



cutting through complexity

Credit Management embedded as STRATEGIC PARTNER

Results of Credit Management Survey

14/10/2015

Christian Pauwels





cutting through complexity

KPMG Management Consulting



Relevance of management consulting

CFO



- Effective decision support
- Finance transformation

COO



- Procurement
- Supply chain
- Customer

HRO



- HR optimization
- Talent management
- Workforce optimization

Making KPMG
more relevant
to our clients

CIO



- IT function efficiency
- IT sourcing

CEO



- Operational strategy
- SSOA
- Enterprise wide cost
- Optimization

Management consulting: service lines





cutting through complexity

Credit Management embedded as STRATEGIC PARTNER

Results of Credit Management Survey

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Agenda

- ❑ **Working Capital & Credit Management**
- ❑ **Credit Management embedded as Strategic Partner**
 - ✓ Survey Questions
 - ✓ Survey Sample
 - ✓ Survey Executive Summary
 - ✓ Survey Results
 - ✓ Benchmark yourself

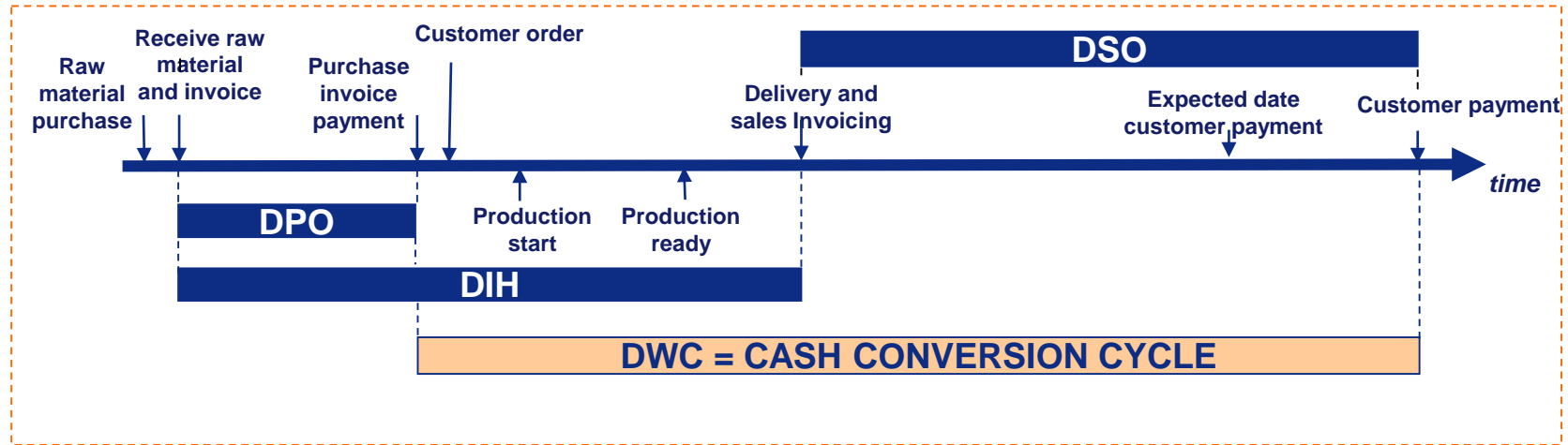
Content

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Internal stakeholders within Credit Management



The Cash Conversion Cycle and Credit Management



WORKING CAPITAL

+ Inventories (F2D)
+ Accounts Receivable (O2C)
- Accounts payable (P2P)
= Working Capital

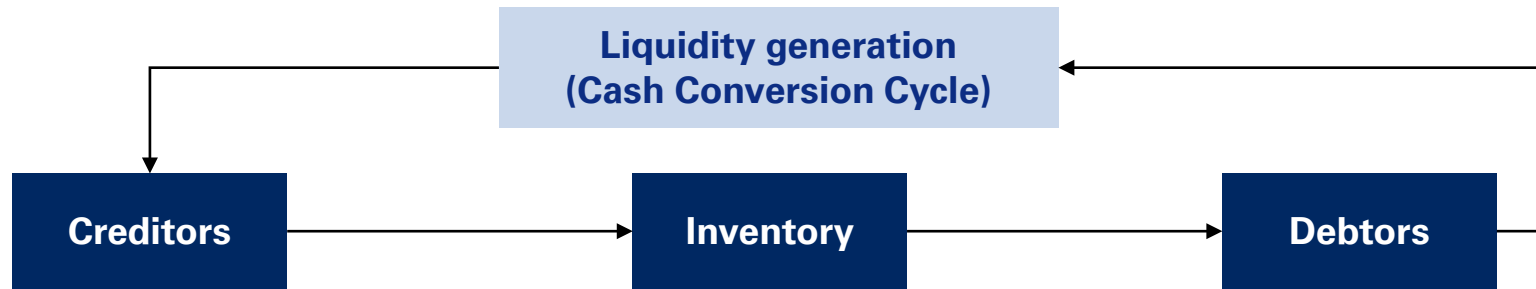
CASH CONVERSION CYCLE

+ Days Inventory Held (DIH)	=	$\frac{\text{Inventory}}{\text{Turnover}}$	X 360 days
+ Days Sales Outstanding (DSO)	=	$\frac{\text{Accounts Receivable}}{\text{Turnover}}$	X 360 days
- Days Payables Outstanding (DPO)	=	$\frac{\text{Accounts Payable}}{\text{Turnover}}$	X 360 days
= Cash conversion cycle	=	$\frac{\text{Inventories} + \text{AR} - \text{AP}}{\text{Turnover}}$	X 360 days

GOAL



Key Performance Indicators are a vital part of an integrated Cash Conversion Management Cycle



Purchase to Pay

- Days Payables Outstanding (DPO)
- Best possible DPO
- Percent early payment and percent payment to terms
- Percent spend via corporate agreements/contracts
- Spend by category
- Spend by customer type/segment
- Spend per functional FTE
- Transactions per functional FTE
- Transactions per supplier
- Spend/Sales ratio

Forecast to Deliver

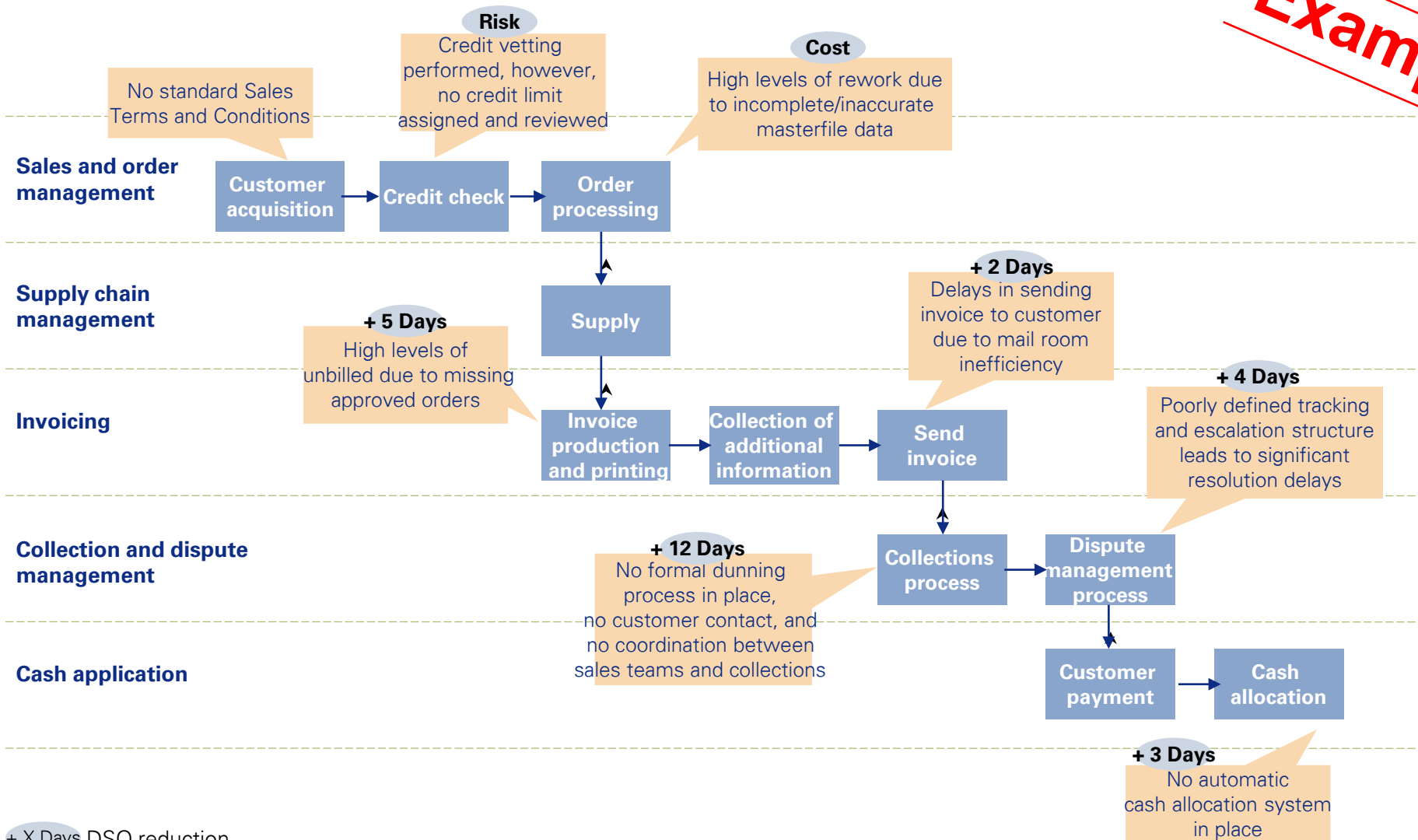
- Days Inventory Held (DIH)
- Inventory turns
- Delivery service levels
- Service levels
- Cash-to-cash cycle times
- Lead times
- Response times
- Fill rates
- Inventory management costs
- Rate/productivity of value add
- Returns rate and costs

Order to Cash

- Days Sales Outstanding (DSO)
- Best possible DSO
- Credit note - invoice ratio
- Percent of invoices in dispute by category
- Dispute resolution time
- Aging and AR rollover rate
- O2C functional headcount
- Pareto analysis of customer base
- Number of transactions by customer
- Transaction type per FTE

Cash leaks identification within cash Conversion cycle

Example



Credit Management Policies – procedures

EXAMPLE

Structure of debtors	Terms and conditions of payment	Overdue debtors
<ul style="list-style-type: none">■ Domestic/ export■ Countries■ Divisions■ Customers■ Age structure■ Sales responsibilities■ Credit risk■ Margins	<ul style="list-style-type: none">■ What Terms/ Conditions ?■ Who defines Terms/Conditions ?■ What are the avg paym terms ?■ How are prepayments handled ?■ Which payment methods exist ?	<ul style="list-style-type: none">■ Are dunning letters being used ?■ How often are customers dunned ?■ What happens after the pre-collection letters are sent out ?■ Are claims enforced by legal action ?■ How is sales department involved ?■ Root Cause analysis for over dues ?■ Which are the largest debtors ?■ How is credit ranking determined ?

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Survey Questions

Topic	Question / Statement
Policies & procedures	A written Credit Management Policy is defined in the company
	The Credit Management Policy is supported by the Board of Directors
	The Credit Management Policy updated on a regular basis
	The Credit Management Policy is available to all stakeholders
	The Credit Management Policy is embedded in our Customer Relationship (CRM) application
	The credit Management policy is integrated in our ERP application

Survey Questions

Topic	Question / Statement
Screening of customers	Is only applicable for orders above a specific amount eg. € 10,000
	Is based on financial ratios
	Is based on a cash flow analysis of the customer
	Is based on reports from external information providers
	uses other than financial information
	Cash payment for first order is mandatory
	For existing customers the credit policy prescribes - a periodic update of customer credit limits
	For existing customers the credit policy prescribes - a periodic update of customer payment conditions
	For existing customers the credit policy prescribes - a periodic risk analysis of the complete customer base
	For existing customers the credit policy prescribes - an ad-hoc risk analysis of specific customers

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Topic	Question / Statement
Role of Credit Management	credit management has an advisory role
	credit management has a decisive role
	credit management has a co-decisive role - 4 eyes principle
	Sales bonuses are influenced by customer payments
Credit Management Tasks	Customer risk assessment
	Personal contact with new customers to discuss credit limits
	Personal contact with existing customers
	Collaboration with external collection agencies
	Dispute management
	Initiate legal procedure
	Credit Management Reporting

Survey Questions

Topic	Question / Statement	
Credit Management is involved in	Offering cash discounts	
	Dispute management	
	Provisions for doubtful debtors	
	Amortization of bad debt	
	Approval of credit notes	
	Credit hold – delivery stop	
	Credit risk evaluation in proposal process	
	Credit Management & Authority	Who can overrule the decisions taken based on credit policy ?
		Who decides on credit hold / stop of delivery of goods or services ?
Who can overrule credit hold decision ?		
Credit Management & Organization	The credit management department is organized centrally at HQ.	
	The credit management is decentralized per subsidiary or country	
	The credit management department has full access to sales visit reports	

Survey Questions

Topic	Question / Statement
Reporting Lines	Credit Management direct report
	Credit Management 'dotted line' report
Techniques used by Credit Management :	Credit Insurance , Retention of title , L/C , Guarantees (parent company, bank , personal) , Factoring
Performance Indicators used	DSO , BDSO , CEI , ADL , Aging balance , % bad debt / TO , Frequency of credit limit overruling's
Education	
Competences	Financial statement analysis on credit risk
	Collection process
	Legal aspects related to credit management
	Tax aspects related to credit management
	Accounting
	IFRS
	Operational Cash flow modelling
	Global picture

Survey Questions

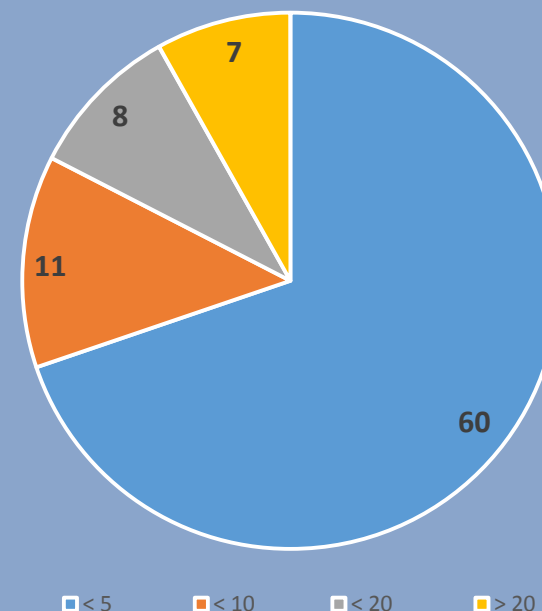
Topic	Question / Statement
Competences	Languages
	Bank instruments to limit credit risk
	Knowledge of customer industry
	Payment techniques
	Credit Insurance , VAT , Technical skills
	Soft Skills :communication , presentation , ...
Credit Management Practices	Cash discount , interest charged , collection cost charged
Career Path & Sourcing	

Survey Sample

First Release

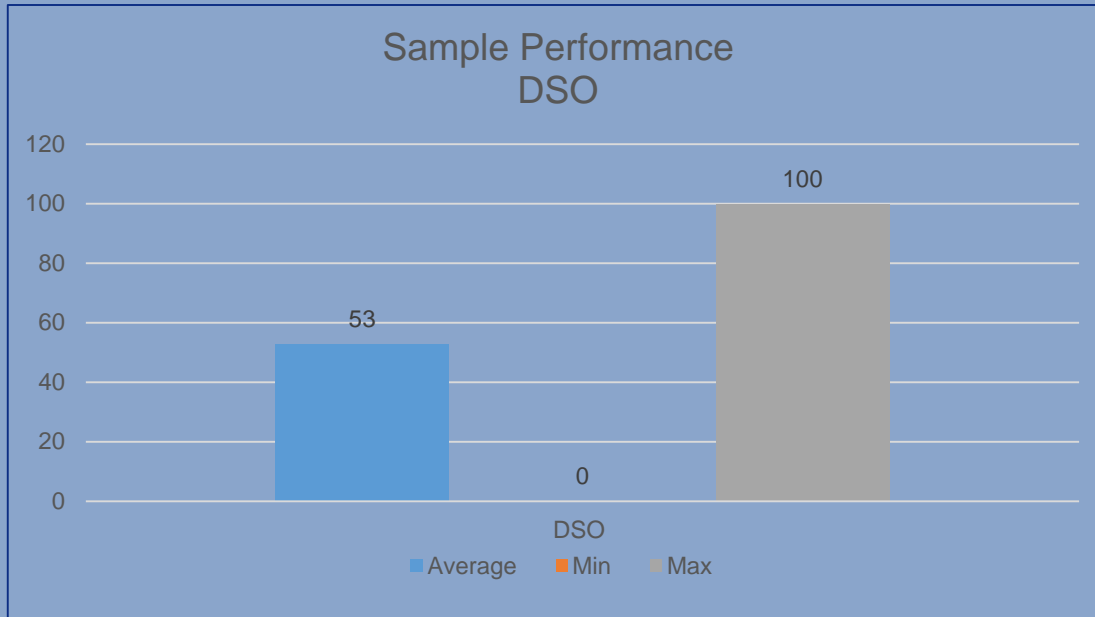
Companies	Number
Turnover > 250 mio	41
Turnover < 250 mio	44
Stock Quoted	34
Non-Stock Quoted	52
Belong to International Group	75
Non-International Group	12

Number of Credit Managers



All sectors represented with predominant companies from Industry sector

Survey Sample Performance in Credit Management



	DSO	Bad debt / turnover	% export	Coverage by credit insurance
Average	53	4%	38%	27%
Min	0	0,00%	0,00%	0,00%
Max	100	75%	100%	95%

Survey Sample

Practices applied in Credit Management



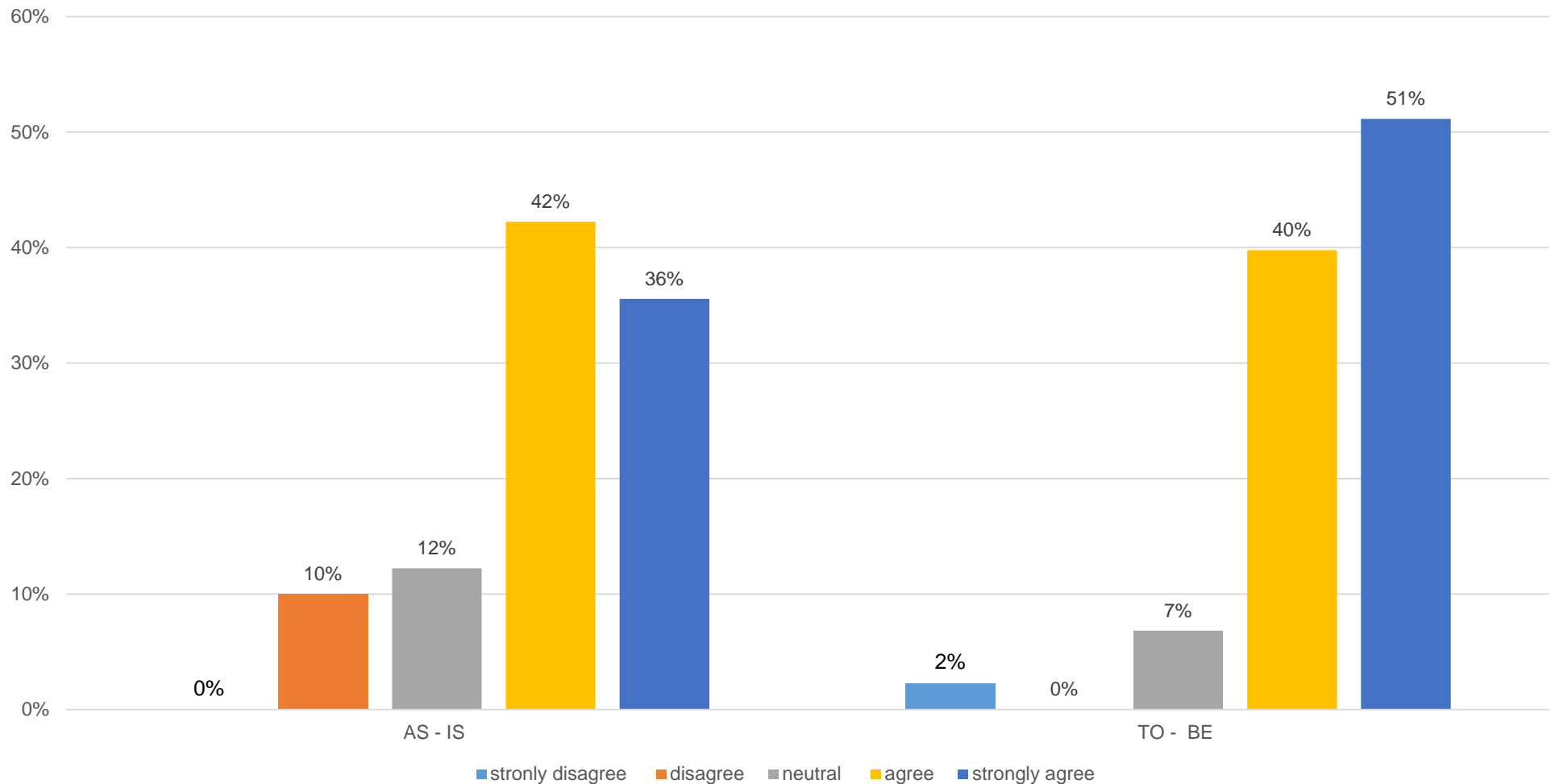
Survey Questions

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	The Credit Management Policy is supported by the Board of Directors
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	The Credit Management Policy is embedded in our Customer Relationship (CRM) application
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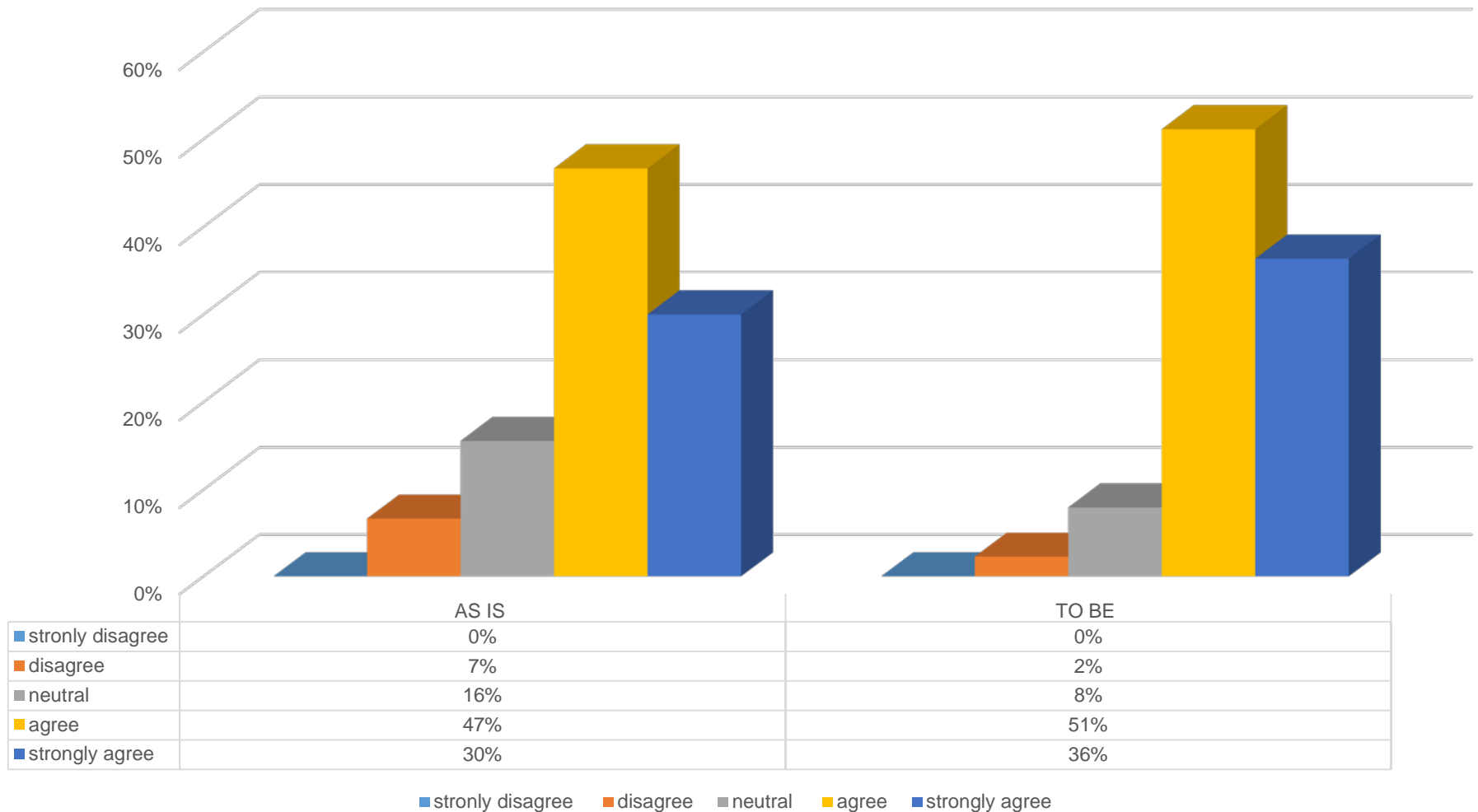
Executive Summary on Credit Management Policies

- In most companies a **WRITTEN Credit Management Policy** is defined and supported by directors or the board → but room for improvement
- The **Credit Management Policy** needs to be updated on a regular basis
- In the current situation we observe that the **Policy** is not available for all stakeholders
- The **Credit Management Policy** is not sufficiently embedded in our systems, although more in ERP than in CRM

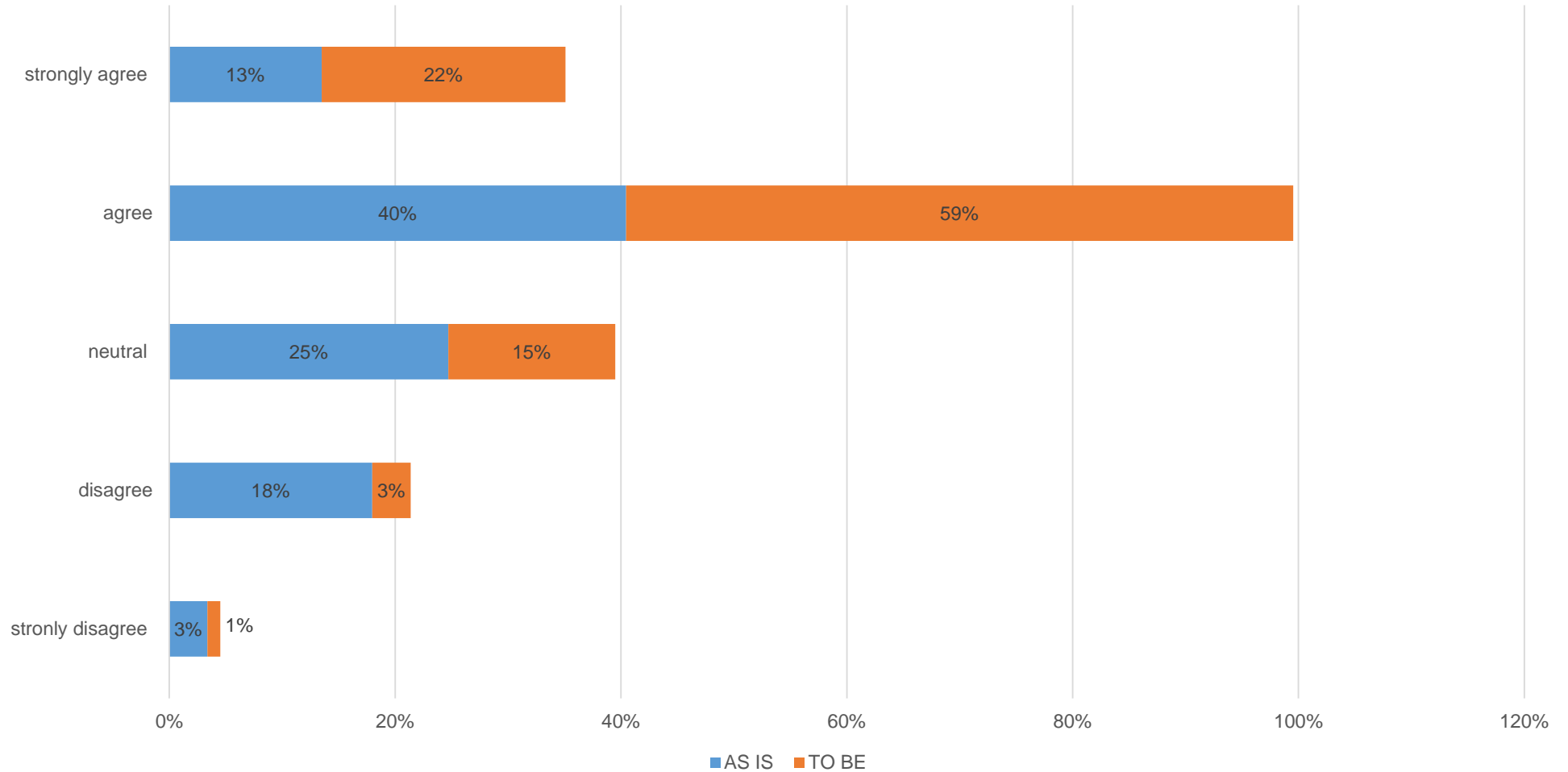
A written Credit Management Policy is defined in the company



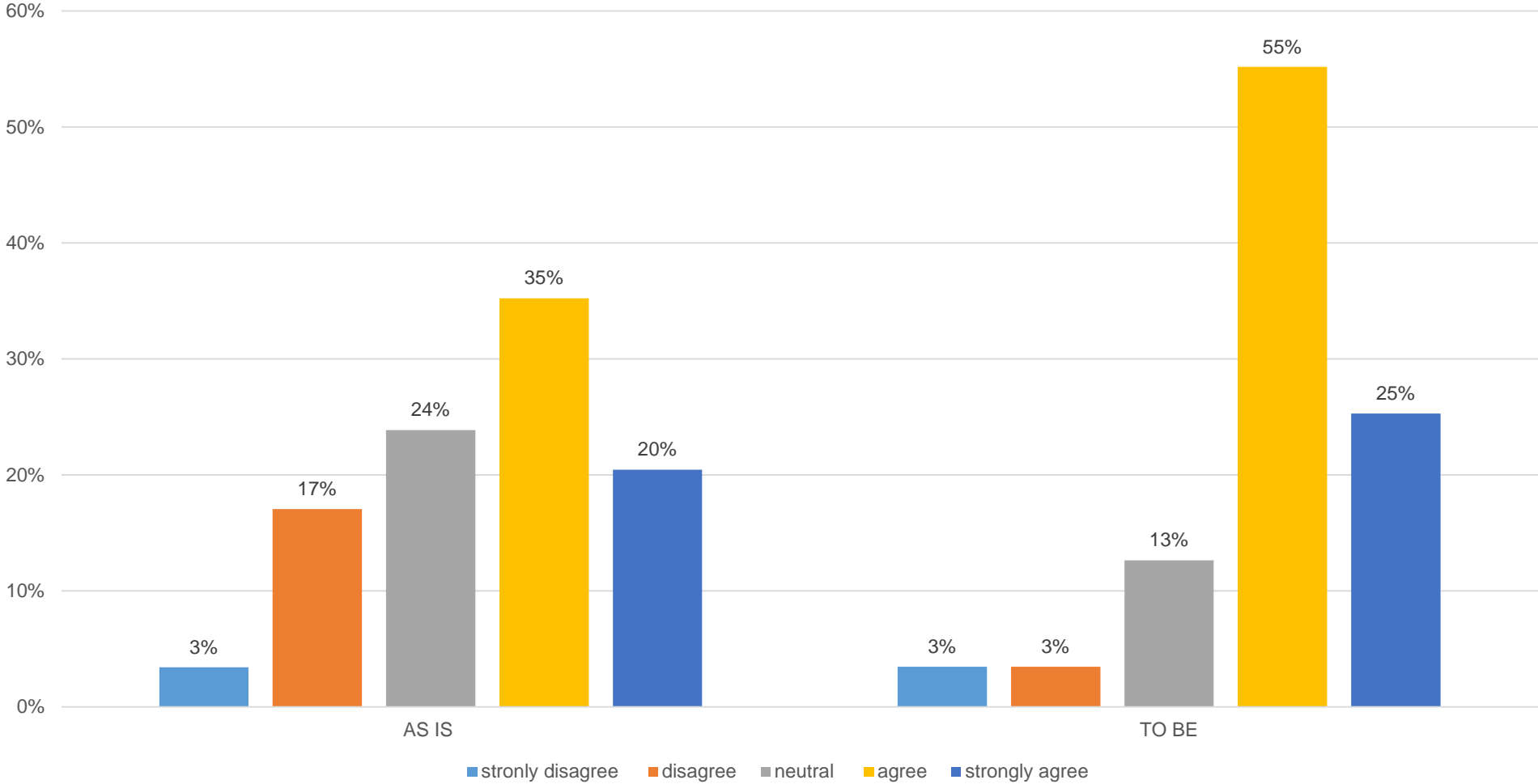
The Credit Management Policy is supported by the Board of Directors



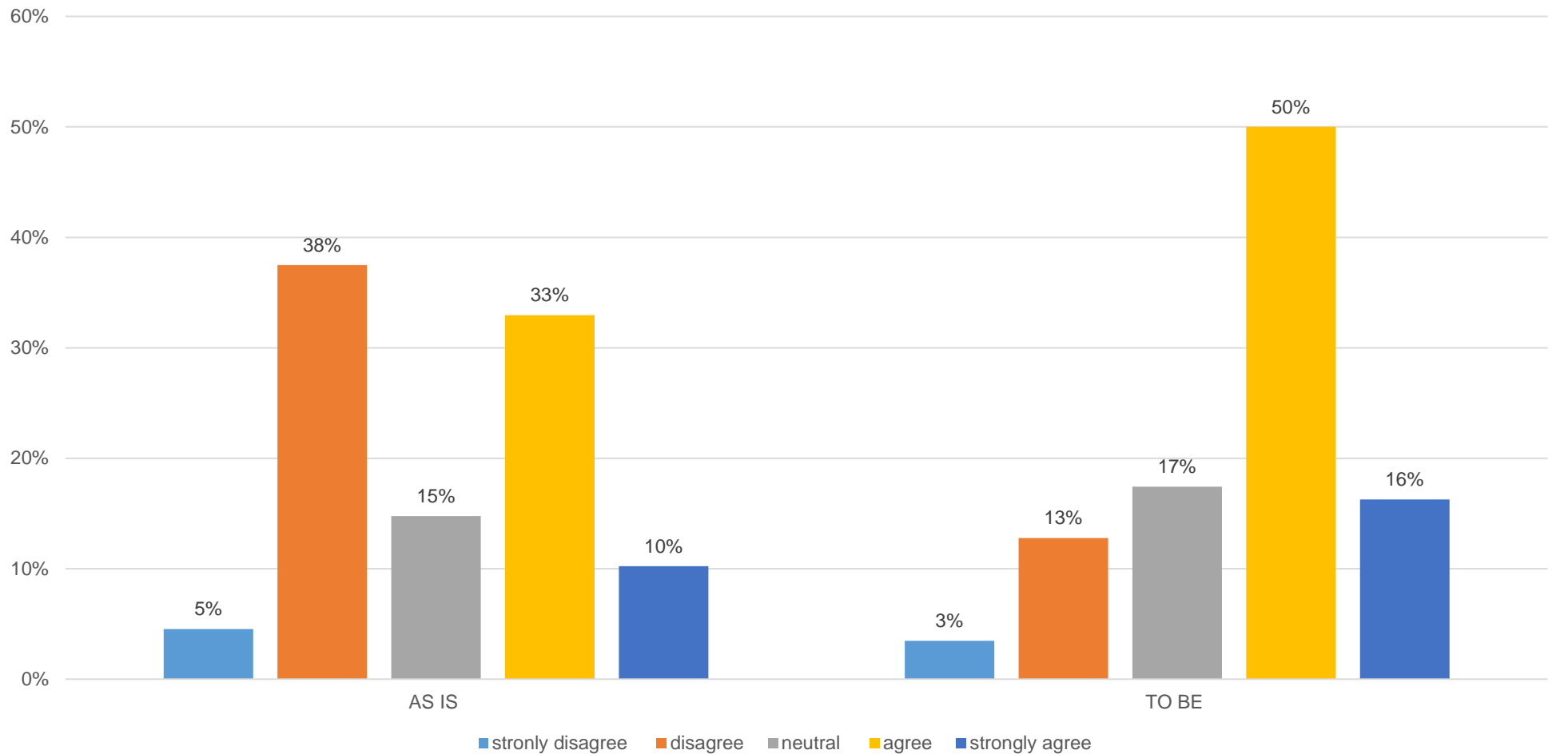
The Credit Management Policy is updated on a regular basis



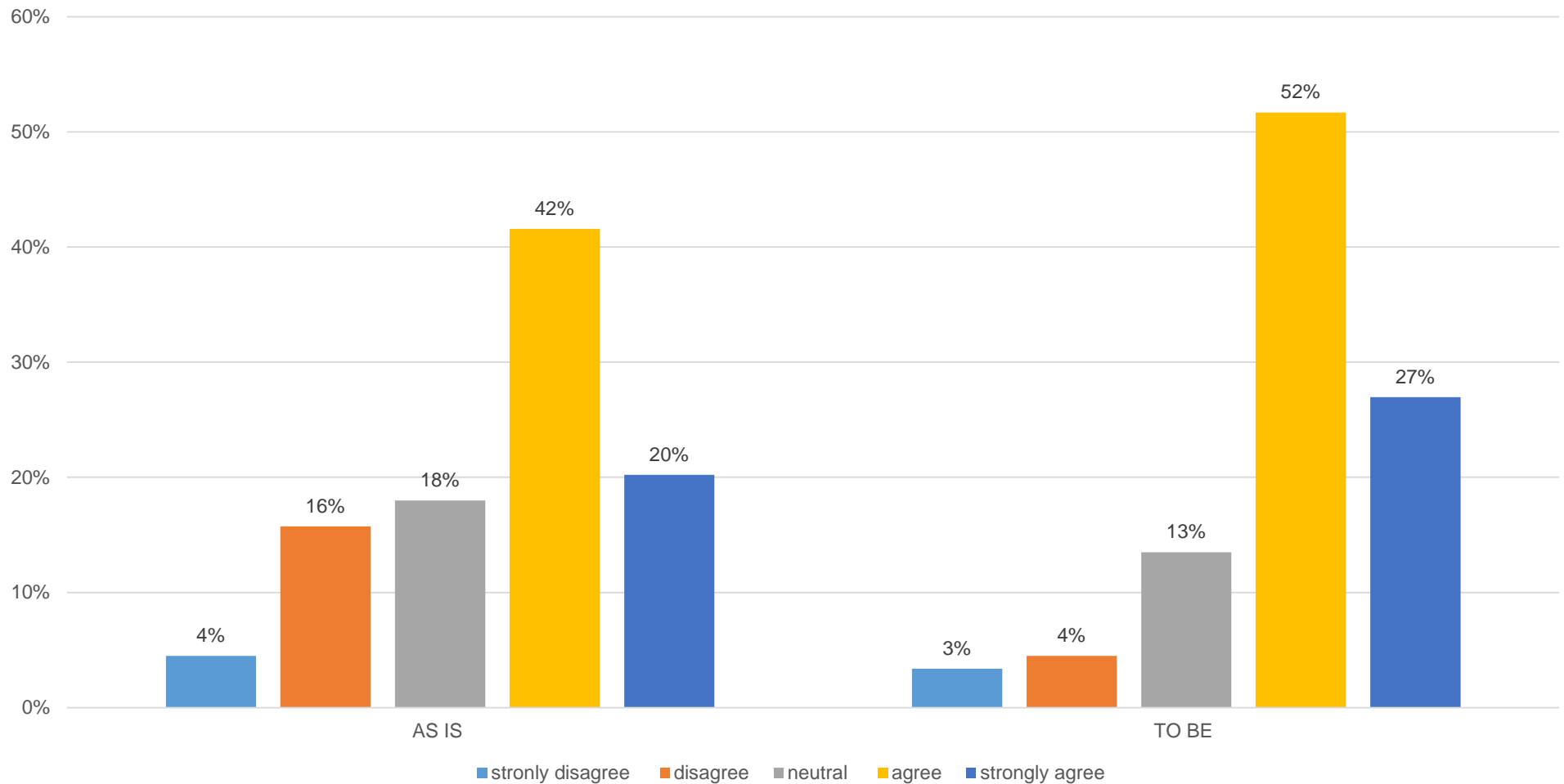
The Credit Management Policy is available to all stakeholders



The Credit Management Policy is embedded in our Customer Relationship (CRM) application



The credit Management policy is integrated in our ERP application



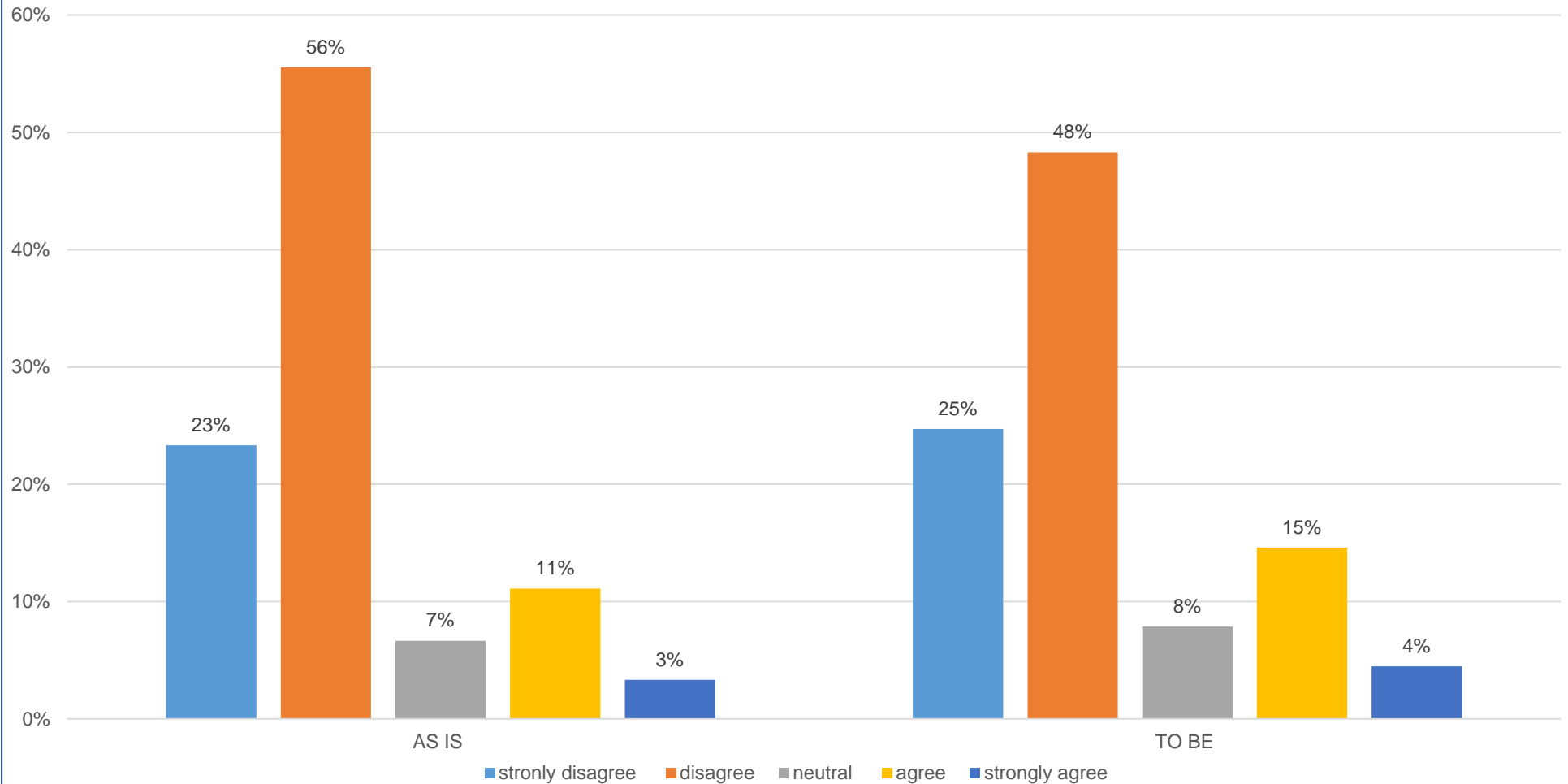
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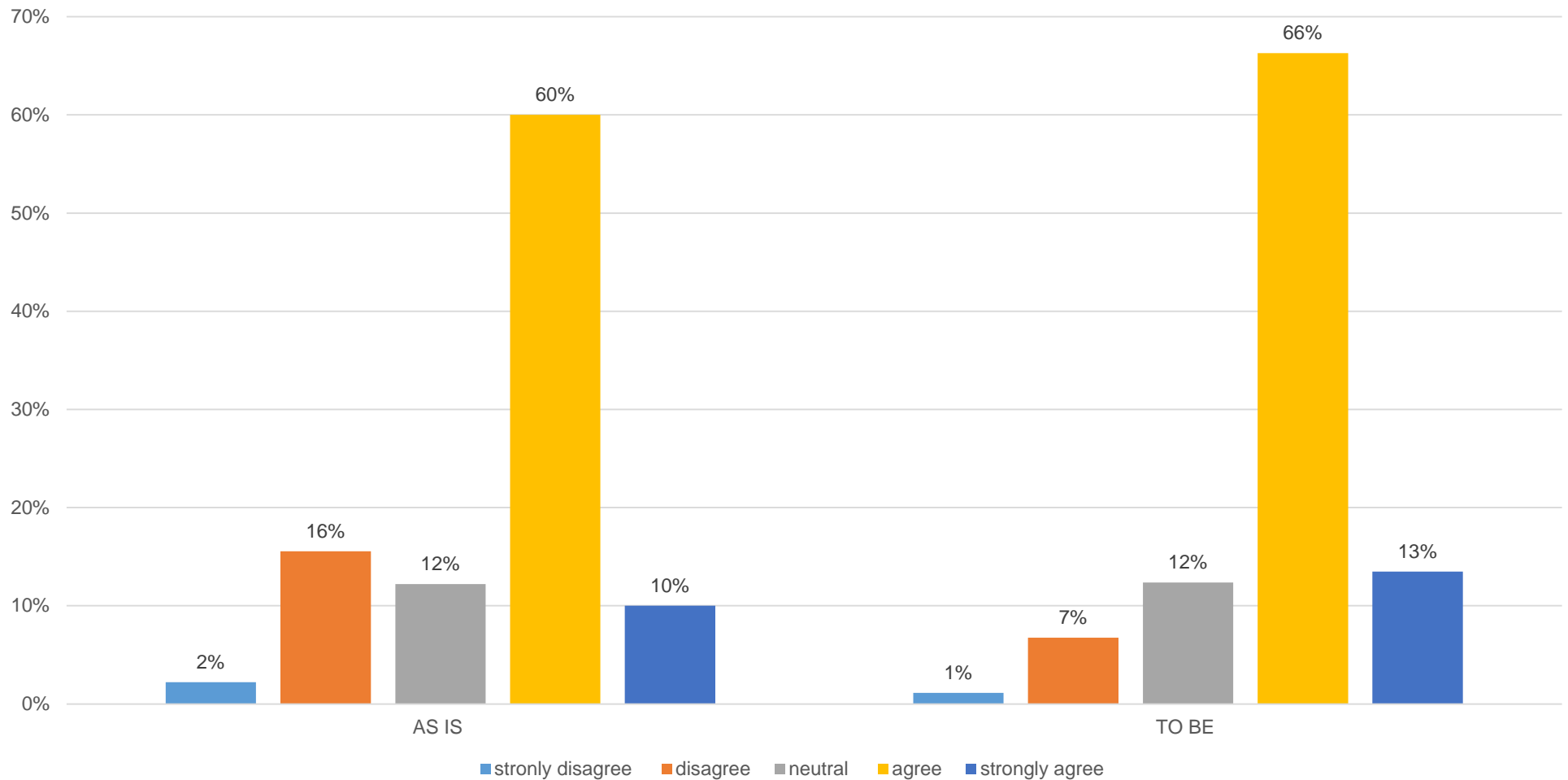
Executive Summary on Screening of customers

- ❑ **Screening of new customers is not limited to an amount of order intake**
- ❑ **Screening is based on financial ratio's from reports of external companies, but we want to move to more insight in the cash flow**
- ❑ **Screening is also based on non-financial information**
- ❑ **Cash payment for first order is not dominantly practiced**
- ❑ **For existing customers an update of credit limits is common practice, an update of payment conditions and risk analysis is currently exercised on an ad-hoc basis, but a trend towards common practice exists**

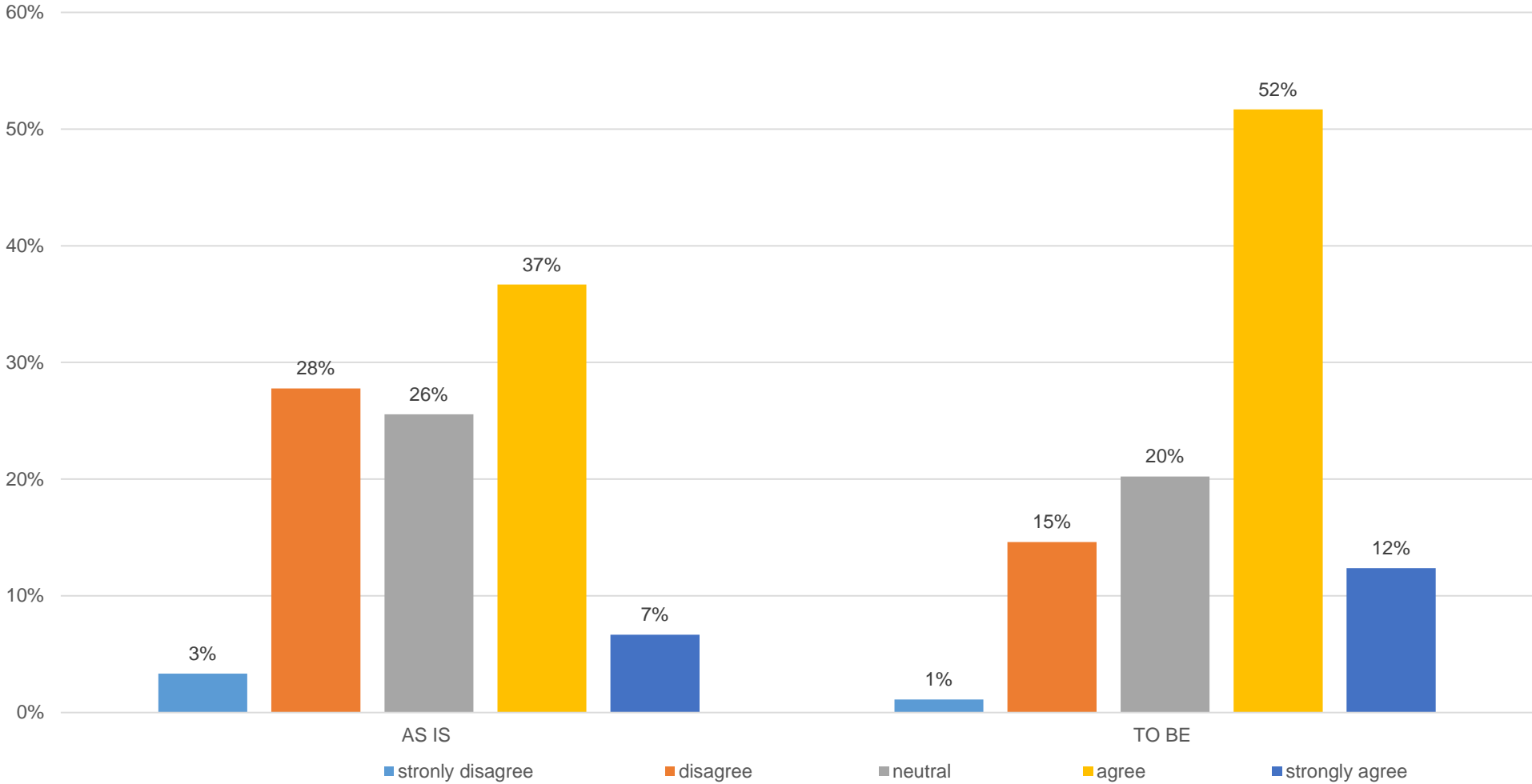
Screening of new customers - only applicabele for orders above a specific amount e.g. € 10,000



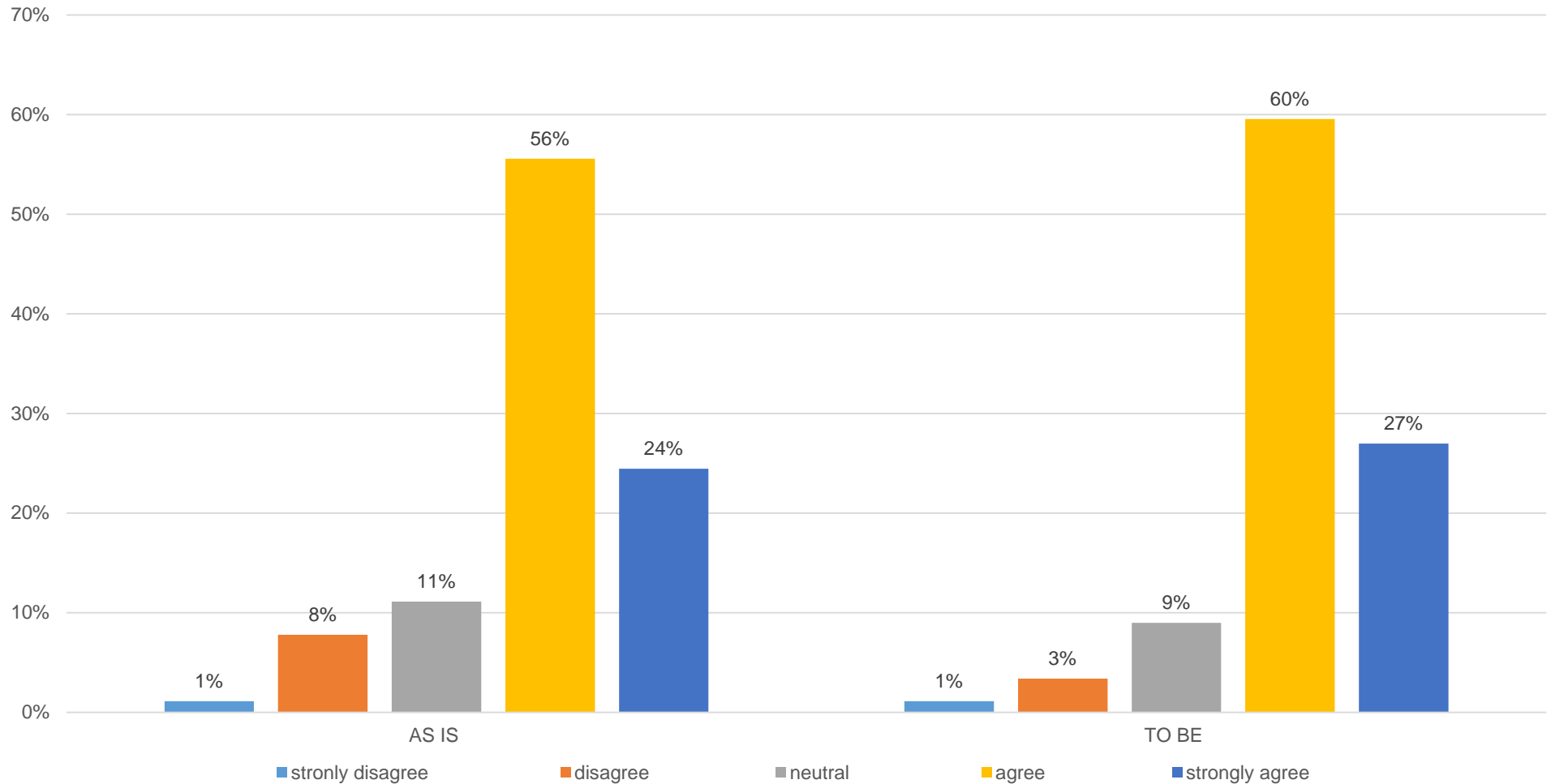
Screening of new customers - based on financial ratios



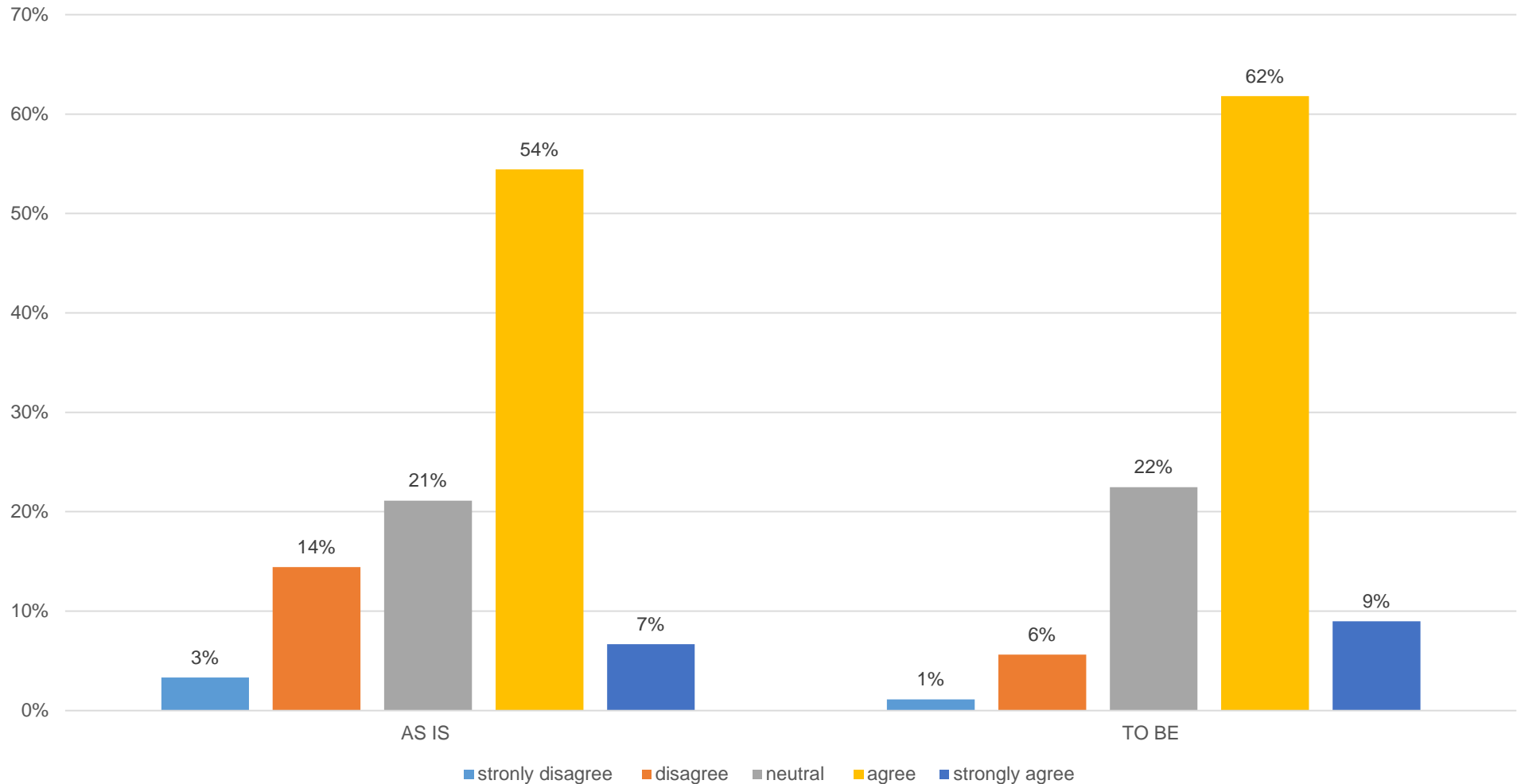
Screening of new customers - based on a cash flow analysis of the customer



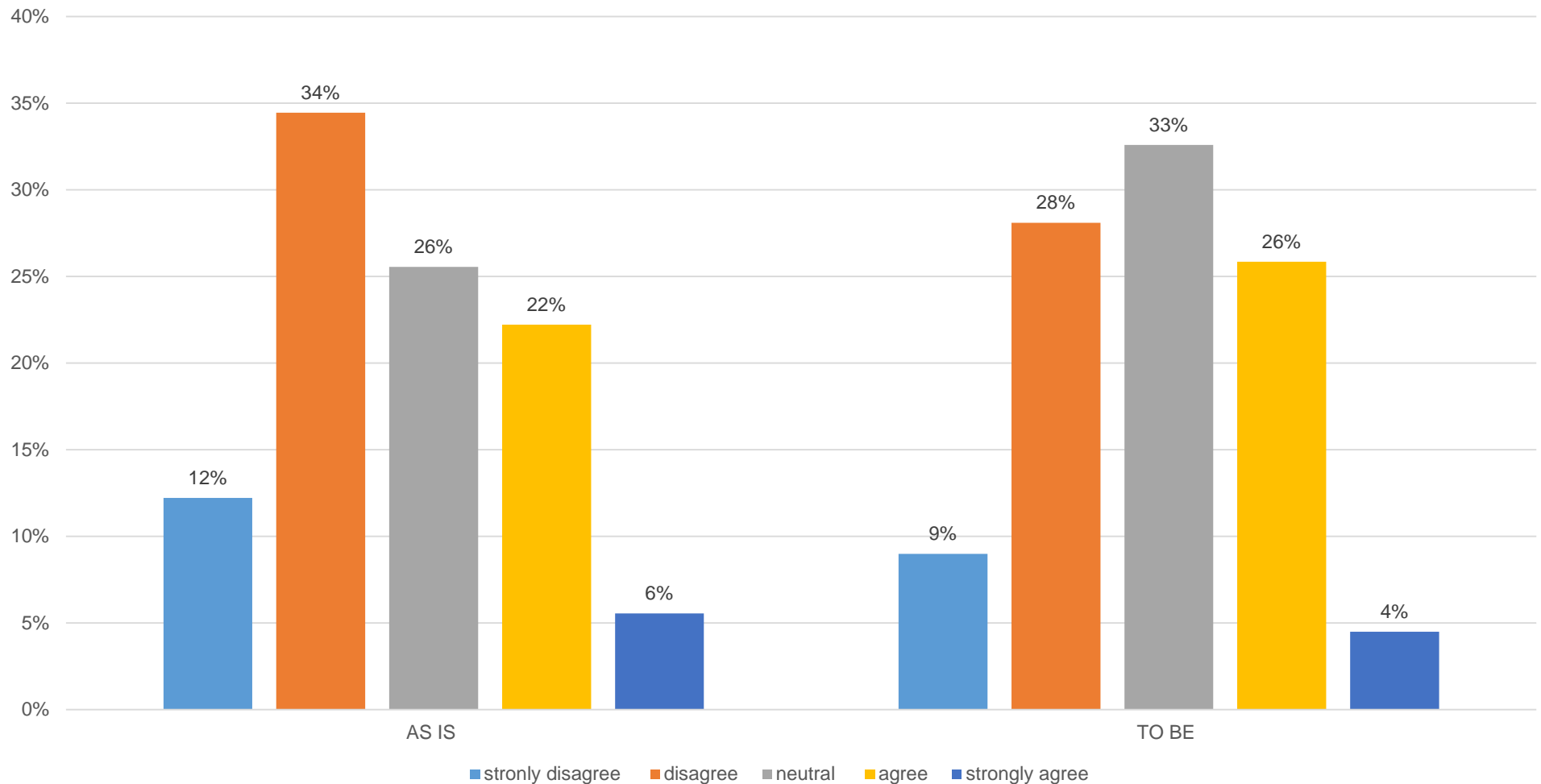
Screening of new customers - based on reports from external information providers



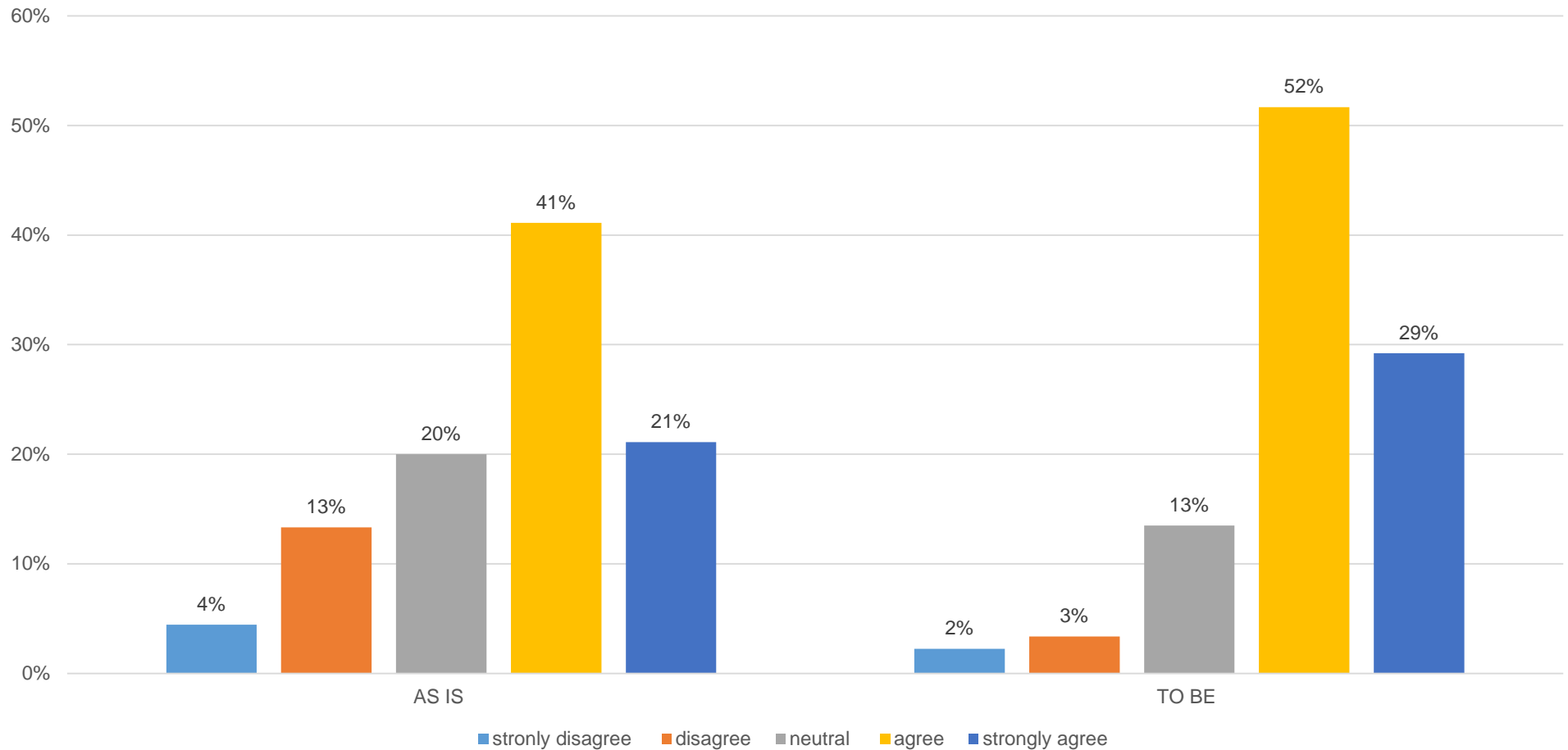
Screening of new customers - uses other than financial information



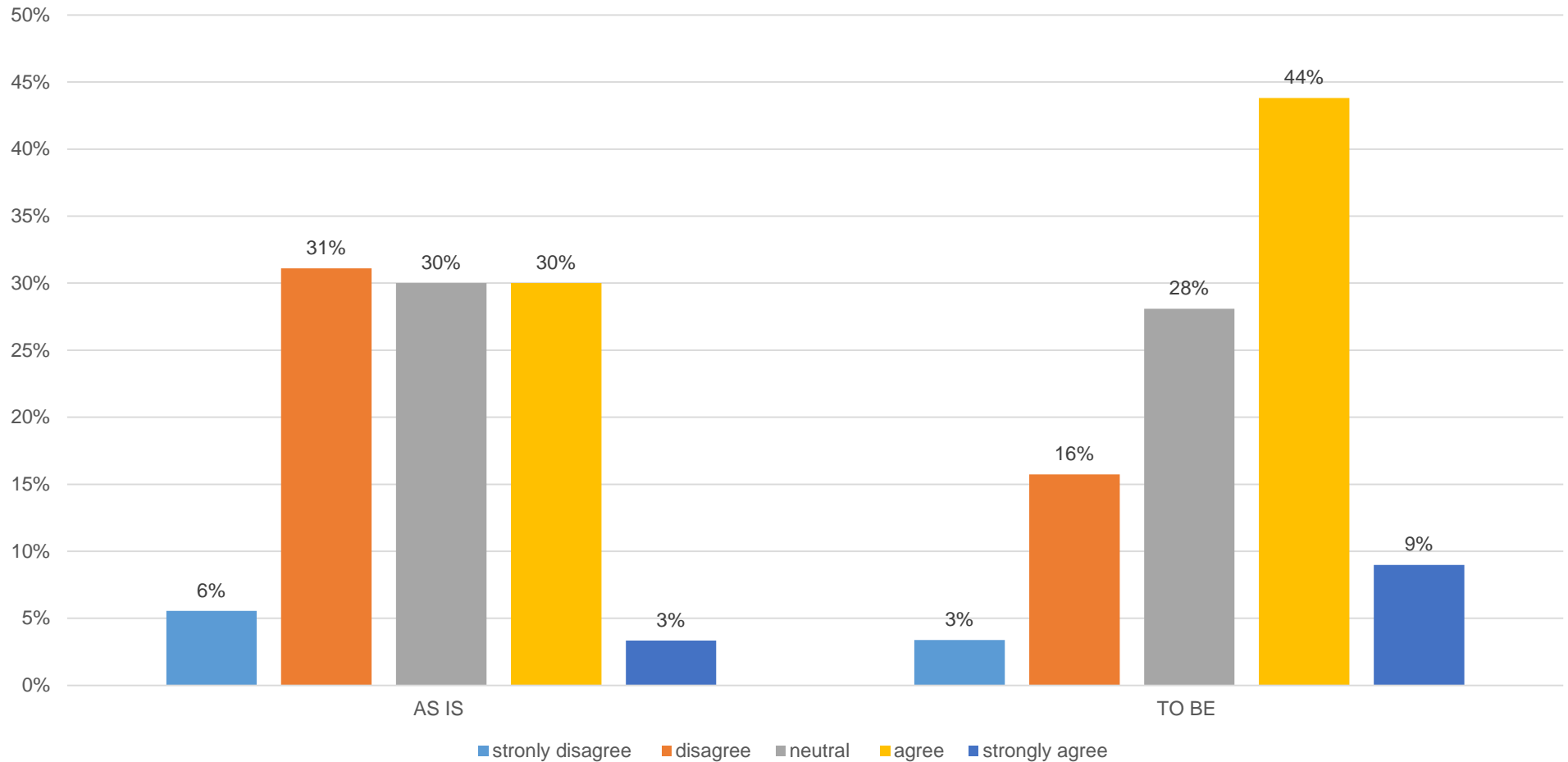
Screening of new customers - Cash payment for first order is mandatory



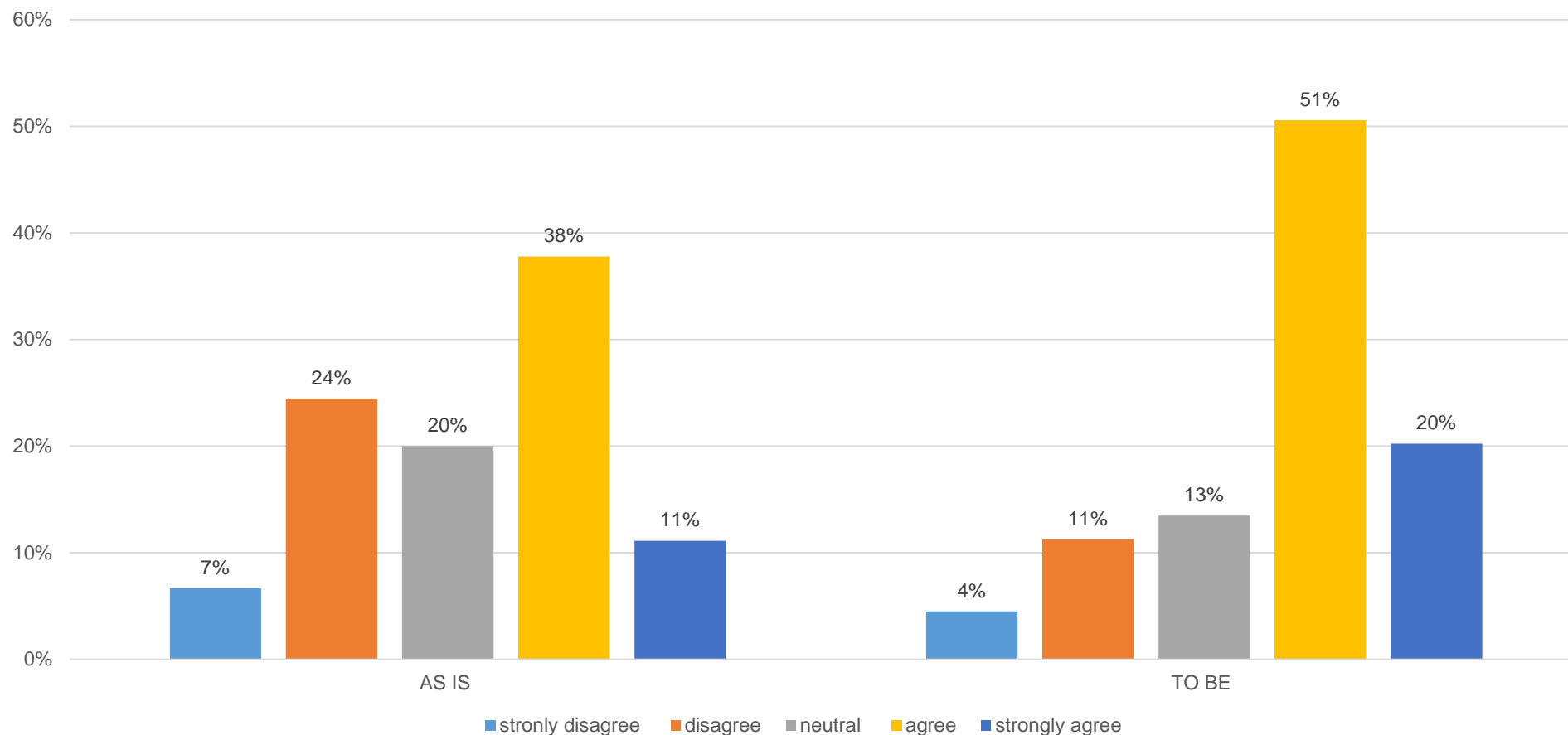
For existing customers the credit policy prescribes - a periodic update of customer credit limits



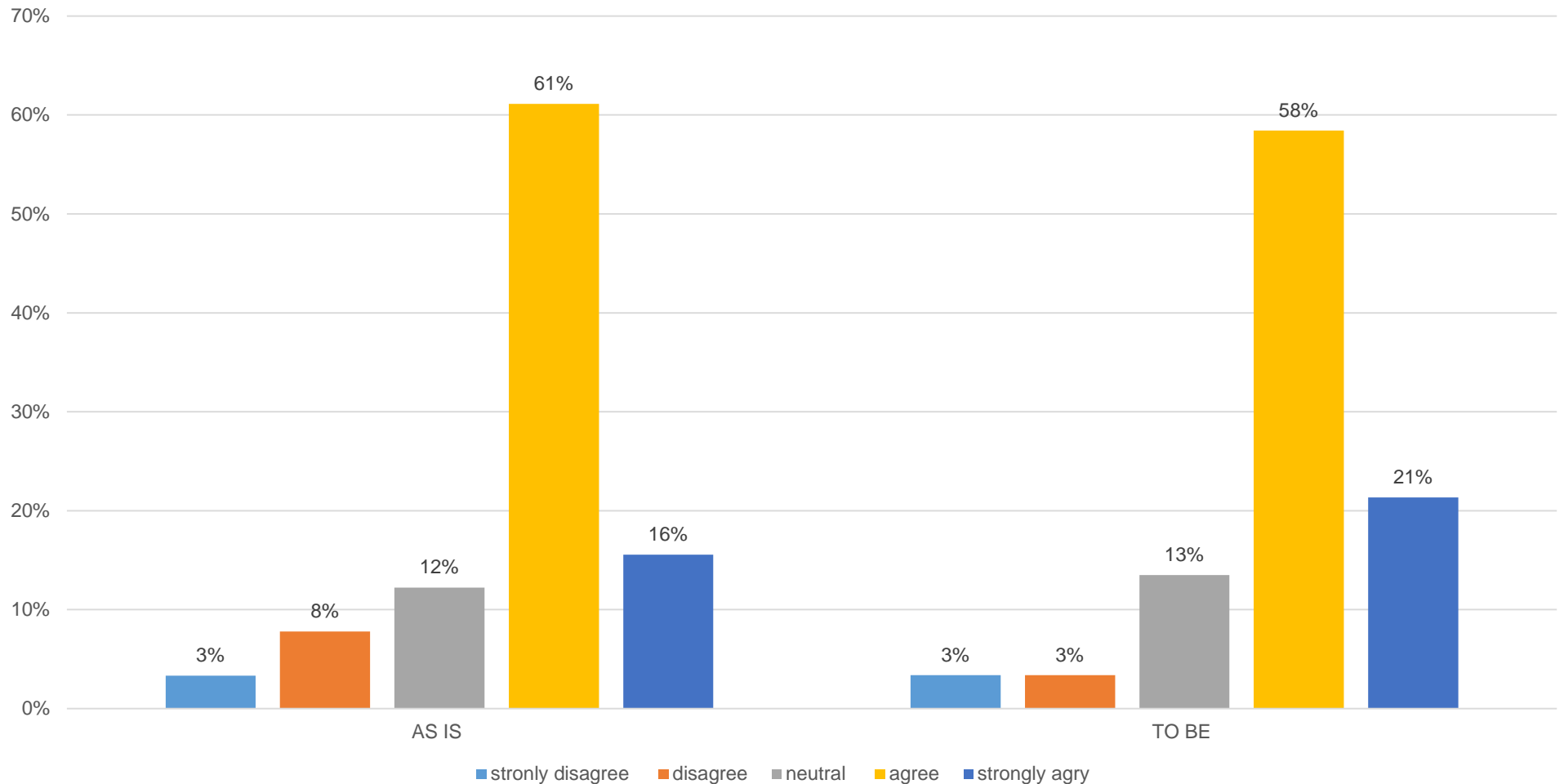
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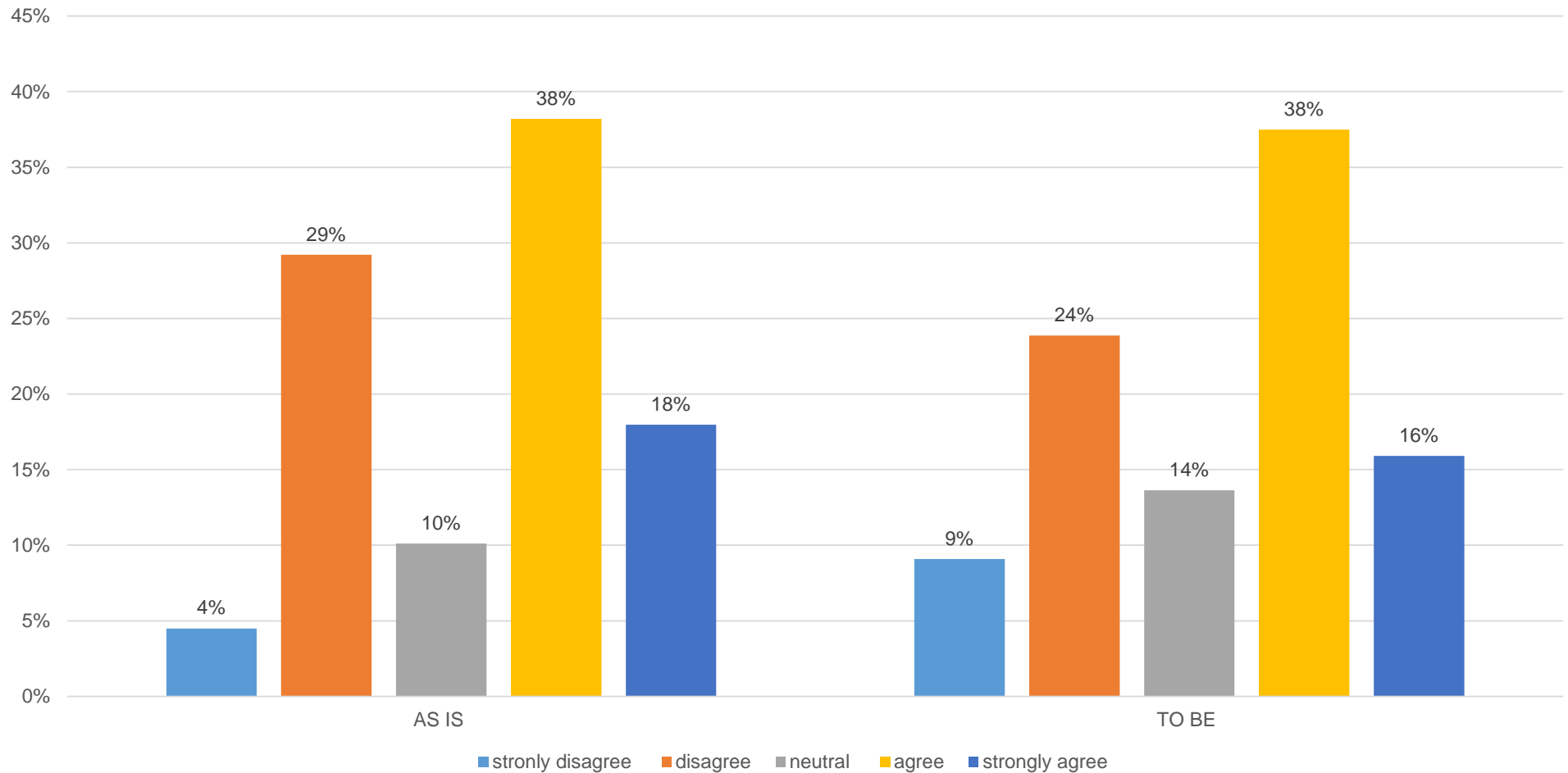
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Role of Credit Management	credit management has an advisory role
	credit management has a decisive role
	credit management has a co-decisive role - 4 eyes principle
	Sales bonuses are influenced by customer payments

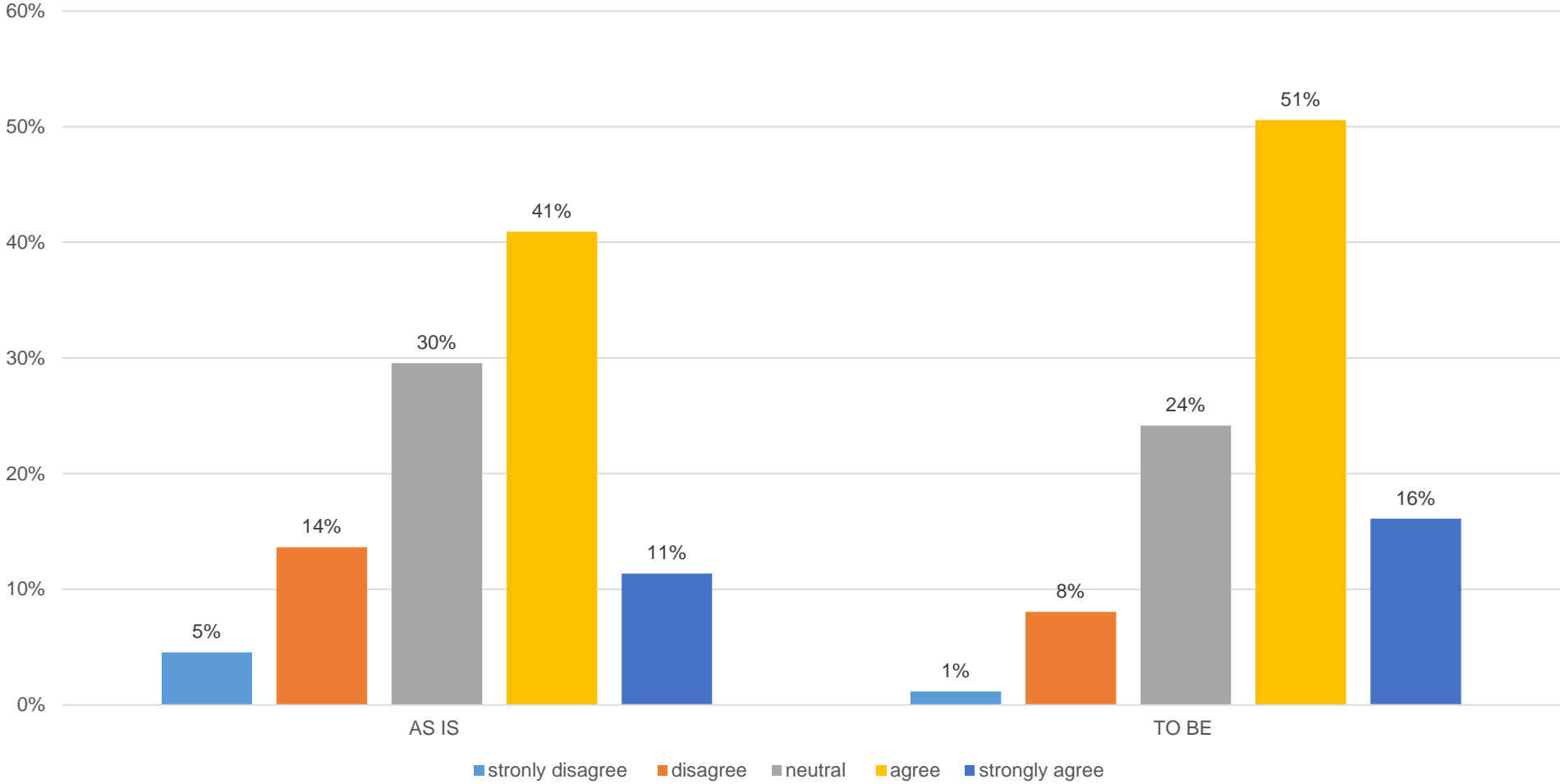
Executive Summary on the role of Credit Management

- ❑ **Credit management has a decisive advisory role in the company, the 4 eye principles is liked**
- ❑ **Sales bonuses are not yet based on customer payments**

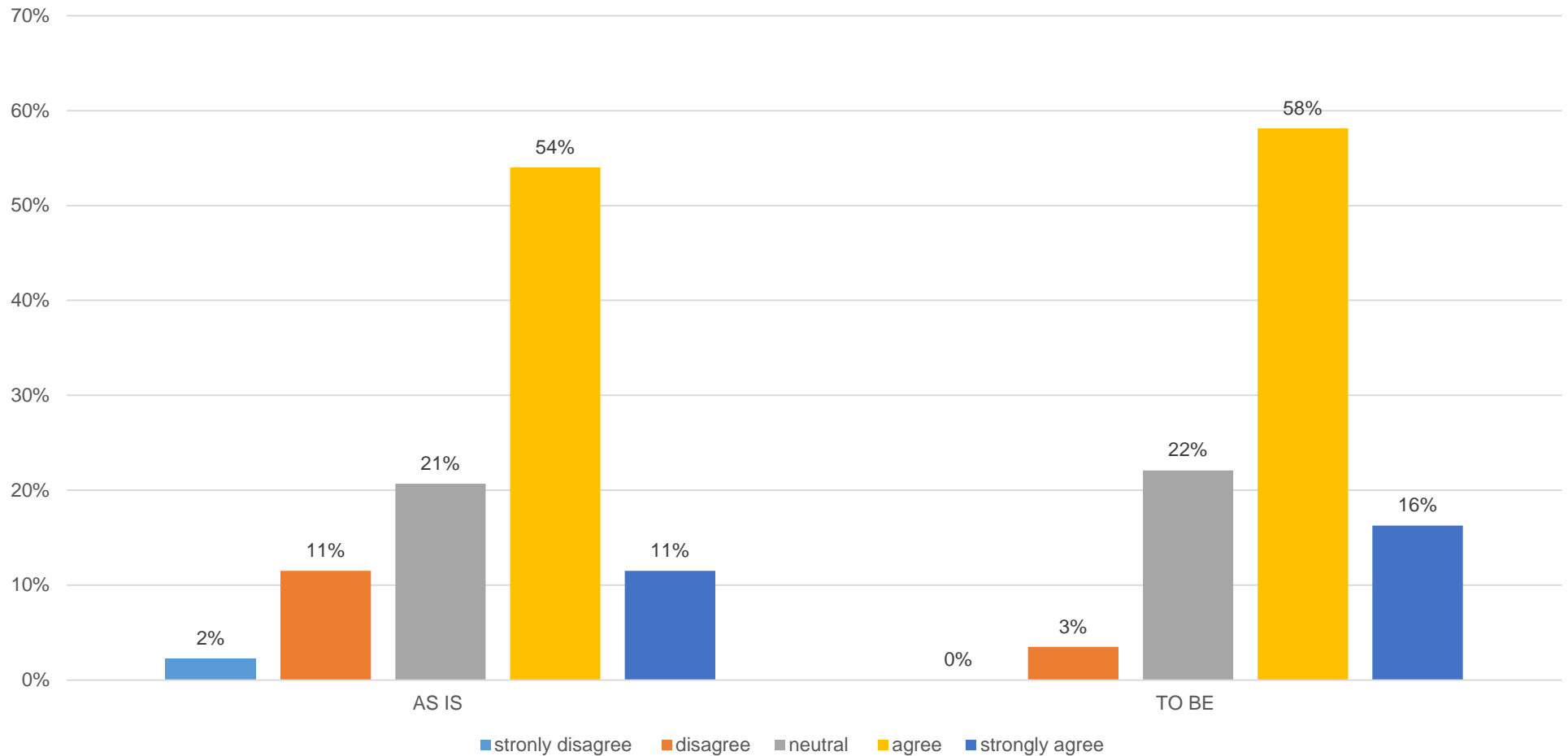
Credit Management Role - credit management has an advisory role



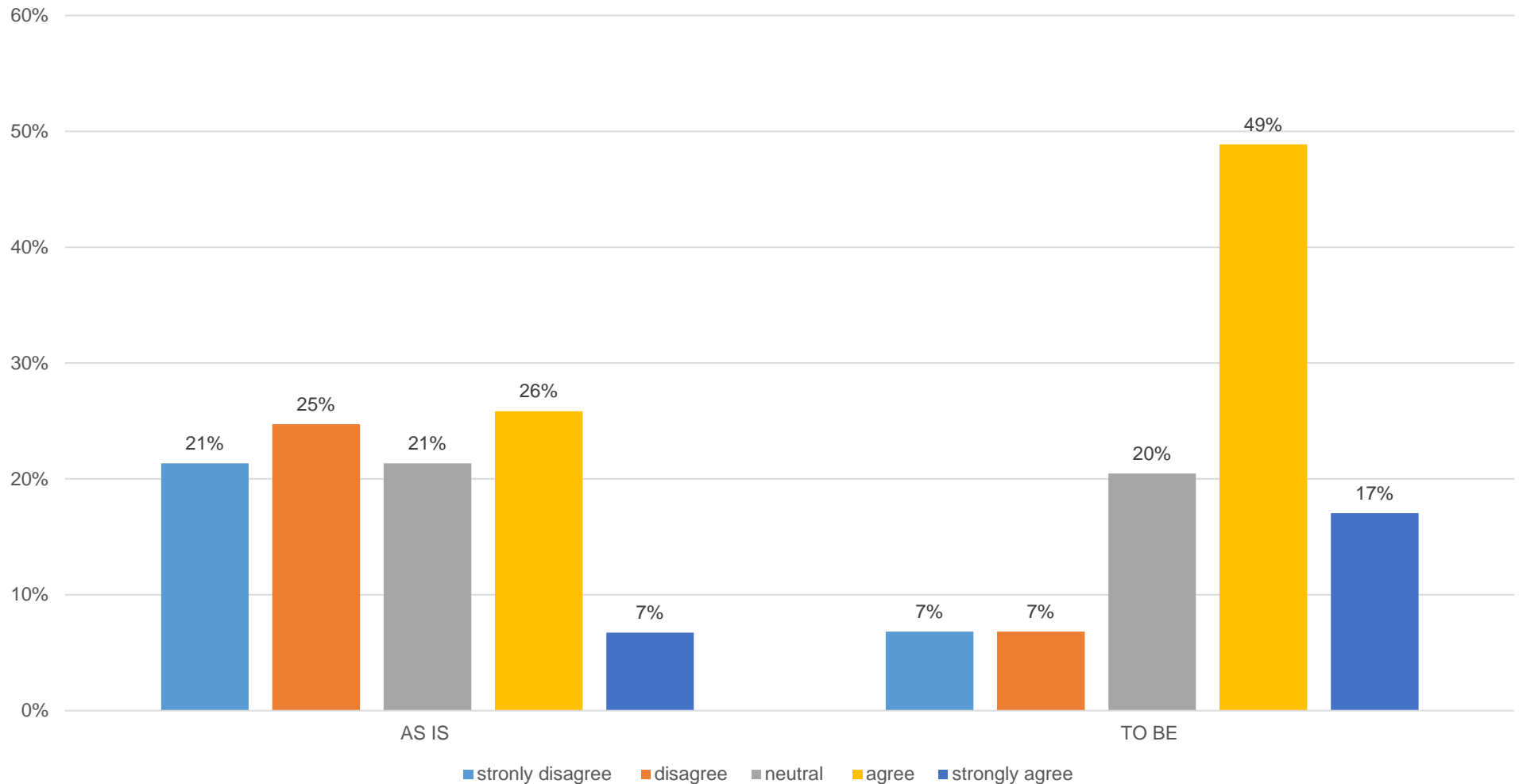
Credit Management Role - credit management has a decisive role



Credit Management Role - credit management has a co-decisive role - 4 eyes principle



Credit Management Role - Sales bonuses are influenced by customer payments



Survey Questions

Topic	Question / Statement
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	Personal contact with new customers to discuss credit limits
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	Dispute management
	Initiate legal procedure
	Credit Management Reporting

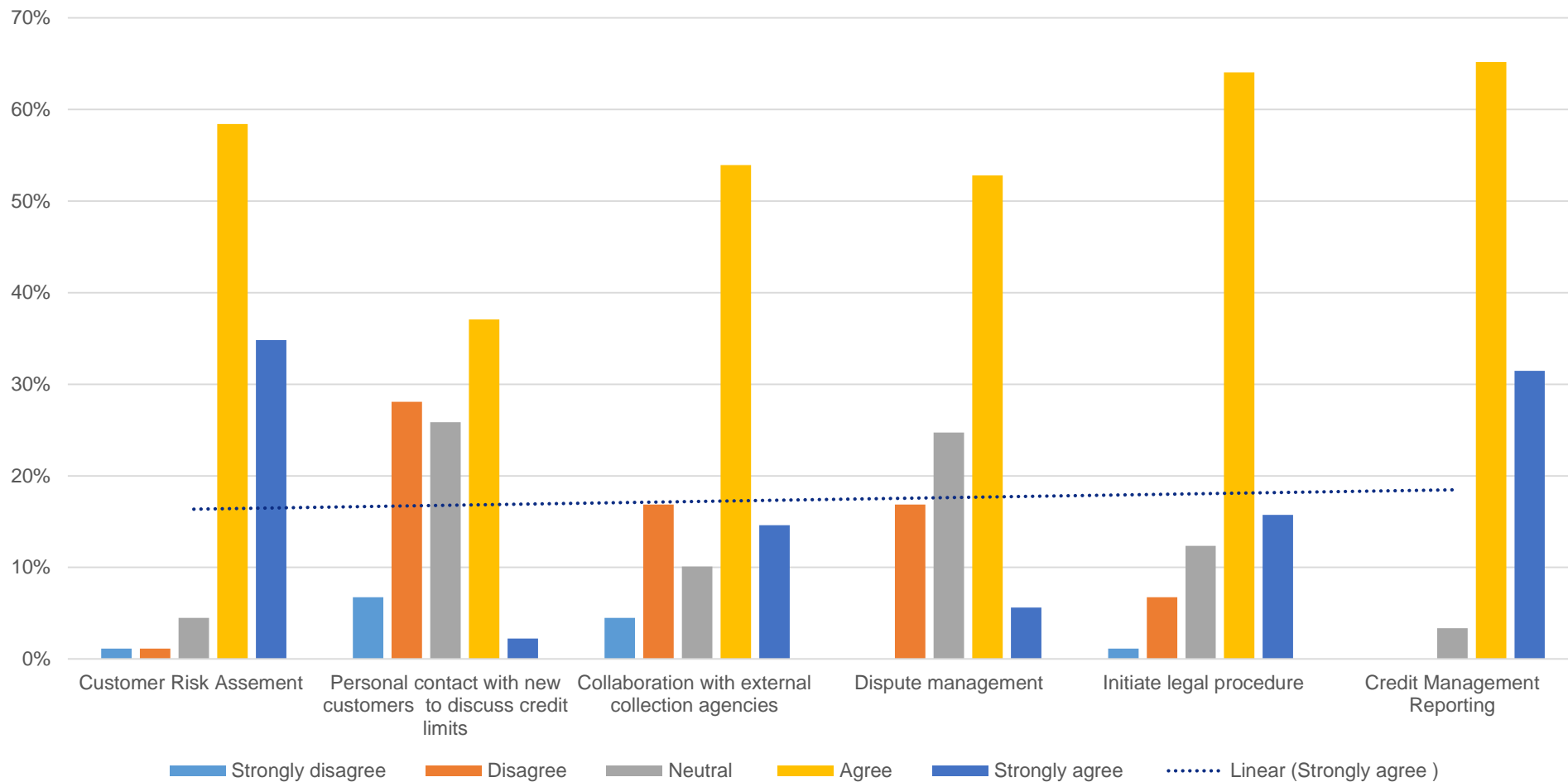
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	Approval of credit notes
	Credit hold – delivery stop
	Credit risk evaluation in proposal process
Credit Management & Organization	The credit management department is organized centrally at HQ.
	The credit management is decentralized per subsidiary or country
	The credit management department has full access to sales visit reports
Reporting Lines	Credit Management direct report
	Credit Management 'dotted line' report

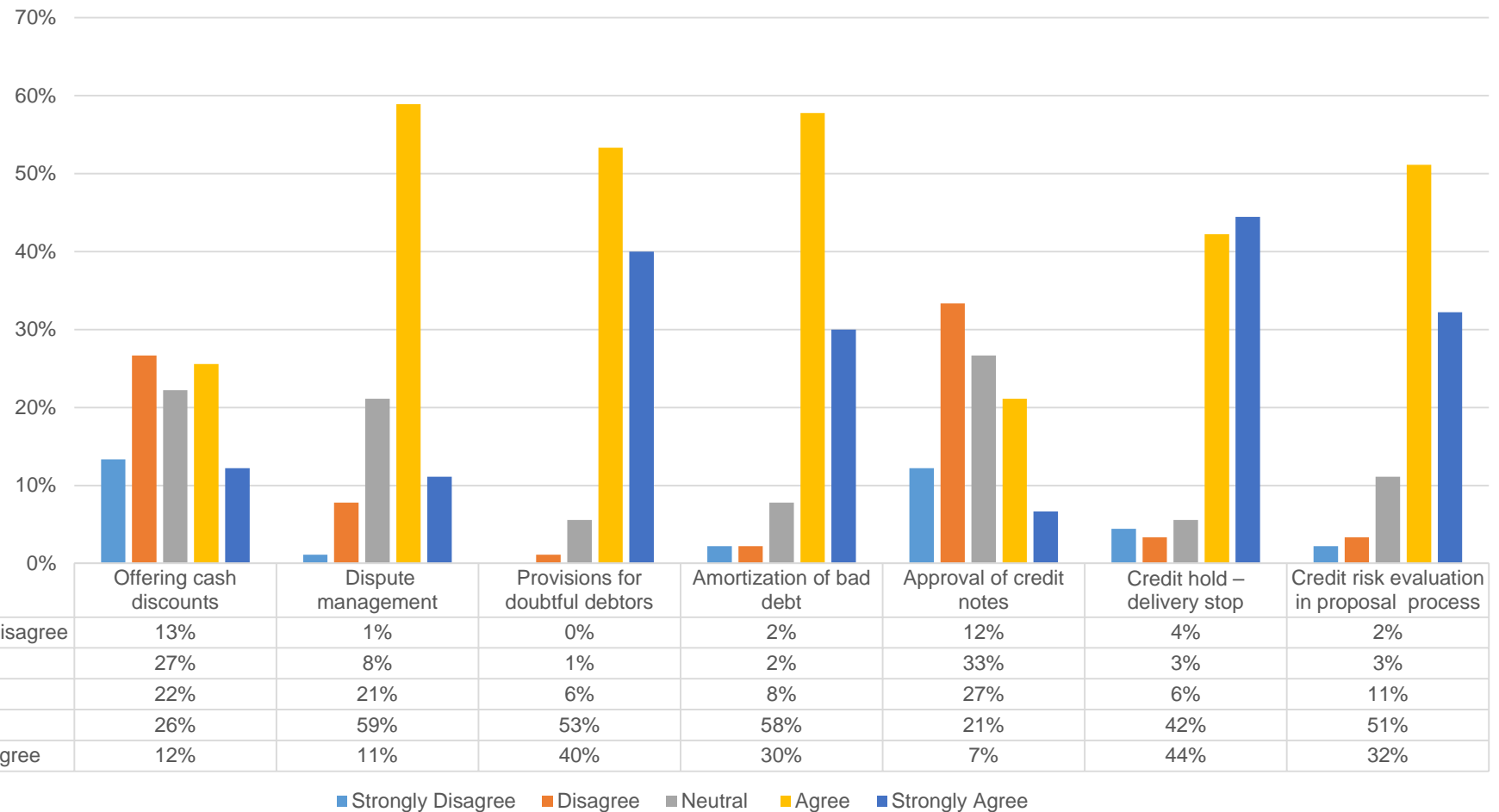
Executive Summary on Credit Management Tasks, involvement and organization

- ❑ **Dispute Management, legal procedure, reporting, risk assessment and collaboration with external agencies are most common tasks. Contact with the customer is perceived as less important**
- ❑ **The credit manager is less involved in issuing credit notes and approval of cash discounts, but he has an important role in the delivery stop, credit risk evaluation in proposal process, amortization of bad debt, provisions for doubtful debtors and dispute management**
- ❑ **Decentralized organization**
- ❑ **Credit Management (CM) in HQ or local has no clear transparency to sales information**
- ❑ **Currently, the CM reports to the CFO, but there is a trend for reporting towards the CEO, at the expense of the CFO**

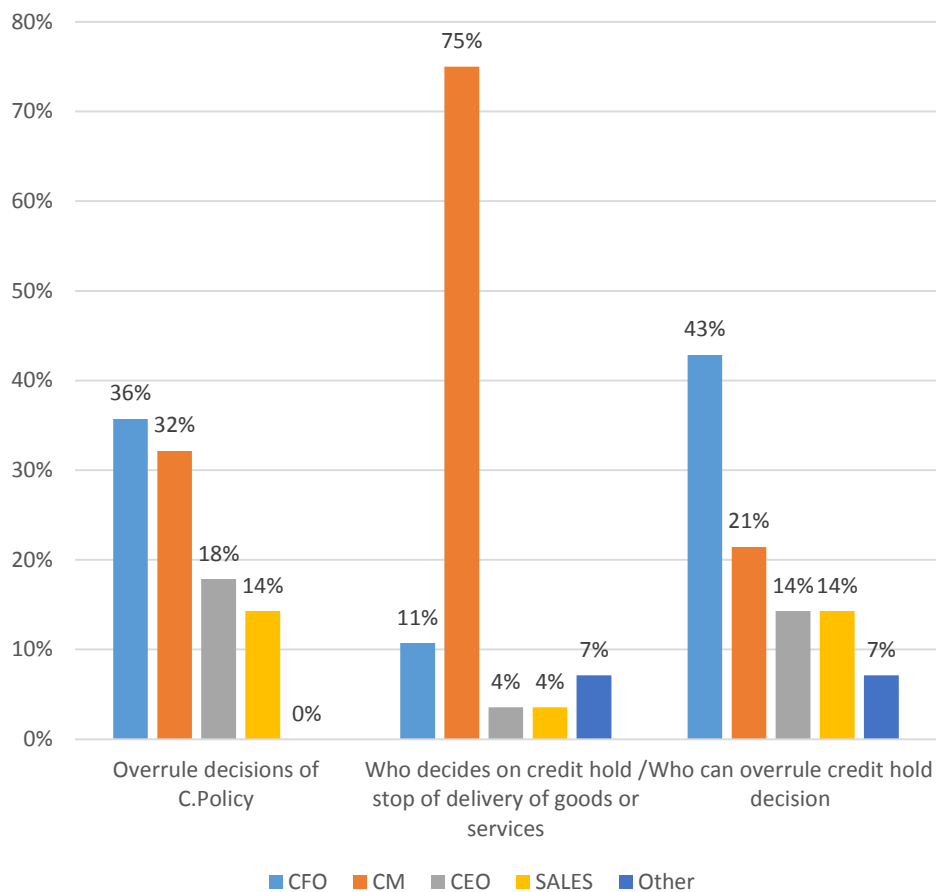
Credit Management Tasks



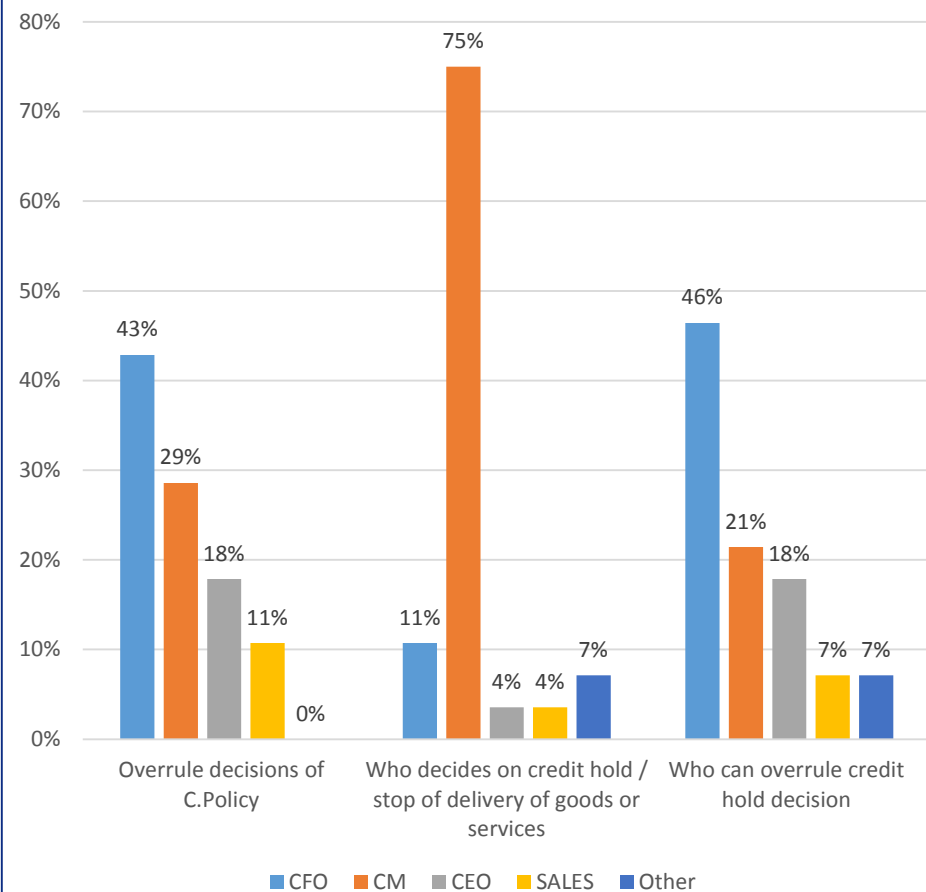
The Credit Manager is involved in :



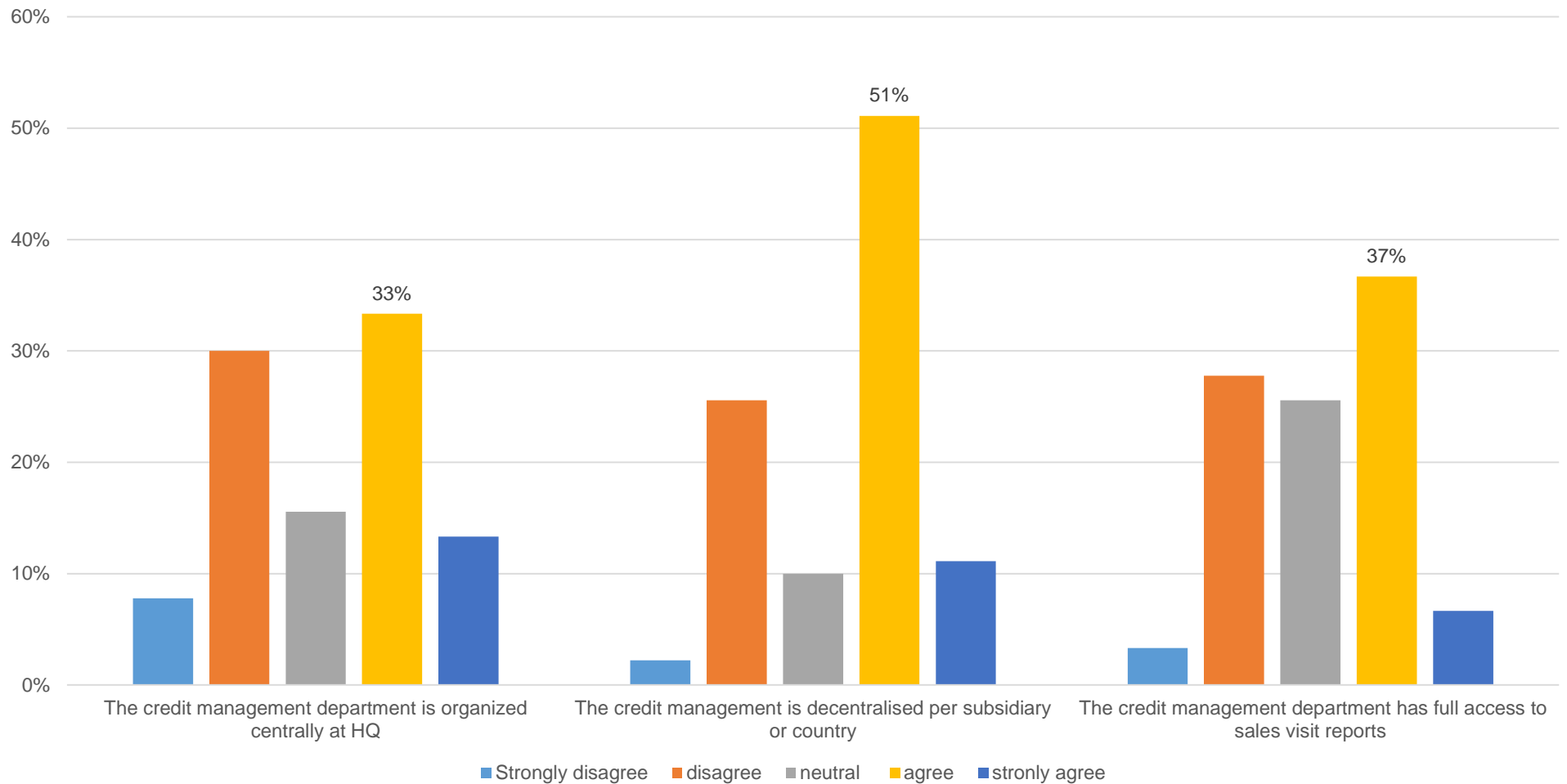
Credit Management Authority AS IS



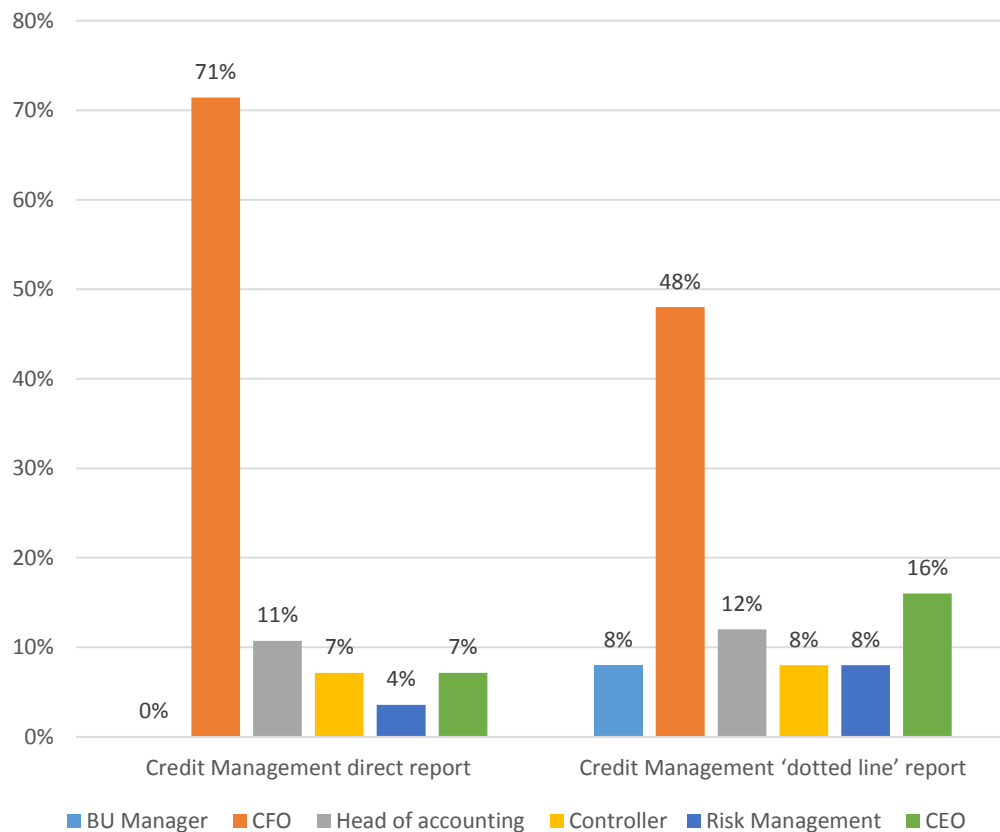
Credit Management Authority TO BE



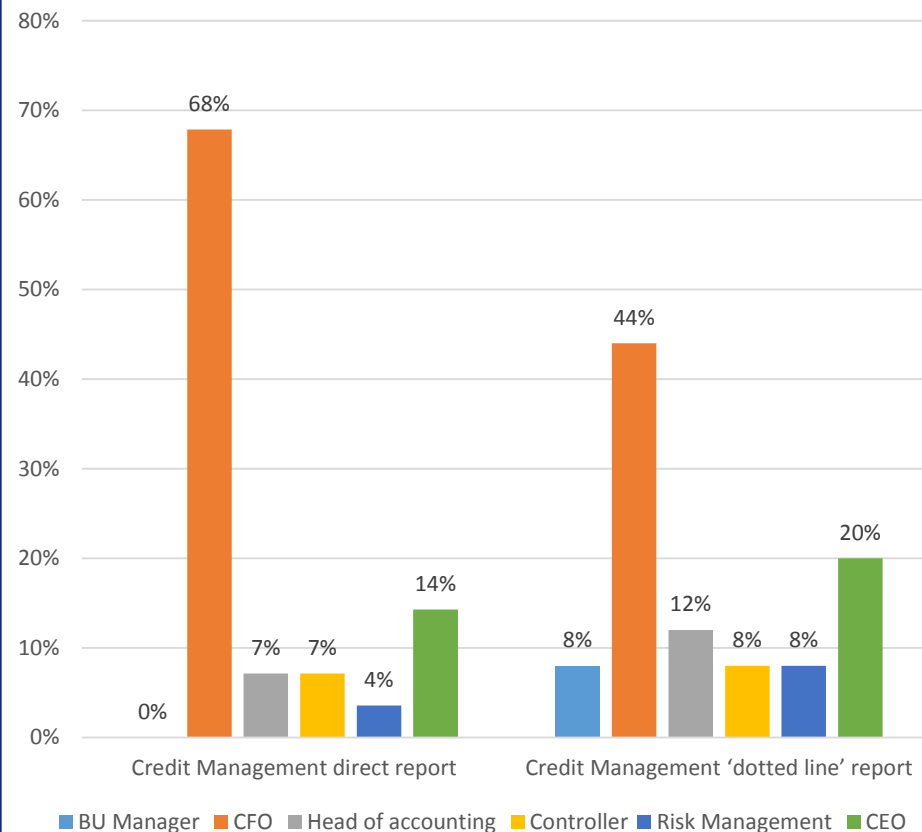
Credit Management Organization



Credit Management Reporting Lines AS IS



Credit Management Reporting Lines TO BE



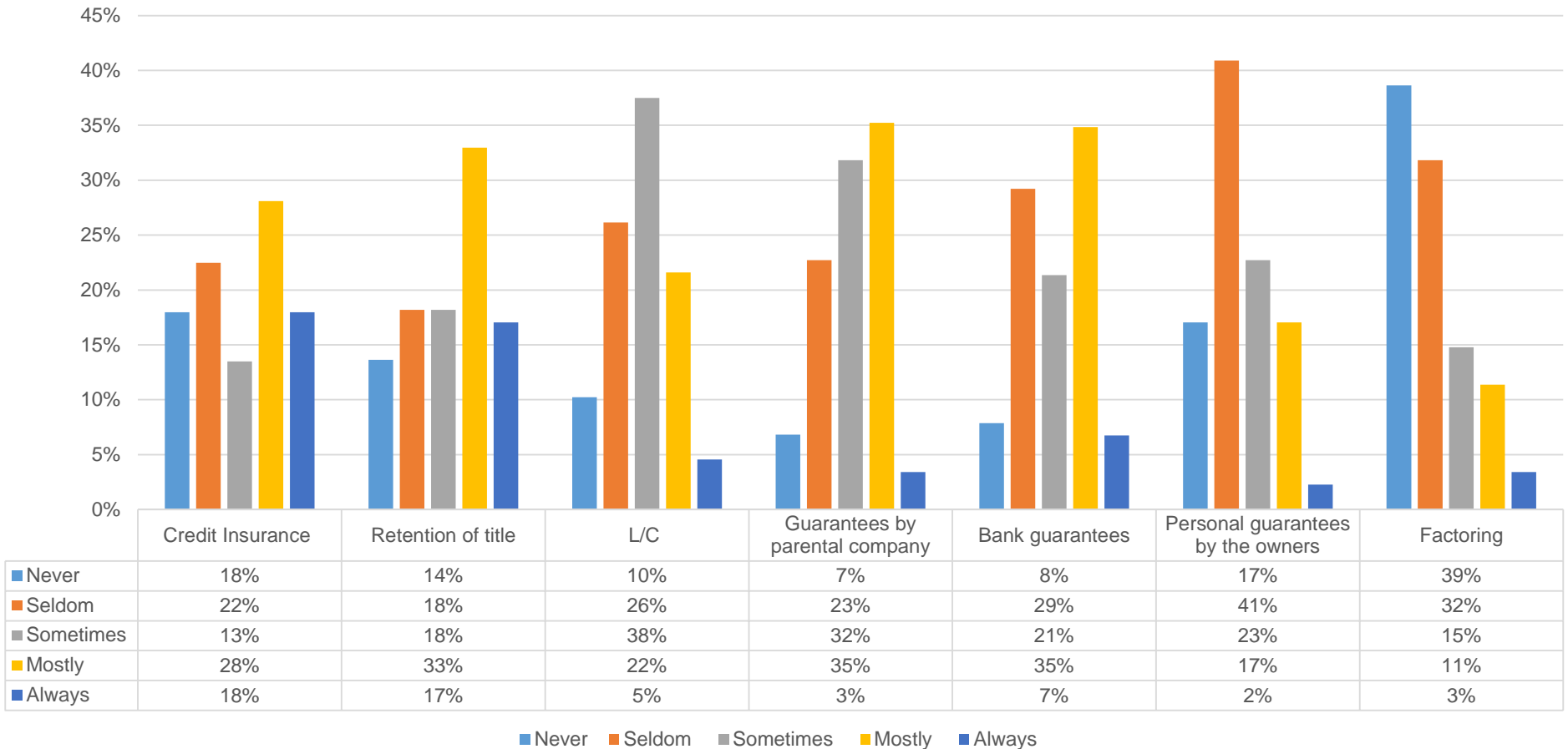
Survey Questions

Topic	Question / Statement
Techniques used by Credit Management :	Credit Insurance , Retention of title , L/C , Guarantees (parent company, bank , personal) , Factoring
Performance Indicators used	DSO , BDSO , CEI , ADL , Aging balance , % bad debt / TO , Frequency of credit limit overruling's

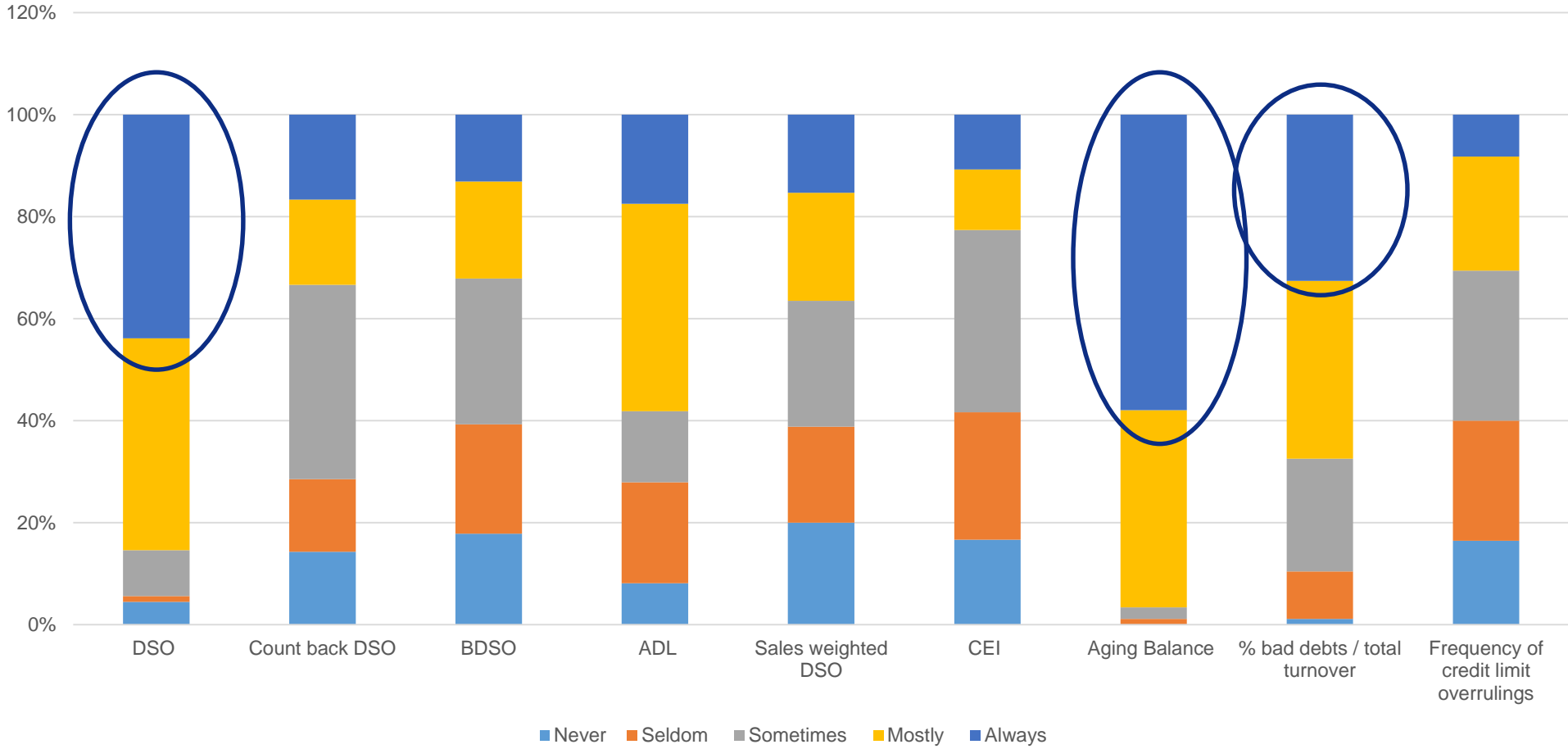
- ❑ **In practice, we observe the CM uses less factoring, bank and personal guarantees to protect the outstanding debts**
- ❑ **L/C, credit insurance , retention of title and parent company guarantees are most used**
- ❑ **For the CM, the DSO, Aging Balance and % of bad debt / TO are the most used performance measurements**
- ❑ **BDSO, frequency of credit limits overruns, CEI are not common yet**

- ❑ Collection Effectiveness Index (CEI):** a measure of the ability of the collections staff to collect funds from customers. The CEI compares the amount that was collected in a given time period to the amount of receivables that were available for collection in that time period.
- ❑ Weighted Days Sales Outstanding (DSO):** measures the average time that receivables are outstanding. It attempts to smooth out the bias of credit sales and terms of sale.
- ❑ Best Possible DSO (BDSO):** utilizes only your current (non delinquent) receivables to calculate the best length of time you can achieve in turning over receivables. The closer your DSO is to your BDSO, the closer your receivables are to your optimal level.

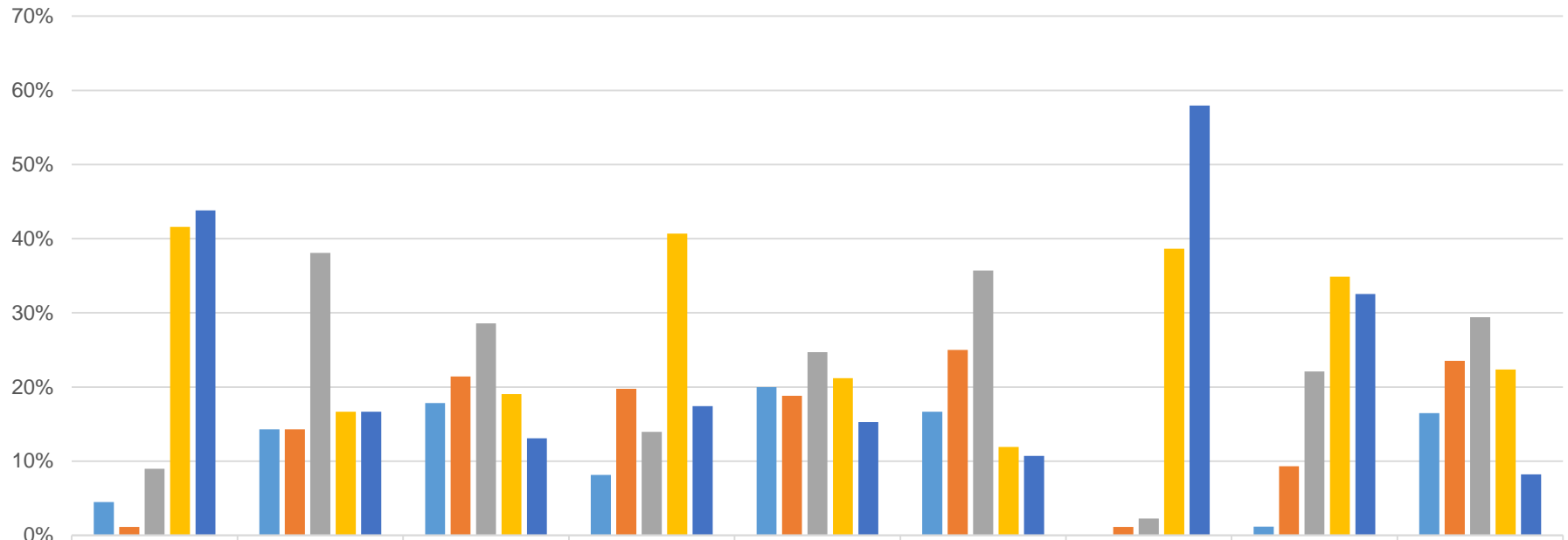
Credi Management Techniques Used



Credit Management Performance Measurement



Credit Management Performance Measurement



	DSO	Count back DSO	BDSO	ADL	Sales weighted DSO	CEI	Aging Balance	% bad debts / total turnover	Frequency of credit limit overrulings
■ Never	4%	14%	18%	8%	20%	17%	0%	1%	16%
■ Seldom	1%	14%	21%	20%	19%	25%	1%	9%	24%
■ Sometimes	9%	38%	29%	14%	25%	36%	2%	22%	29%
■ Mostly	42%	17%	19%	41%	21%	12%	39%	35%	22%
■ Always	44%	17%	13%	17%	15%	11%	58%	33%	8%

■ Never ■ Seldom ■ Sometimes ■ Mostly ■ Always

Survey Questions

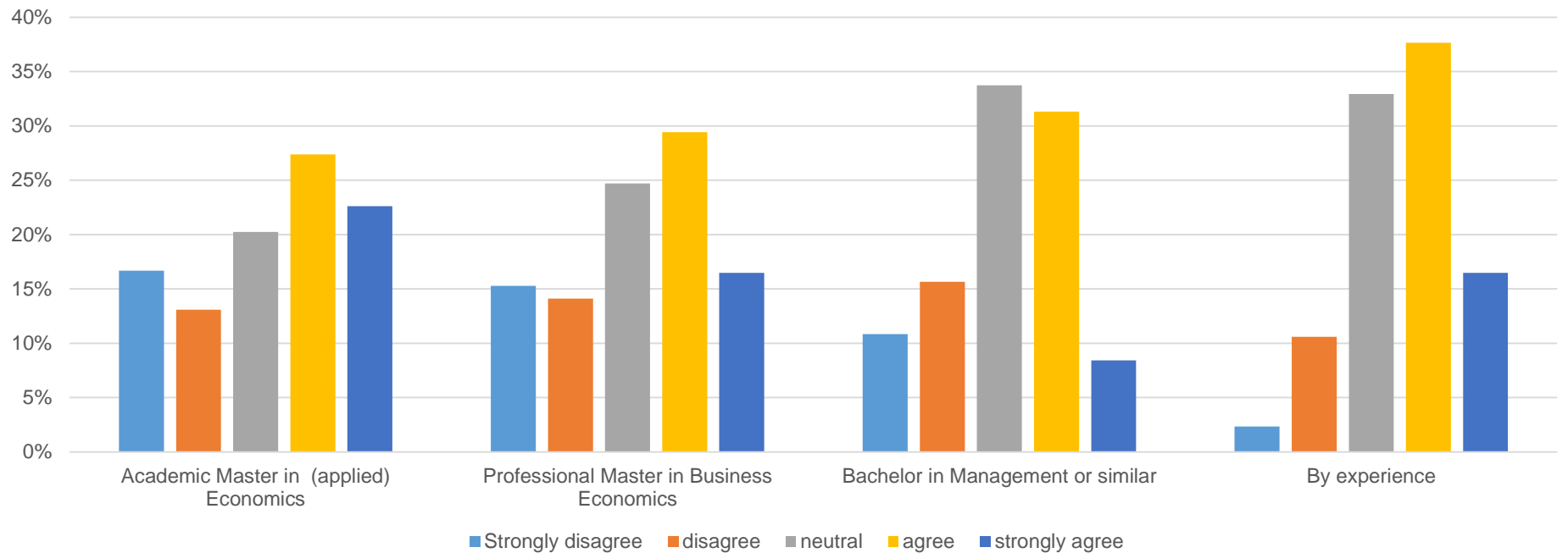
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Survey Questions

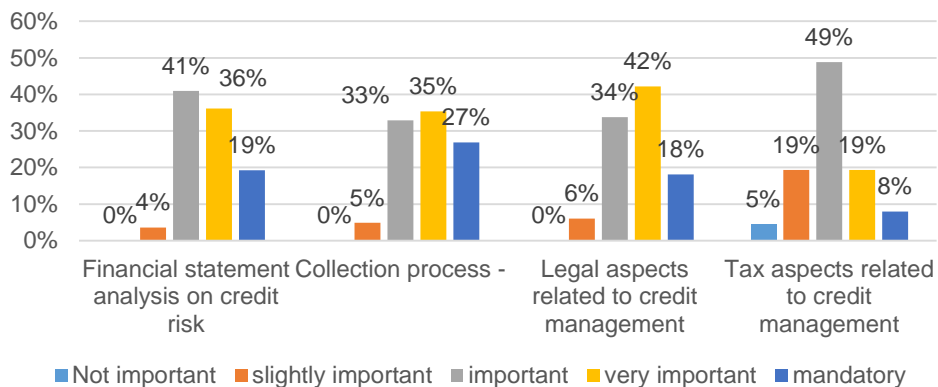
Topic	Question / Statement
Competences	Languages
	Bank instruments to limit credit risk
	Knowledge of customer industry
	Payment techniques
	Credit Insurance , VAT , Technical skills
	Soft Skills :communication , presentation , ...
Credit Management Practices	Cash discount , interest charged , collection cost charged
Career Path & Sourcing	

- ❑ **By preference the CM has a university degree, but experience is more important**
- ❑ **According to the importance of experience, payment techniques and knowledge of the customer industry are recognized as high-valued competences in order to understand the Order to Cash process**
- ❑ **IFRS, VAT and credit insurance are less important!**
- ❑ **Soft skills are very important**
- ❑ **The CM is not an interim manager but externally hired and on payroll**
- ❑ **No clear career path is observed**

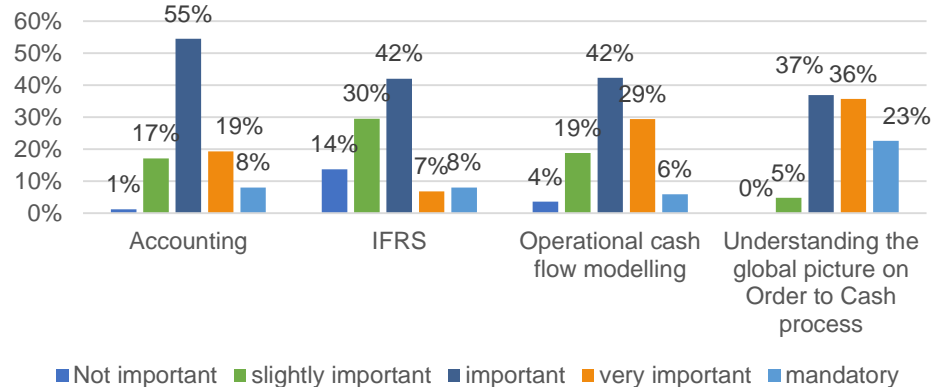
Credit Management Education



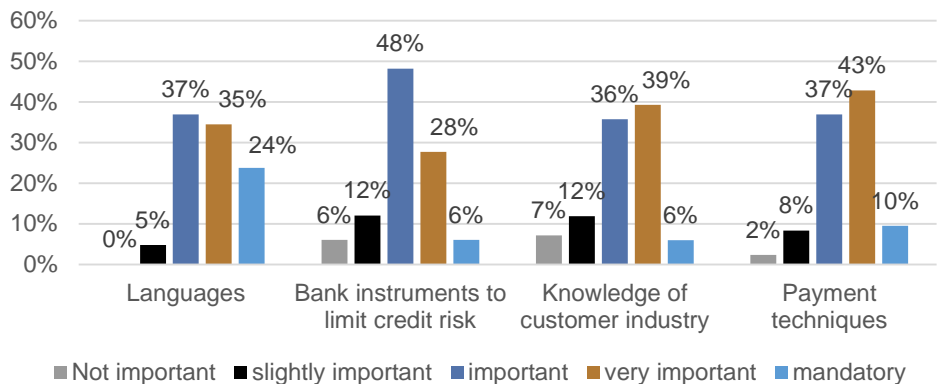
Credit Management Competences



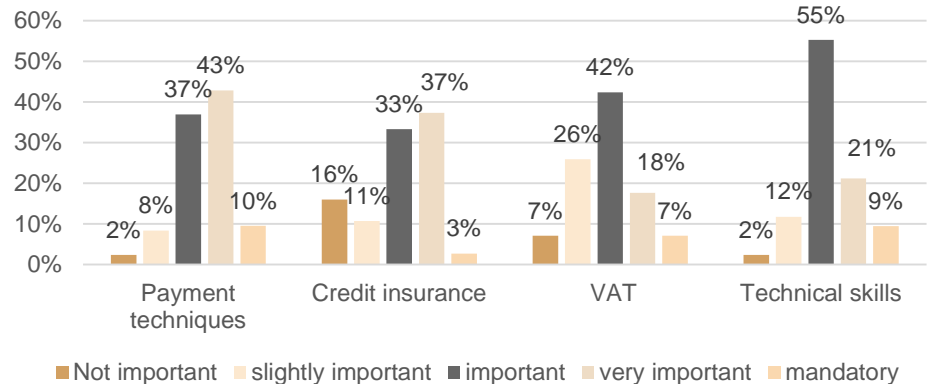
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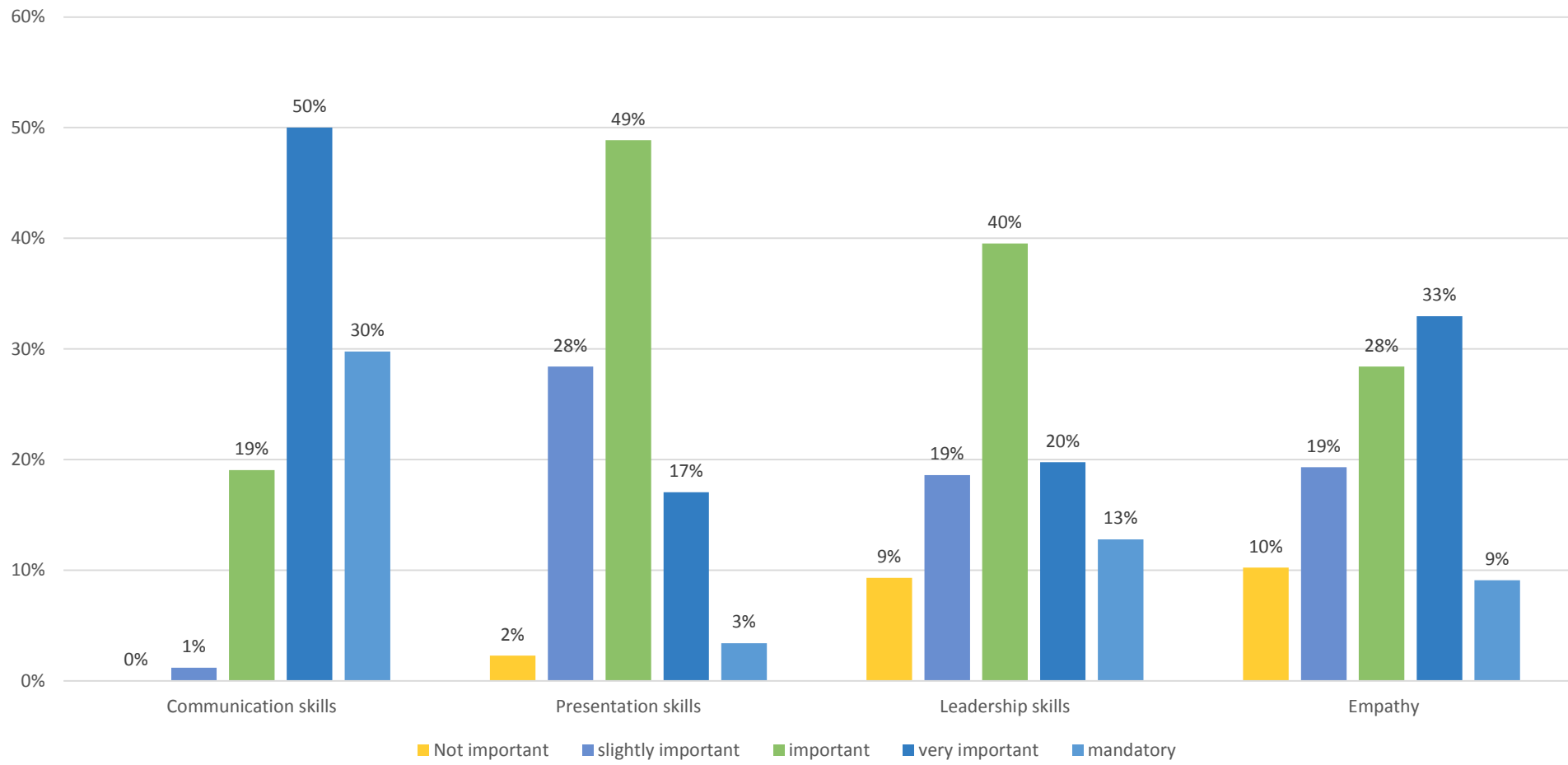
Credit Management Competences



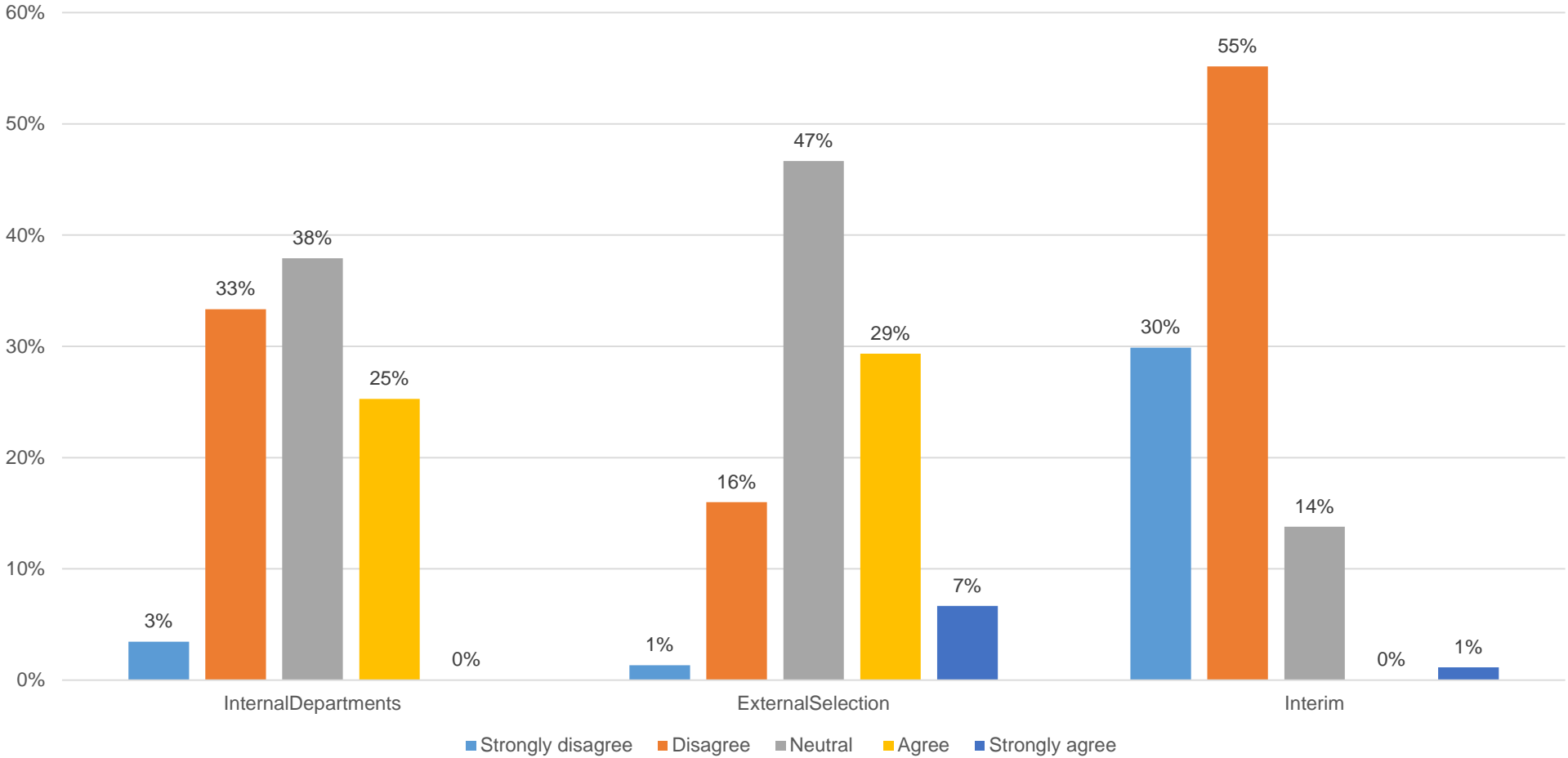
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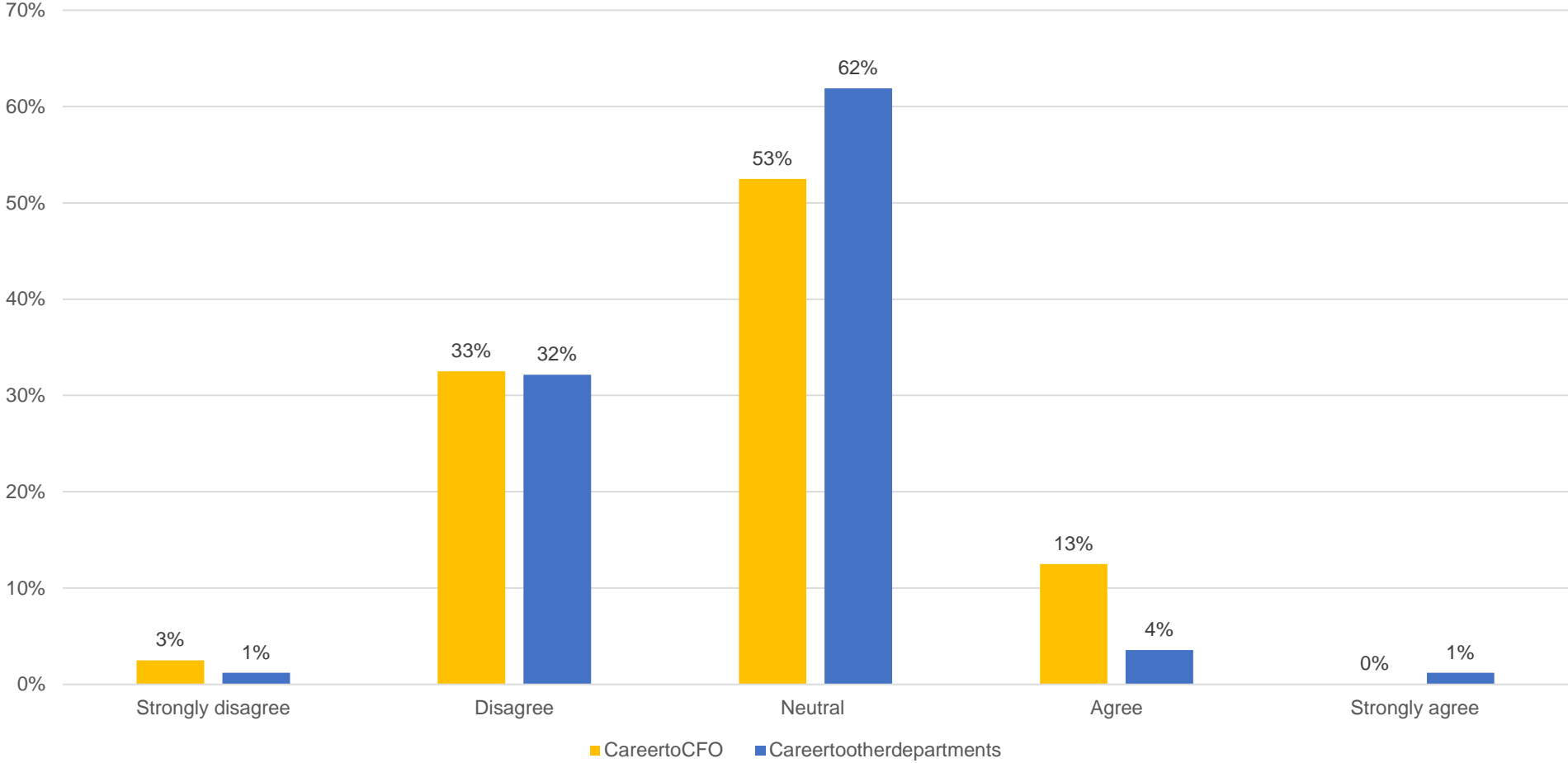
Credit Management Soft skills



Credit Managers Sourcing



Credit Management Career Development



Conclusion

- The Credit Management policy need to be available for a all stakeholders and updated on a regular basis .**
- The policy should be embedded in a system.**
- Customer payment analysis should be done on regular basis to update sales conditions and credit limits and not ad – hoc .**
- The tasks of the credit manager are known and can be maintained.**
- The credit manager need to have a full recognition as advisor in acceptance of new clients and related credit limits and payment conditions**
- Performance should be measured by other KPI's then DSO as CEI , ADL , BDSO**
- Communication skills are important**
- Career path development need to be taken into consideration**

Thank you

Presentation by Christian Pauwels



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