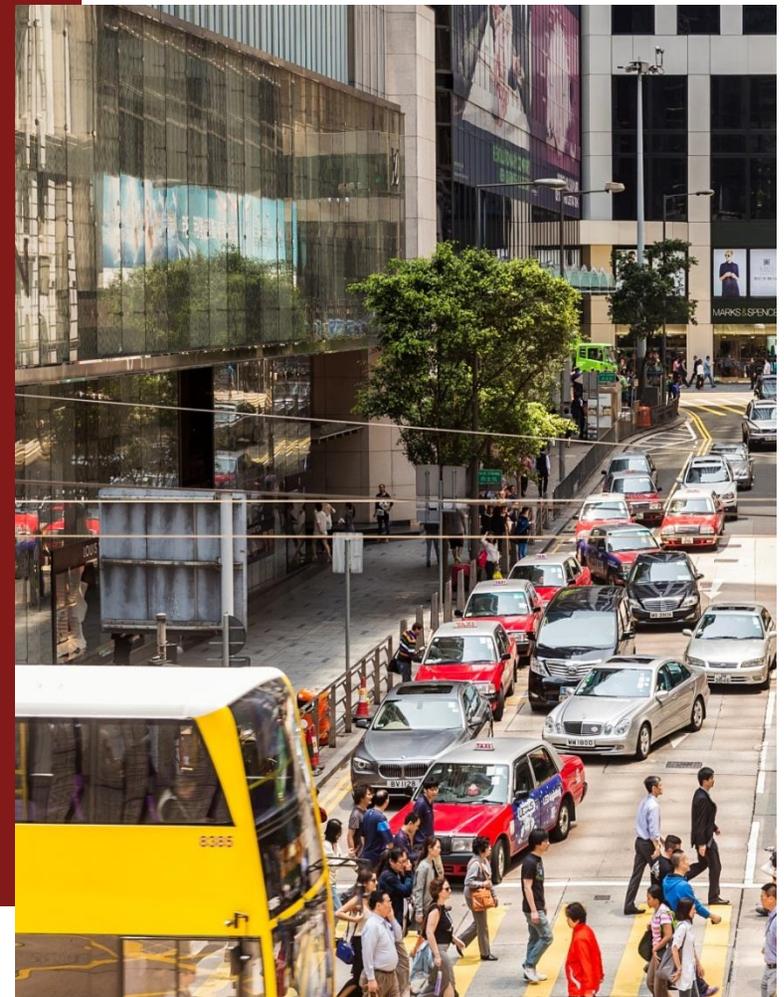
Following strong recent sales growth, working capital performance has deteriorated as companies struggle to manage their cash effectively. A key driver is the decreased payables position following the introduction of the EU payment directive in March 2013.

Customer demands are continually increasing. They want products quicker and with longer return rates. Online retail is driving growth which increases the complexity of supply chains and inventory management. Investments are therefore essential and retailers need to optimise their operations in order to release much needed cash from their working capital.

In this study we will be looking at the key working capital trends in various sub-sectors within retail and how performance levels vary widely.

Our study shows that if retailers move to the next performance quartile, they could generate a total of €2.7 billion of cash, while moving to upper quartile performance would release €4.9 billion of cash.

PwC can work with you to help achieve sustainable performance improvement. Act now.



Results show an overall return to sales growth...



Overall sales for the top 40 companies in the German, Swiss and Austrian retail sectors grew by 7.7% since FY11, equivalent to a compound annual growth rate (CAGR) of 2%. The rate of growth has shown a recent positive trend with overall FY15 sales increasing by 4.6%.

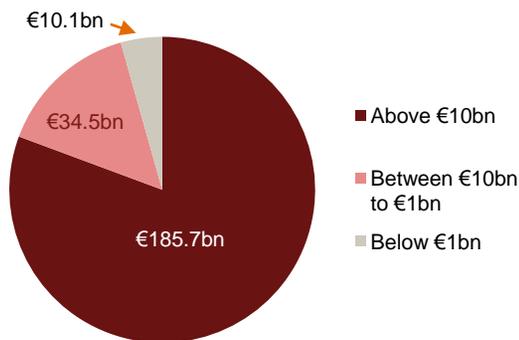
Top growth contributing sub-sectors:

- Food / Hypermarkets
- Sportswear

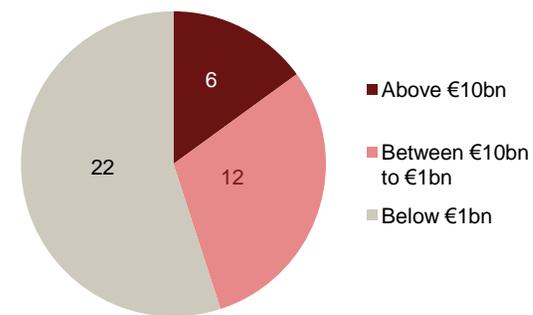
Revenue trend in the retail sector



Revenue distribution of companies in study (split by sales)

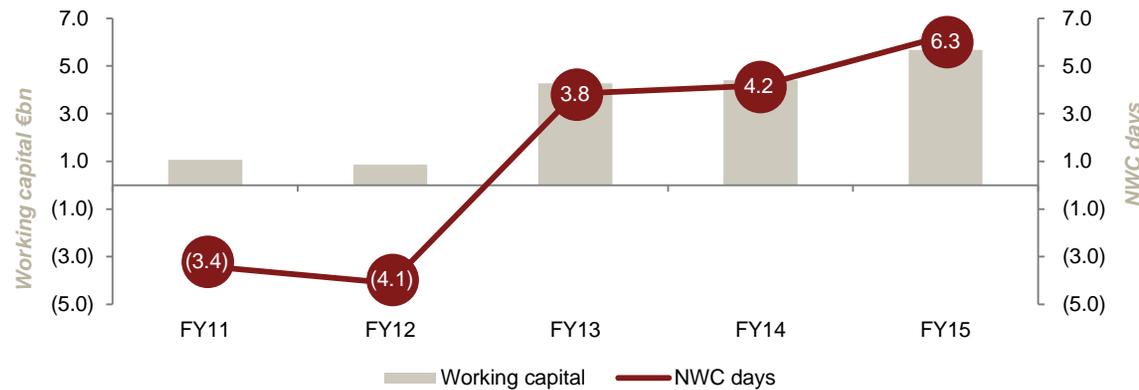


Number of companies in study (split by sales)



...but working capital performance has been negatively impacted

Retail sector working capital trend



€1.3bn
increase in working capital since FY14



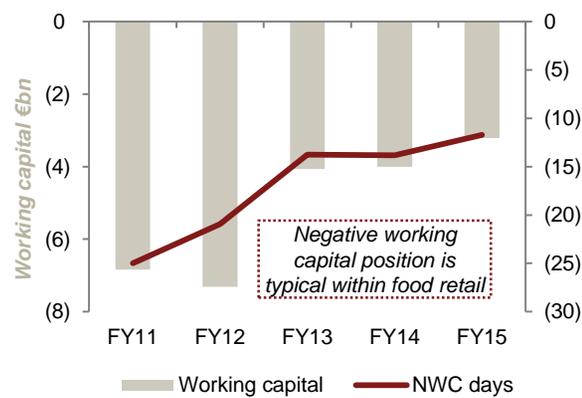
Working capital performance has steadily deteriorated since FY11. Over the past five-year period an additional €4.6 billion has become trapped in working capital and this has resulted in an overall 9.7 days increase to the net working capital days ("NWC"). Following the EU late payment directive being introduced in March 2013, the overall position shifted between negative and positive, driven by a 9.3 days decrease in the DPO.

Increasing levels of working capital require cash to fund daily operations and thus inhibit a company from investing in future growth.

The current level of trapped working capital within the retail sector suggests significant opportunities for improvement.



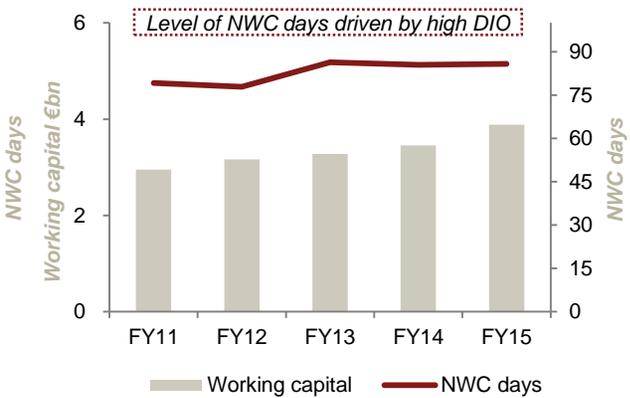
Food / Hypermarkets
20% increase in working capital



Negative working capital position is typical within food retail



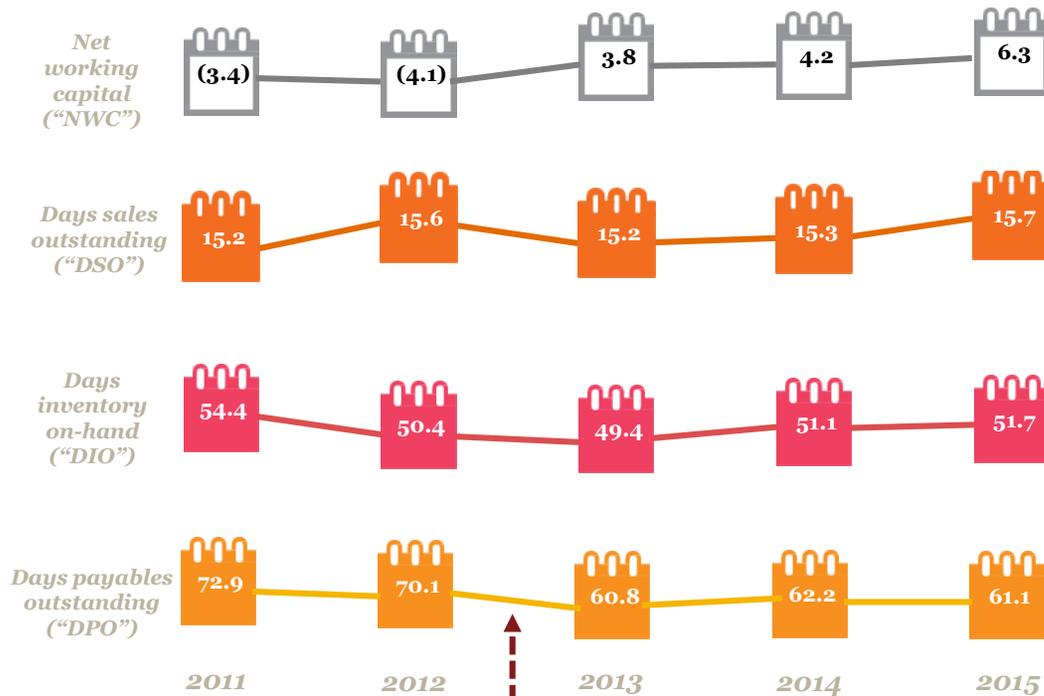
Sportswear
13% increase in working capital



Level of NWC days driven by high DIO

All working capital cycles show room for improvement

Working capital performance



Food /
Hypermarkets



Sportswear



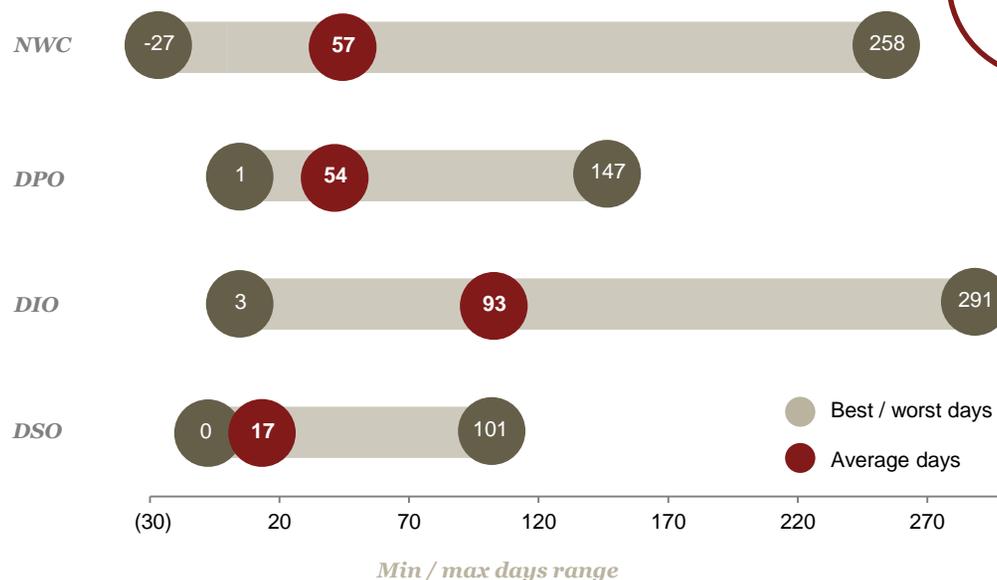
Overall, net working capital performance has deteriorated, largely driven by the DPO position.

68% of retailers increased their working capital since FY14, totalling an additional €1.5 billion. With 47% of this coming from the food consumable & hypermarket retailers (approx. €700 million).



Performance varies widely within retail...

Working capital performance range



€23bn
trapped
inventory
(FY15)

288
inventory days
range



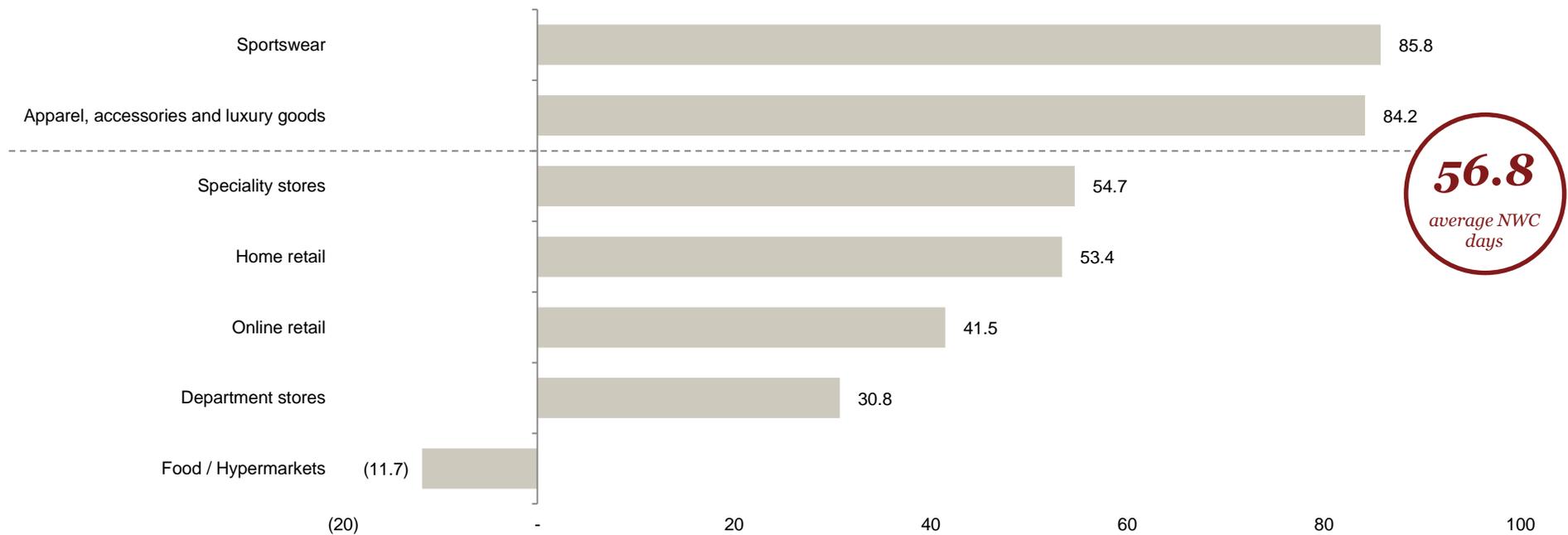
The working capital performance range shows vast variances across the retail sector, with an average of 56.8 days working capital.

Retail is typically characterised by low receivables days (DSO) which is a key driver of the overall working capital position.

Inventory performance (DIO) is the most widespread (approx. 288 days range) and is therefore the most likely key performance differentiator for retail companies.

...highlighted by significant variances within retail sub-sectors

Average net working capital days by retail sub-sectors



(11.7) NWC days & €163.8 bn sales
(FY15)

€3 billion Sales increase vs FY14.

Overall decline of 2.1 NWC days since FY14 due to worsening inventory management and quicker payables repayment.



85.8 NWC days & €21.2 bn sales
(FY15)

€2.9 billion Sales increase vs FY14.

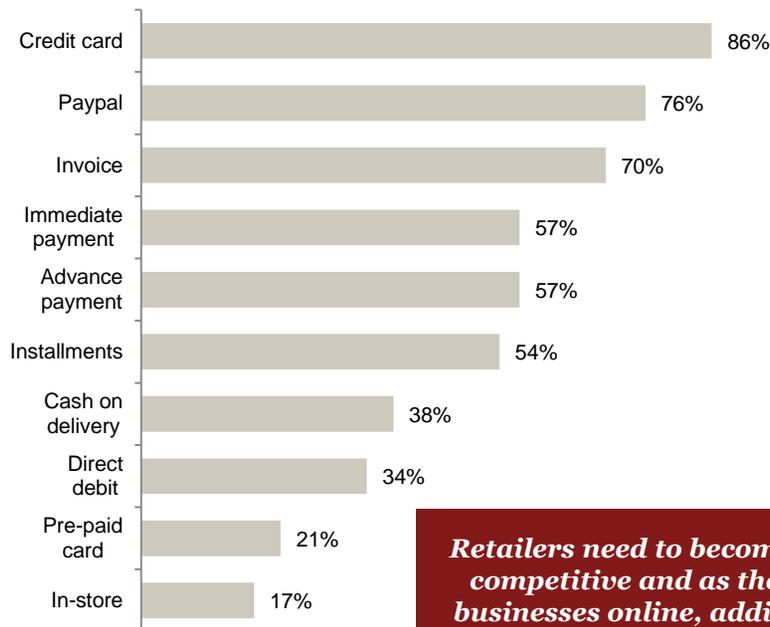
Overall decline of 0.3 NWC days since FY14 due to worsening inventory management.

On average, the retail sector could improve working capital performance by €2.7 billion to €4.9 billion...



...which could help fund future development as retailers move online...

Payment methods accepted by top 100 online retailers



5

average online payment methods

Key online retailer trends:

- Wider variety of payment methods
- Extended return conditions (up to 100 days)
- Invoice payments continue to be most commonly used (which increases receivables levels)
- “Fast return to shelf” quote a prerequisite for a capital-efficient inventory management
- Combination of sales channels (“omni-channel”) requesting higher levels of working capital

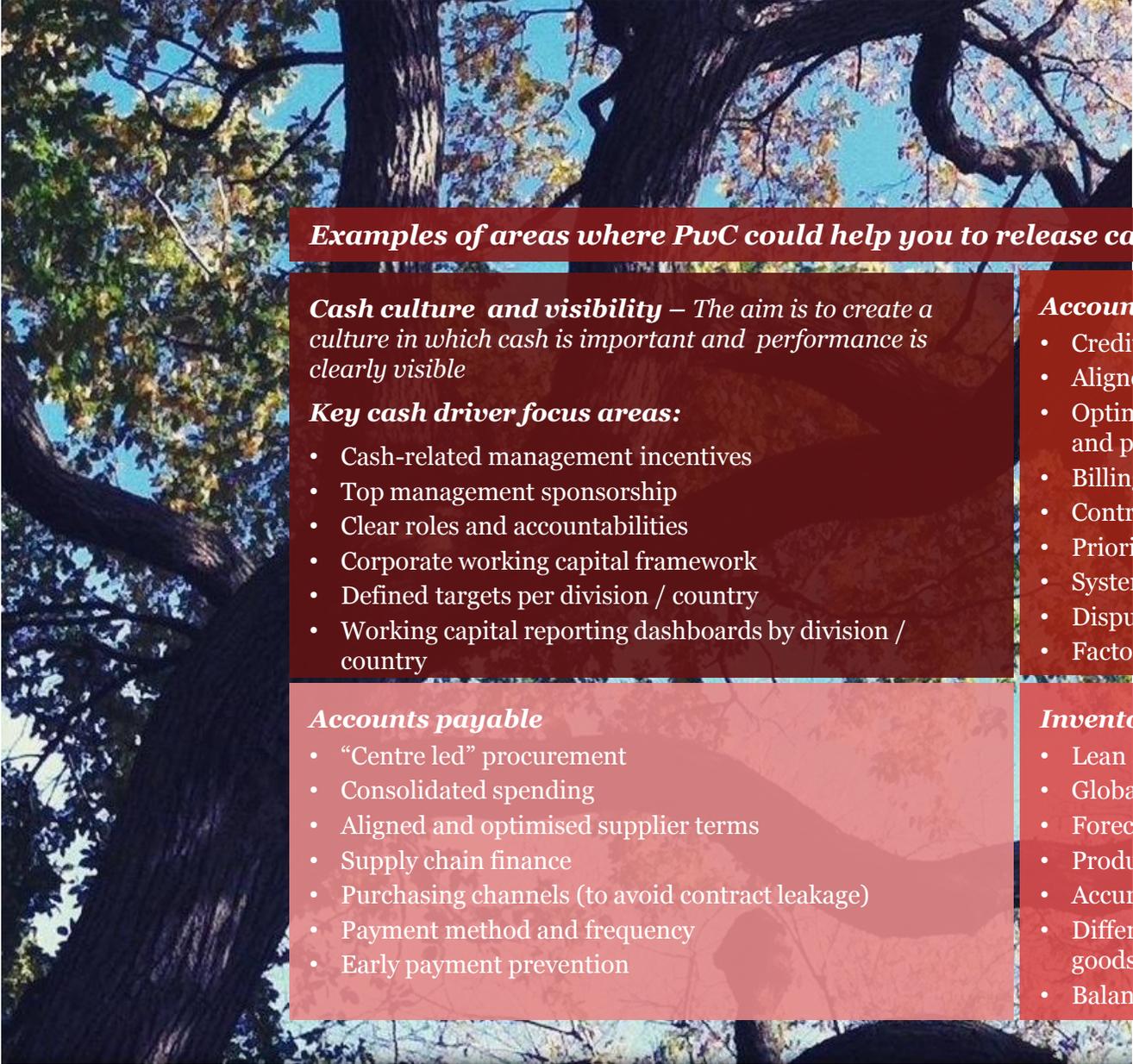
Retailers need to become increasingly competitive and as they move their businesses online, additional funding will be needed for development...

How can we support you?

- 1.** PwC can complete a working capital benchmarking exercise to compare your performance against your peers and identify potential improvement opportunities.
- 2.** We can perform a diagnostic review to identify “quick wins” together with longer-term working capital improvement opportunities.
- 3.** Develop detailed action plans for implementation to generate cash and make sustainable improvements.
- 4.** Assist the realisation of sustainable working capital reduction by implementing robust, efficient and collaborative processes.

How to address the key levers:

- Identification, harmonisation and improvement of commercial terms.
- Process optimisation throughout the end-to-end working capital cycles.
- Process compliance and monitoring.
- Creating and embedding a “cash culture” within the organisation, optimising the trade-offs between cash, cost and service.



Examples of areas where PwC could help you to release cash from working capital

Cash culture and visibility – *The aim is to create a culture in which cash is important and performance is clearly visible*

Key cash driver focus areas:

- Cash-related management incentives
- Top management sponsorship
- Clear roles and accountabilities
- Corporate working capital framework
- Defined targets per division / country
- Working capital reporting dashboards by division / country

Accounts payable

- “Centre led” procurement
- Consolidated spending
- Aligned and optimised supplier terms
- Supply chain finance
- Purchasing channels (to avoid contract leakage)
- Payment method and frequency
- Early payment prevention

Accounts receivable

- Credit risk policies
- Aligned and optimised customer terms
- Optimised customer marketing agreements and processes
- Billing timeliness and quality
- Contract and milestone management
- Prioritised and proactive collection procedures
- Systems-based dispute resolution
- Dispute root cause elimination
- Factoring

Inventory

- Lean and agile supply chain strategies
- Global coordination
- Forecasting techniques
- Production planning
- Accurate tracking of inventory quantities
- Differentiated inventory levels for different goods
- Balanced cash, cost and service

Our approach to sustainable working capital...

Change management

Establish a more cash-focused culture that is able to sustain the higher levels of performance and drive continuous improvement.

Stakeholder management

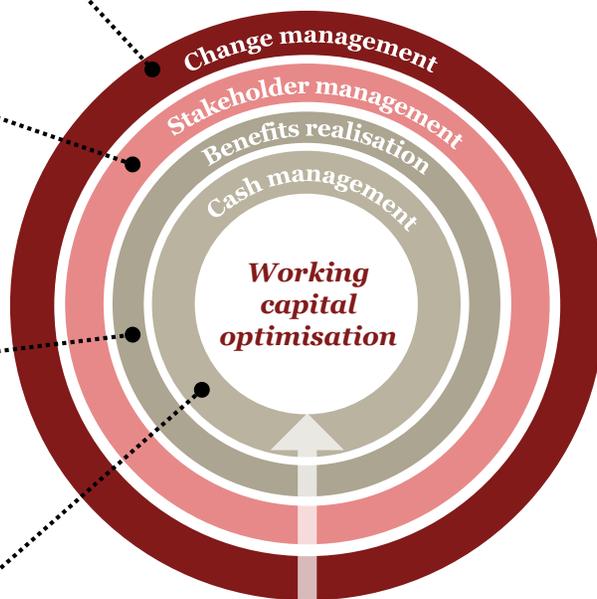
Ensure that key stakeholders remain engaged during the project.

Benefits realisation

Ensure that cash generation objectives are achieved and maintained.

Cash management

Ensure effective utilisation and forecasting of cash.



We supplement our working capital and cash management methodologies with core consulting approaches to make sure that improvements are tangible and sustainable.

Case study: Operational working capital improvement programme for a rapidly expanding online fashion and shoe retailer

The key issue

The company had faced historical problems from fraud and high inventory levels which had impacted the working capital performance and created challenges in planning and forecasting future working capital levels.

How we helped

An internal project was launched to establish a working capital dashboard in order to improve the central tracking of working capital developments together with obtaining operational insights into the strengths, weaknesses and opportunities of the capital efficiency.

We created a combined team of working capital specialists and SAP data analytical experts to develop an IT-based dashboard solution with the client.

We performed a total working capital diagnostic review, including procure to pay (creditors), forecast to fulfil (inventories) and order to cash (debtors), following which we held joint workshops with the client process owners. As a result we defined the best suited KPIs to provide the greatest visibility of future financial and operational needs.

During the 12-week project, the team also supported the client to establish a new working capital governance model.

The result

We identified gaps to leading practices within all processes and also increased working capital awareness across the entire organisation.

A fully interactive SAP design studio working capital dashboard was created with smart financial and operational KPIs.

The company had improved visibility of its working capital performance and the possibility to drill down further on a granular level (by supplier / customer).

Process recommendations were identified and linked to financial and operational KPIs (for further monitoring).

Working capital experts and contact details



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Co-author of the study



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Glossary

Metric		Basis of calculation	
NWC % (net working capital %)	<i>NWC % measures working capital requirements relative to the size of the company.</i>	(Accounts receivable + inventories – accounts payable) / sales	<p>Methodology Retail data is based on publicly available data (CapitalIQ) of top 40 companies in the German, Swiss and Austrian retail sector, according to Capital IQ sectorisation.</p> <p>The division of sub-sectors is based on Capital IQ Primary Industry classification (data available for 100% of sample).</p>
NWC days (net working capital days)	<i>Indication of the total days to complete the full cash conversion cycle.</i>	(accounts receivable + inventories – accounts payable) / sales x 365	
DSO (days sales outstanding)	<i>DSO is a measure of the average number of days that a company takes to collect cash after the sale of goods or after services have been delivered.</i>	Accounts receivable / sales x 365	
DIO (days inventories on-hand)	<i>DIO gives an idea of how long it takes for a company to convert its inventory into sales. Generally, the lower (shorter) the DIO, the better.</i>	Inventories / cost of goods sold x 365	
DPO (days payables outstanding)	<i>DPO is an indicator of how long a company takes to pay its trade creditors.</i>	Accounts payable / costs of goods sold x 365	



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