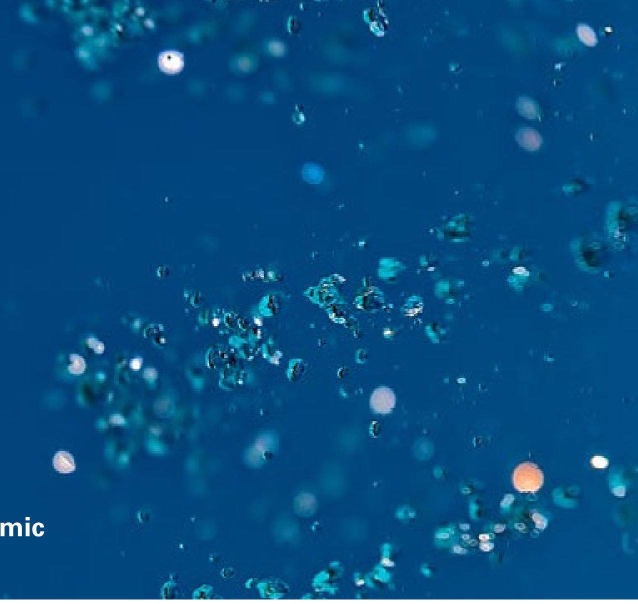


Stringent cash management

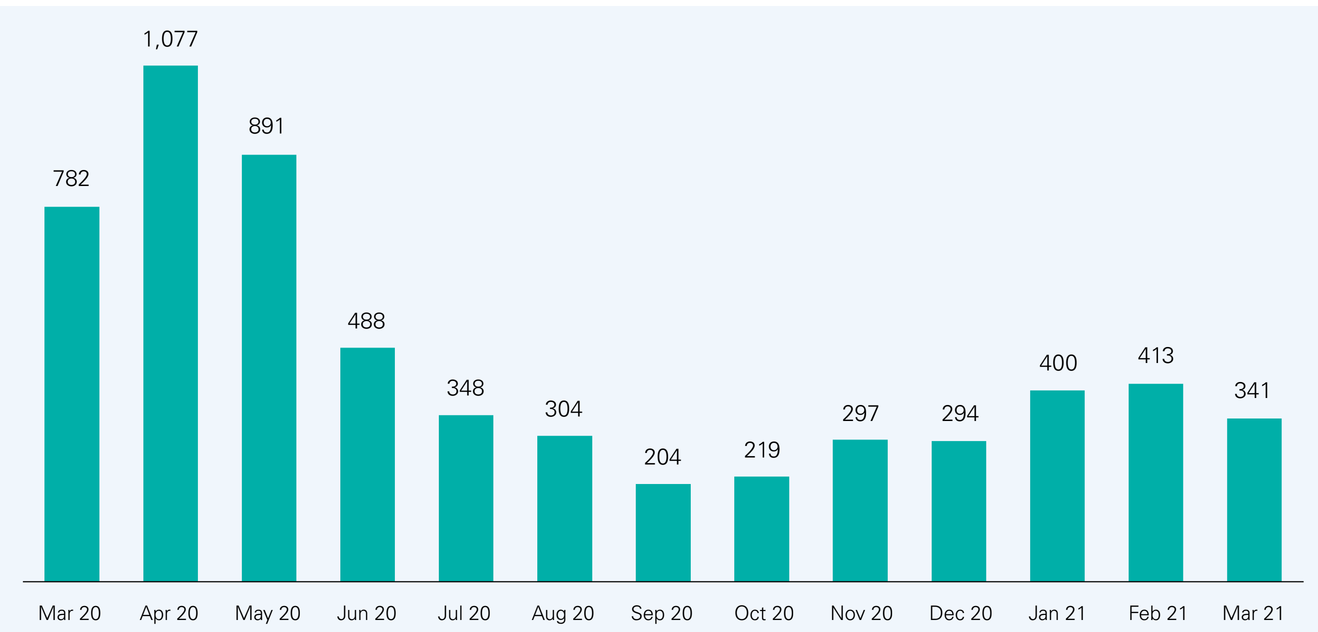
A key prerequisite in the aftermath of the COVID-19 pandemic

As the global COVID-19 pandemic hopefully will soon come to an end, it becomes apparent that businesses in several industries have been severely impacted by government directed lock-downs, supply chain disruptions and changing consumer behaviour (e.g. acceleration of e-commerce, changing travel habits, remote working, etc.). The critical question remains how companies can best navigate out of the current crisis and seize the opportunities to build business resilience. In this regard, the current crisis revealed the importance of cash excellence, although many struggling organizations found some temporary relief through extensive governmental support, lax lending requirements and a low interest rates environment.

Governmental support is only a temporary solution

During the first wave of the COVID-19 pandemic in 2020, many companies refinanced their current loans and borrowed additional capital in the form of COVID-19 bridging loans. Our analysis of 134 listed Swiss companies shows that small cap companies (< CHF1bn market capitalization) raised larger amounts of debt to offset the loss of cash flow, while large cap companies (> CHF 1bn market capitalization) companies tended to strengthen their equity capital base. Notably there were 6.4% fewer insolvencies in Switzerland in 2020 compared to 2019, which was directly connected to the financial support provided by the Swiss government. The record amount of CHF 2.5bn in hardship funds and more than one million employees on short-time work compensation granted by the Swiss state at the peak compound the underlying issues of overleveraged and unfit companies.[1]

Number of Swiss employees on short-time work (in 1,000)



[1] State Secretariat for Economic Affairs, SECO (2021)

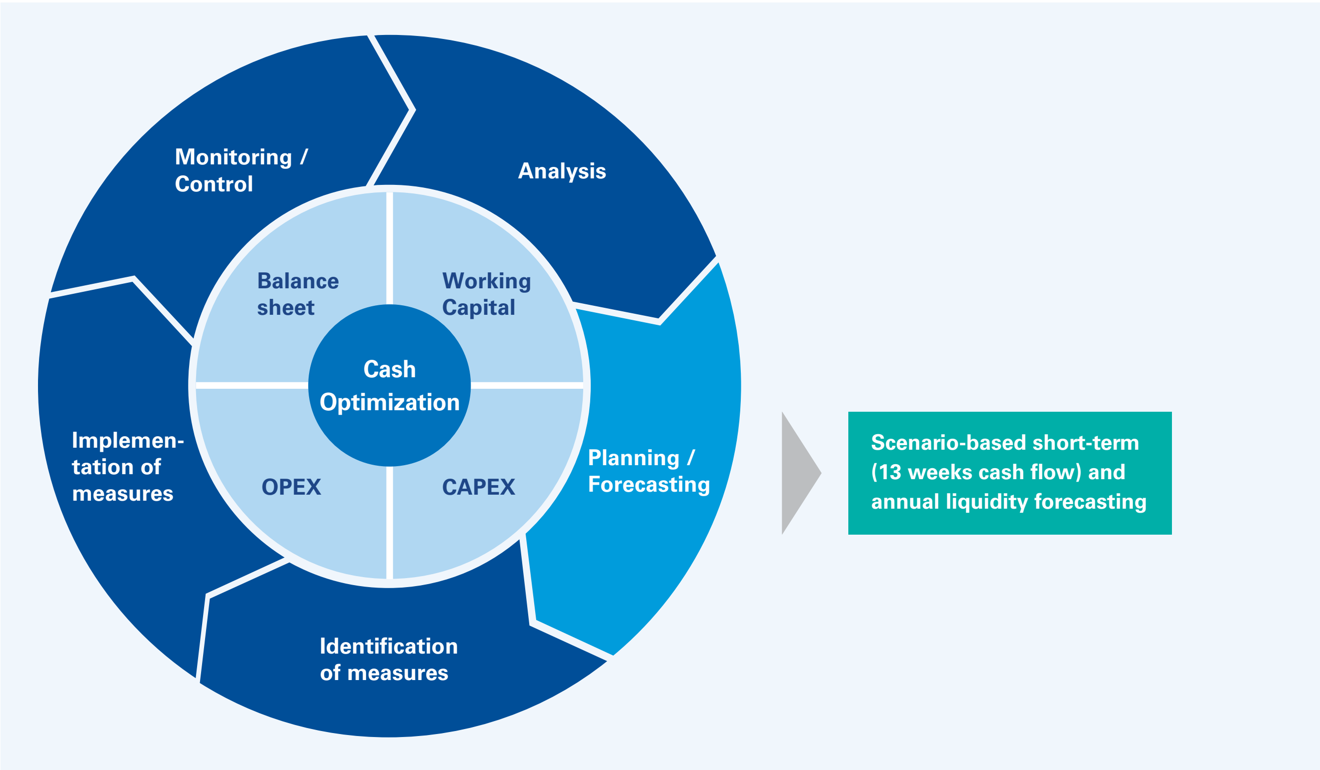
In addition, the hardship aid will not be treated as debt when applying the over-indebtedness threshold (Article 725 (2) CO) until 31 March 2022[2]. This unhealthy situation of delayed structural market adjustments might ultimately magnify business risks in the near term. The Swiss Economic Institute (KOF) highlights the combination of potential negative effects related to the pandemic and generally increased economic risks[3]. As governmental support will progressively be phased out, companies will have to ensure the transition to a post-pandemic world independently. However, our experience shows that many companies lack appropriate forecasting as well as cash management tools and processes, which are crucial in the upcoming recovery period.

Cash excellence culture is key

In the aftermath of the pandemic, companies are well advised continue to plan in multiple scenarios addressing potential risks, reassessing their business plans and monitoring short-term liquidity and funding requirements. Also, worst-case scenarios should be considered in business planning and short-term liquidity forecasting. This allows management to prepare and adequately respond to adverse situations. To optimize cash generation, the following four levers should be considered:

1. Working capital
2. Capital expenditures (CAPEX)
3. Operational expenditures (OPEX)
4. Balance sheet (Financing)

Cash excellence framework



Working Capital

Effective working capital management was particularly challenging during the pandemic as customers and suppliers faced unprecedented disruptions, highlighting the importance of rigorous process management through the entire cash-conversion cycle. Balancing inventory levels depends on a wider set of variables as new sourcing strategies, overall market shifts, changing consumer trends and supply chain frictions increase the uncertainties. In this regard, improvements in the planning process can be best achieved through visibility in the supply chain, where real-time data can be synchronized consistently from the point of order to the point of sale. Credit risk related to outstanding receivables should be closely tracked and monitored to avoid potential defaults that would negatively impact the liquidity position. In addition, management could attempt to negotiate a stretching of payment terms for outstanding invoices to manage short-term liquidity and to reduce an immediate cash outflow.

Capital expenditures

Investments of Swiss companies have been low since 2018.[4] Many businesses that abruptly reduced capital expenditures incurred significant sunk costs and impairment

[2] Art. 3 Covid-19-SBüV; Art. 24 Covid-19-SBüG & Art. 21 Covid-19-Härtefallv.
[3] Swiss Economic Institute, KOF (2021)
[4] Swiss Economic Institute, KOF (2021)

losses on cancelled projects. A strict and selective process for capital allocation should be emphasized going forward.

Operational expenditures

The cost structure of many businesses has experienced several shifts in response to the pandemic. Expenses related to travel, event or marketing and representation were significantly reduced and might not reach pre-crisis levels in the near future. A granular, bottom-up budgeting process helps companies challenge unnecessary spending and gain transparency of the key business drivers.

Balance sheet (Financing)

During the pandemic, several companies were forced to renegotiate loan terms (e.g. due to covenant breaches) and refinance maturing debt to bridge liquidity needs. Additionally, capital injections and debt subordinations were required to recapitalize the balance sheet and address the risk of over-indebtedness. The need for additional financing is expected to continue to be strong as government support will end at some point.

Key messages

Successful businesses are characterized by having adequate tools and processes in place to mitigate economic shocks. They distinguish themselves by efficient liquidity forecasting processes and robust business planning, which are highly relevant during and after a global pandemic. A scenario-based approach helps to proactively determine the liquidity need also in the worst case in order to achieve business resilience, allowing timely responses and the leverage of the cash optimization levers.

Contacts

KPMG AG
Badenerstrasse 172
PO Box
CH-8004 Zurich

kpmg.ch/restructuring

Peter Dauwalder
Partner
Head of Restructuring

+41 58 249 41 80
pdauwalder@kpmg.com