SimpliCapital

Simple AI for Finance

GROW MARGINS BY TURBO-CHARGING ACCOUNT RECEIVABLES (AR) MANAGEMENT

"There is no sale till you collect", is a well-known adage in business. No surprise then that Account Receivables (AR) Management is one of the most critical activities for a company and Days Sales Outstanding (DSO) is the best metric to appraise the effectiveness of an AR strategy.

We analyzed over 1,200 publicly traded US companies and found significant variations not only across, but within industry sectors. The best performing companies have 6X better performance going right to their bottom line. A company can significantly reduce their capital cost or leverage investment opportunities by minimizing their DSO.

Our research suggests that the challenges to understanding and improving performance include short-staffed finance departments and fragmented data with limited use of analytics to predict payment behavior. Payment terms negotiated without payment behavior analysis also lead to less-than-ideal outcomes.

Finance managers can easily adopt a simple 6-step process to significantly improve DSO. It's founded on building a connection directly to ERPs, and utilizing AI based models to guide proactive actions to minimize past dues. A comprehensive package of on-demand analysis and reports enables finance managers to improve payments terms and past dues.

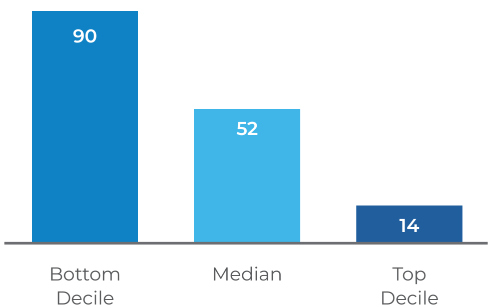
SimpliCapital's AI-based system provides finance managers intelligent and powerful tools to improve DSO and DPO, and significantly reduce their cost of working capital.

Why Top performing companies have 6X better DSO

Days Sales Outstanding (DSO) is a key indicator of how well a company manages its receivables. Of the 1,200 companies that we analyzed, the top performing companies have a DSO of 14 days or less; the corresponding figure for bottom performing companies' is over 90 days (Fig 1).

Fig. 1: Days Sales Outstanding (DSO)

Publicly Traded US Companies



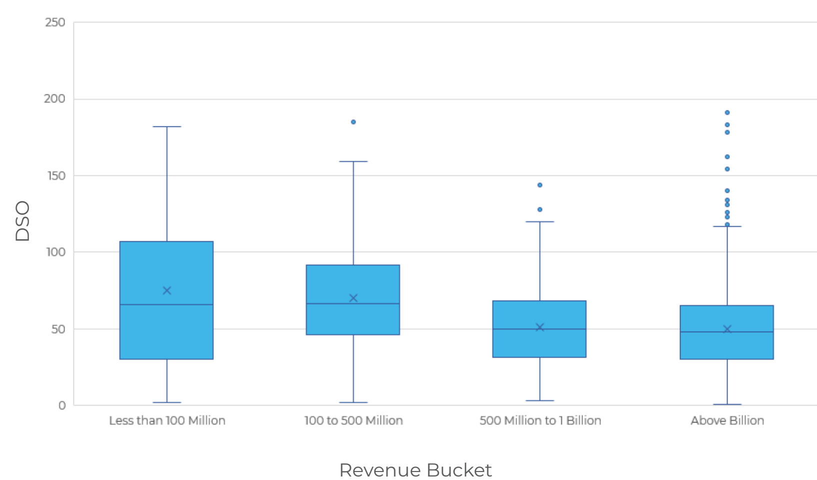
The higher the DSO, the bigger is a company's Accounts Receivable. To illustrate, company A with a 90 day DSO and credit revenue of $100M will have about $25M Account Receivables on their balance sheet and could incur a $0.5M capital cost which directly impacts their pre-tax income.

Company B with similar revenue but with a top decile DSO will have only $14M Account Receivables and would incur only $150K capital cost. If Company A improves their DSO to the top decile, it can save about $350K annually or an average **improvement in pre-tax income by 3-5%.**

Currently, we find significant variations across sectors in companies' DSO performance with a standard deviation of 30 days. Barring exceptions, Manufacturing, Construction, and Services sectors fare the worst by far with larger past dues and longer payment terms.

Interestingly, larger companies manage their DSO better than smaller companies (Fig 2). We believe that they typically deploy significant resources to minimize their DSO. On the other hand, smaller companies are unable to deploy their limited resources and have limited negotiating power to minimize their DSO.

Fig. 2: Days Sales Outstanding (DSO)



Lack of collection transparency and payment uncertainty drives poor DSO performance

Minimizing DSO is not a trivial problem for most companies. There are two key elements that affect DSO.

- **Past Dues** - The best performing companies track customer dues diligently and allocate significant resources to minimize DSO whereas poor performing companies lack data transparency and/or resources allocated towards collections
- **Payment terms** - The best companies strategically offer payment terms to win highly competitive deals whereas poor performing companies use payment terms as a competitive advantage but rarely truly understand the overall financial impact

In addition, our research confirms that DSO performance is confounded by multiple factors:

- Finance teams are short-staffed and therefore, focus on a few large issues, or on improving averages, but do not benchmark with best-in-class performance
- Invoice collection data is not available in real-time
- Most firms use manual spreadsheets to track receivables
- Lack deeper insights into payment behavior and predictability
- Deploy reactive collection tactics after payments are past due date
- Inconsistent payment terms with respect to customers' payment behavior
- Inability to access digital tools to analyze, predict and manage their AR portfolio

Given these manifold challenges, what can finance managers do to improve AR and DSO performance? Below, we outline 6 steps to improve AR performance.

6 steps to build a best-in-class Account Receivables (AR) process

The key drivers of less-than-optimal performance are understandable with the limited tools that most organizations are currently using. In order to make immediate and measurable improvements, the following steps should be taken.

1. Create **data transparency** by directly connecting to the company's ERP system. Accurate and real-time AR data enables finance managers to track past dues and take corrective actions quickly and is the foundation for building a best-in-class AR process

2. Build **predictive analytics** to proactively identify past dues before it is too late. Using previous payment behavior, Artificial Intelligence based systems can accurately predict “who” would and “when” a payment will be made. Alerts from such systems can signal problems allowing finance managers to act preemptively
3. Design a **balanced collections contact strategy** to minimize past dues. Our research suggests that most customers pay on-time if contacted proactively. On the other hand, an aggressive contact strategy can lead to customer abrasion. Utilizing predictive analytics, finance managers can optimize their collections contact strategy while maintaining a high-quality client relationship
4. Create **customer tear-sheets** to estimate the long-term impact of payment terms and behavior on overall customer profitability. These on-demand reports include life-time relationship data and market benchmarks enhancing the ability to negotiate more attractive payment terms
5. Negotiate **attractive payment terms** with customers. Armed with customer tear-sheets and predictive analytics, finance managers and sales teams can negotiate best-in-class payment terms
6. Deploy a **real-time payment platform** to accept customer payments. Introducing one-click payment capabilities creates a much improved customer experience and drives faster time-to-cash

Once this 6-step process is fully implemented, companies will have a virtuous cycle of measurable improvements. Companies can also use AR financing to improve their DSO. However, it typically comes at a cost without improving inherent shortcomings. We believe companies should focus on improving their AR process and payment terms before using AR financing.

Where do we fit in?

SimpliCapital delivers an AI based system to enable best-in-class AR and AP performance

SimpliCapital’s integrated system is designed to empower finance managers to dramatically improve AR and AP performance, and as a result reduce working capital costs for the company.

We recognize that accurately predicting cash availability is a complex task. The lack of accurate predictions drives most CFOs to keep large cash buffers in their bank to pay suppliers, employees, and creditors, akin to the inventory that a manufacturing organization builds to protect from uncertainties. However, the more predictable a system, the less there is a need for a buffer

SimpliCapital's intuitive user interface connects directly with the company's ERP system to predict cash availability. A library of AI models automatically trains on a company's data, and accurately predicts cash availability from each outstanding invoice to allow finance managers to initiate a proactive contact strategy to minimize past dues. An on-demand tear-sheet on each customer enables sales and finance teams to negotiate better payment terms. Our integrated AP optimization module recommends supplier payment dates to maximize Days Payable Outstanding and early payment discounts. An integrated payment platform supports 135+ currencies and enables automatic cash reconciliation and application.

With SimpliCapital, Finance managers can turbo-charge their ability to improve DSO and DPO, and positively impact their company's bottom line.

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