KPMG

Working capital trends in the Dutch market

Strategies to unlock cash and stay competitive

KPMG Annual Working Capital Study

September 2024

Foreword

While 2024 is showing signs of a slow recovery, economic instability created over the last couple of years persists, with issues such as the rising cost of capital, conflicts in Ukraine and the Middle East, and ongoing global supply chain disruptions impacting global trading. The global and Dutch mergers and acquisitions (M&A) markets have been impacted by the same conditions, with decreased deal volumes due to high interest rates. In the last year, the majority of Private Equity (PE) assets sold were the best-performing ones in the portfolios of private equity firms. The economic situation has led companies and private equity firms to look further into improving cash culture and optimising working capital as a key value lever.

Working capital optimisation can help to protect your business and gain competitive advantage

Optimising inventory, receivables, and payables can provide many benefits, such as greater liquidity, extra funding for strategic growth, funding for M&A, faster paydown of net debt, and funding to execute performance enhancement programmes. Now more than ever, businesses are starting to think strategically about how to manage their working capital more effectively to improve cash and mitigate risk.

Assessing working capital performance

In this working capital study, we have:

- Analysed over 1,200 businesses in the Netherlands;
- Gained insights from our working capital and business sector experts, as well as turnaround and transformation specialists;
- Summarised key considerations for CFOs and executives looking to optimise working capital.

Evgenia Bodaar-Molotova
Lead author

Highlights from the study

Cash conversion cycle (CCC) days for Dutch companies decreased by 8 days from a median of 53 days in 2018 to 45 days in 2022. This effect was driven largely by an increased focus on payment management during the Covid-19 pandemic. Over the last four years global supply shortages determined companies' cash cycles, with many companies experiencing falling revenues due to insufficient inventory, while others ended up with high levels of slow-moving stock when post-pandemic demand declined, while the knock-on effect of high interest rates meant that consumers now have less disposable income.

CCC days of Dutch companies increased by 19 days from 2022 to 2023, with inventory on the rise while payment terms reverted to pre-pandemic levels.

At a sector level, TMT, automobile, healthcare and materials witnessed a worsening CCC trend while real estate, consumer & retail, industrials and energy showed improvement in CCC.

The **TMT** sector faced significant working capital challenges, attributed to a combination of post-pandemic demand fluctuations and disruptions in the global supply chain.

In the **automobile** sector, demand slowdown, particularly in the EV segment, and the need for timely payments to suppliers to secure sufficient stock posed obstacles in working capital management.

Supply chain obstacles, strategic preferences leading to increased medicine stocks, and equipment shortages resulted in a deterioration of the CCC through higher inventory levels in the **healthcare** sector.

Conversely, the **consumer and retail** sector demonstrated improvements in CCC, although inventory levels remained a persistent concern amidst the return to pre-pandemic demand levels and heightened global supply chain challenges.

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Executive summary

Economic outlook

The Dutch economy is gradually recovering in 2024 after a slowdown in 2023, supported by an increase in wages and consumer spending and an expansion in public investments related to the green transition and defence.

Business investment is expected to remain relatively weak due to persisting labour shortages and challenging financial conditions. Inflation has started to fall compared to the high levels experienced in 2023 and is projected to continue to decrease over the remainder of the year[(2)].

Although the labour market remains tight, there are signs of this easing. While the number of outstanding vacancies is falling, it continues to exceed the number of unemployed[(2)].

GDP is expected to grow by 0.8% this year, with stronger growth of 1.5% expected in 2025 on the back of solid private consumption growth and an improved outlook for business investment and trade[(2)].

Labour market remains tight

The Dutch labour market continues to be tight, with low unemployment and several sectors experiencing labour shortages. On the back of a slowing economy, the unemployment rate is forecast to increase to 3.9% in 2024 and 4.0% in 2025[(2)], albeit remaining below the unemployment rates prior to the pandemic. Fuelled by a tight labour market and surging inflation, nominal wage growth increased considerably last year and is expected to reach 5.9% in 2024 before easing to 3.8% in 2025[(2)].

Interest rates still high but easing in 2024

Central banks worldwide have tightened their monetary policy considerably since 2022, with the ECB raising its rate to 4% in 10 steps between July 2022 and October 2023[(4)]. This tightening contributed to the fall in inflation towards the ECB's target, partly by making it less attractive for households, firms and governments to borrow money as interest rates kept growing over the course of 2023. As inflation has started to decelerate, the ECB lowered its interest rate by 0.25% in June 2024[(4)] to help boost economic growth. Rates remained unchanged in July 2024, with the next decision on monetary policy expected in September 2024[(5)]. Interest rates in the euro area are expected to gradually decrease to 3% by the end of 2025[(3)] and to 2% in the longer term[(5)].

Inflation continues to decelerate

Inflation (HICP) fell significantly during 2023, from 7.2% in the first quarter to 2.7% in May 2024[(1)], mainly attributed to a strong decrease in energy prices. HICP inflation is set to decelerate to 2.5% in 2024 and 2.0% in 2025[(2)]. Core inflation, which excludes energy and food, has also declined, although more gradually, to 2.5%[(2)]. A similar decrease is seen in the euro area, with inflation and core inflation standing at 2.6% and 2.9% respectively in May 2024[(1)].

Source: (1) DNB – Financial stability report – Spring 2024. (2) EC – Economic forecast for Netherlands – May 2024. (3) EC – Economic forecast – Autumn 2023. (4) DNB – Current economic issues – interest rates. (5) EC – Monetary policy decisions press release – July 2024.

Summary of findings

€72.5bn

Estimated working capital that can be released across the 1,200+ Dutch companies included in this study

65 days

difference between CCC of leaders and laggards

8 days overall improvement[a] in CCC, but

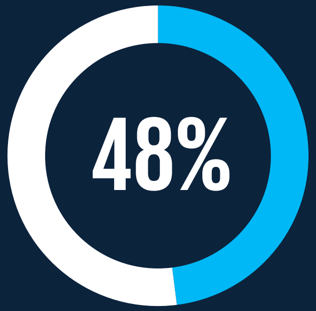
6 days deterioration[a] of DIO

Top sectors showing improvement[a] in CCC

- Real estate
- Consumer & Retail
- Industrials

Top sectors showing deterioration[a] in CCC

- TMT
- Automobile
- Healthcare



of companies in the study saw a deterioration[a] in CCC of which:

- 34% showed increase in DIO
- 33% showed decrease in DPO
- 21% showed increase in DSO

Note(s): (a) in 2022, with respect to 2018

02

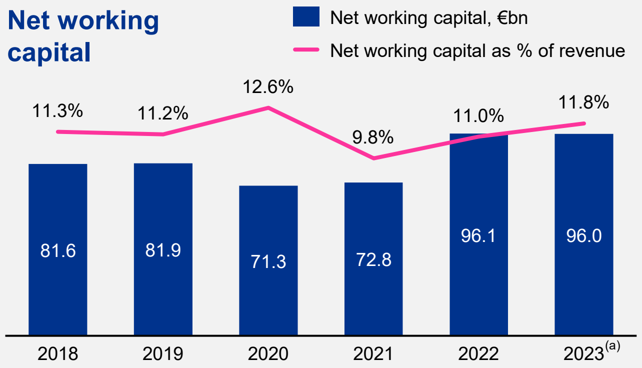
Working capital study

From 2018 to 2022, DPO and DSO have improved for companies in the Netherlands, while DIO deteriorated

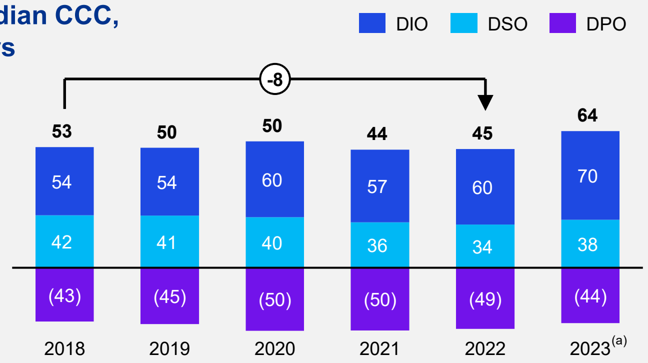
Working capital metrics have been deteriorating since the pandemic

In 2022, a substantial €96.1bn was tied up in net working capital on the balance sheets of Dutch companies. Following the decline in cash conversion cycle days during the pandemic, this metric started to deteriorate in 2022 driven by an increase in slow-moving stock as lower demand and high inflation discouraged consumer spending, while payable days shortened as recently implemented European and Dutch legislation requires companies to pay smaller suppliers faster.

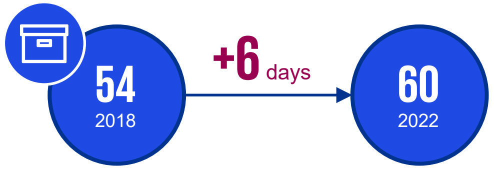
Net working capital



Median CCC, days

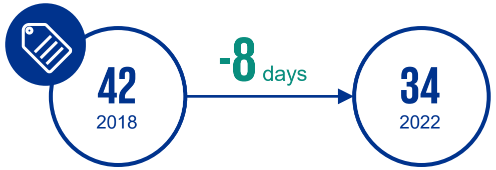


Median DIO, days



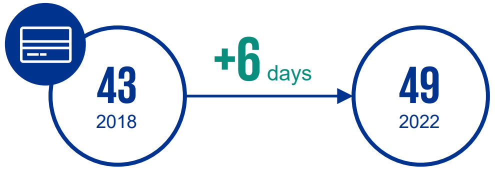
DIO was at a five-year high in 2023
The desire to maintain service levels in the face of supply chain uncertainty, coupled with material cost increases, led to absolute and relative inventory metrics increasing. Companies moved away from just-in-time to just-in-case inventory management as unpredictable consumer demand resulted in higher levels of safety stock.

Median DSO, days



DSO of Dutch companies benefitted during the pandemic from an increased focus on collections as DSO declined by 8 days from 2018 to 2022
While 2023 DSO is still below pre-pandemic levels, the downward trend has started to reverse. The temporary benefit appears to be driven by larger companies which strengthened their customer payment collection management as a first measure to offset the growing DIO days.

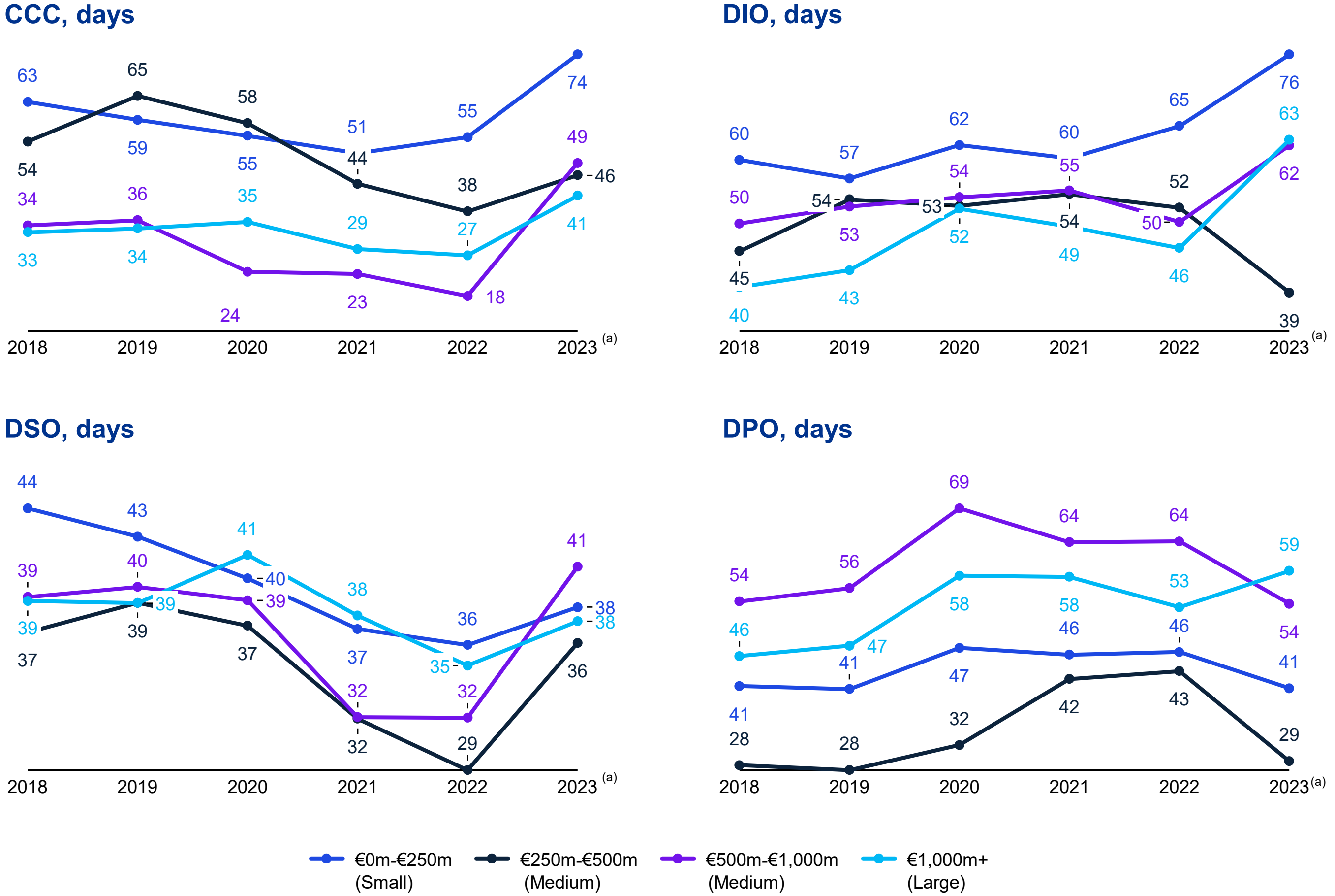
Median DPO, days



DPO, which was the driver of improving CCC days up to 2022, started to fall and was back to pre-pandemic levels in 2023
Following the pandemic, companies put more of a focus on stronger discipline in payables management to offset the deterioration in inventory, resulting in an increasing DPO. Since 2022, however, DPO started to revert to pre-pandemic levels. Part of this is due to the continued rollout of payment terms directives in the eurozone. This trend is likely to continue in the near future in the Netherlands as new legislation came into effect in 2022 that shortens the legal payment terms applied by large companies to SMEs from 60 to 30 days.

Note(s): (a) 2023 trend is based on analysis of 610 companies of the total of 1,232 companies analysed for the period of 2018 to 2022 due to limited data availability
Source(s): Capital IQ, Gain.pro, Company.info

Although medium sized companies saw the greatest decline in CCC from 2018 to 2022, the trend reversed in 2023



From 2018 to 2022 CCC days for all company sizes decreased with the most significant decrease in the medium companies (€250m - €500m and €500m - €1,000m revenue, - 16 days) on the back of DPO increase. This trend appears to be reversing in 2023, with DPO and DSO moving closer to pre-pandemic levels while DIO has continuously risen across most company sizes.

DIO

Since the pandemic, DIO has consistently been increasing with the steepest increase in 2023 for all company sizes except the **mid-range** (€500m - €1,000m). **Large companies** saw the highest increase in 2023 with 17 days increase as compared to 2022.

DSO

After a downward trend for **DSO** from 2018 to 2022 across all company sizes, the trend appears to have started reversing in 2023 with **medium-sized** companies returning to, and even surpassing pre-pandemic levels. At the ends of the spectrum, **small** and **large companies** were able to maintain some of the **DSO** decrease achieved up to 2022.

DPO

Large companies, which already had high **DPO** days due to their stronger negotiating power, saw the least improvement up to 2022 as European payment legislation is targeting larger buyers to pay their smaller suppliers more quickly. **Medium companies** had the highest **DPO** increases from 2018 to 2022, with 15 days (€250m-€500m) and 10 days (€500m-€1,000m), respectively.

In 2023, **DPO** started to revert back to pre-pandemic levels and the **DPO** of **small** and **medium-sized companies** appeared to reach 2019 levels.

Note(s): (a) 2023 trend is based on analysis of 610 companies of the total of 1,232 companies analysed for the period of 2018 to 2022 due to limited data availability
Source(s): Capital IQ, Gain.pro, Company.info

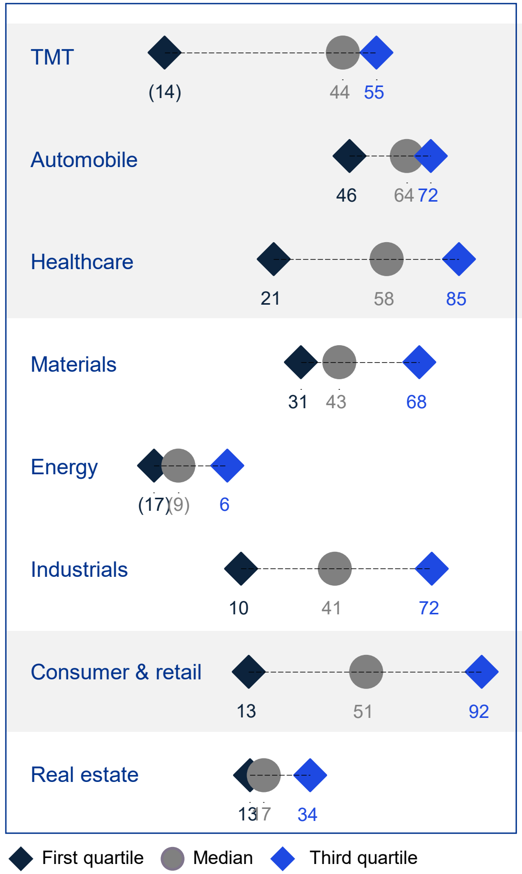
The TMT, automobile & healthcare industries saw deterioration, with consumer & retail witnessing varying performance

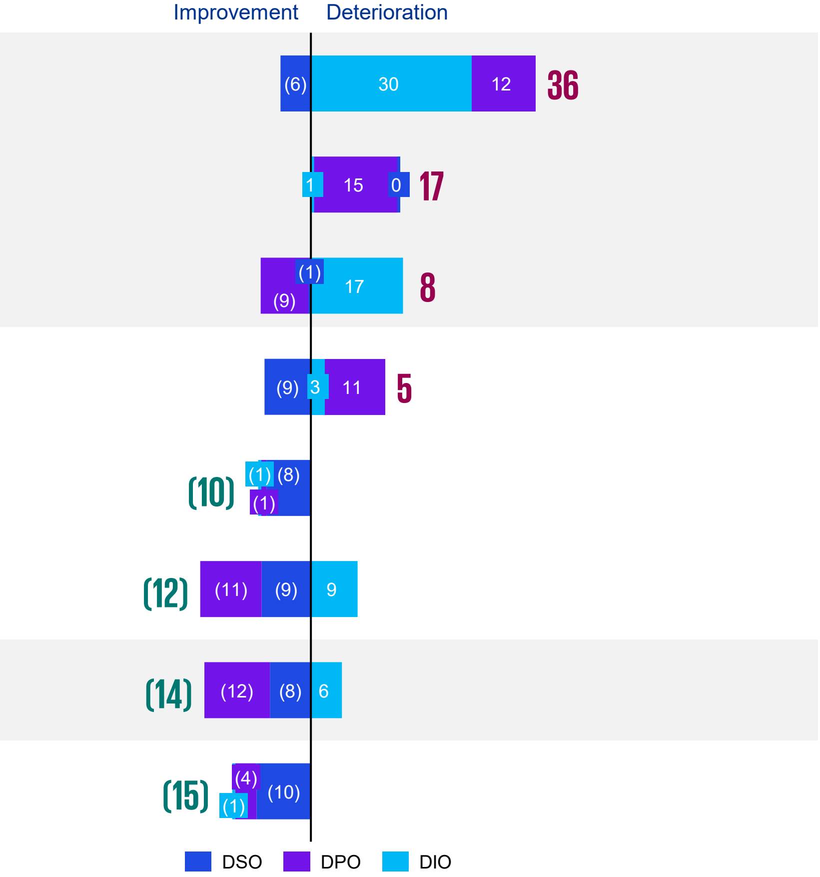
Technology, Media and Telecom (TMT) saw the largest increase in cash conversion cycle (CCC), largely driven by large DIO increases at technology hardware and equipment companies, while DSO and DPO decreased by 6 and 12 days respectively.

Automobile saw an increase of 17 days in overall CCC, mostly driven by a worsening of DPO as global supply shortages pushed car dealers towards early payments to secure stock, while DIO and DSO remained rather stable. The automobile sector has a small spread of 26 CCC days between the top and bottom performers as all sector players were affected by the same supply challenges, leaving little that could be done to differentiate working capital positions.

Healthcare was the third most impacted sector with 8 days increase in CCC, mostly driven by 17 days increase in DIO, somewhat offset by 9 days increase in DPO. The increase in DIO was mostly due to companies consciously increasing inventory in response to supply disruptions.

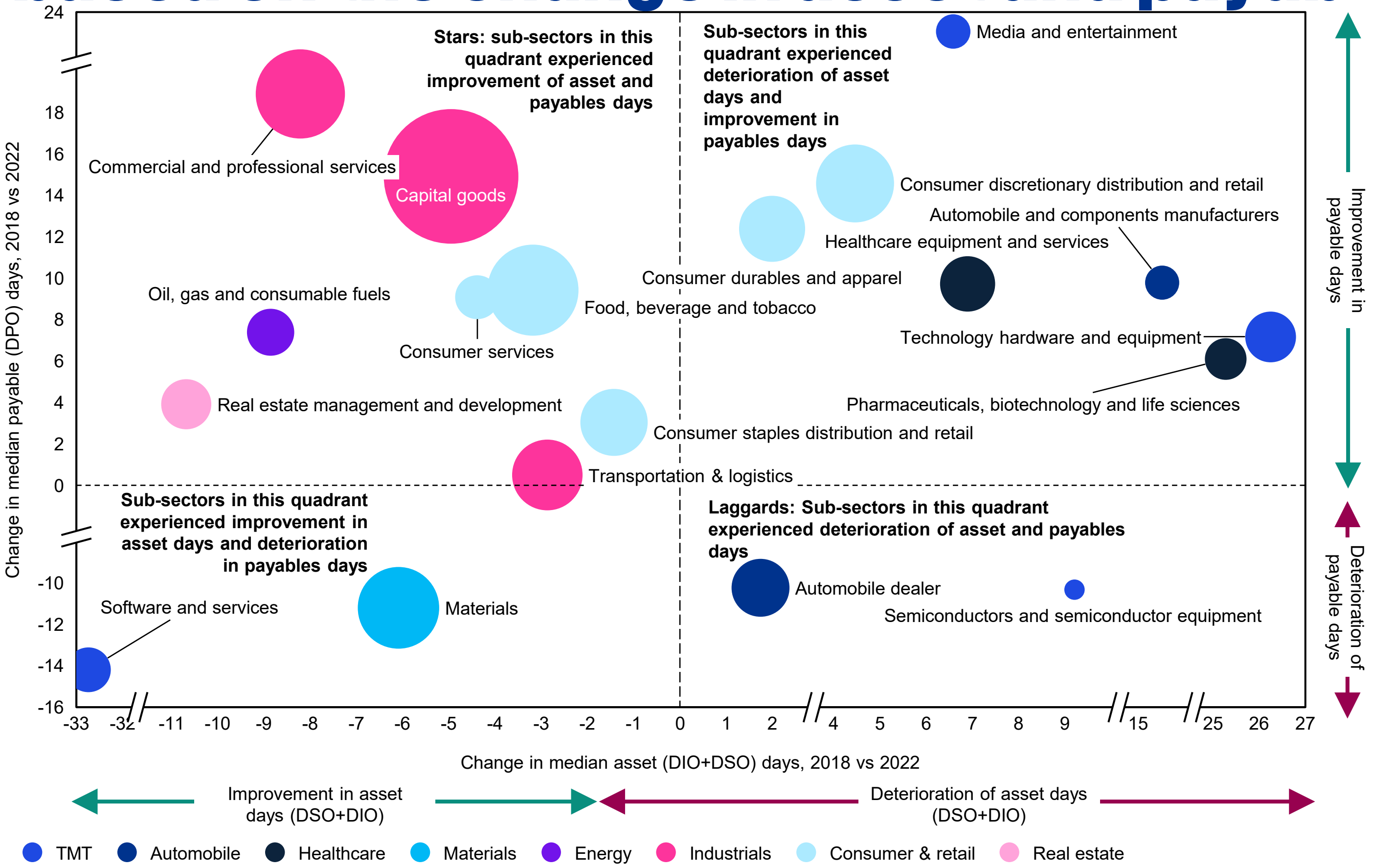
Consumer & retail saw an improvement in CCC of 14 days with both DSO and DPO improving, while the negative impact of DIO was more limited. This is the sector with the most inconsistent CCC between the top and bottom quartile. The large spread could be explained by the difference in the size of the various companies in the sample and their negotiating power. For instance, large food and beverage producers and retailers were able to substantially benefit from delaying payments and implementing strict customer control during the pandemic while smaller companies did not have this opportunity. Smaller companies also take longer to implement better financial control amidst global shortages and rising raw material costs.





Source(s): Capital IQ, Gain.pro, Company.info

Sub-sector view distils performance into stars and laggards based on the change in asset and payable days over time



Size of the bubble represents the count of companies

Note(s): Asset days are calculated as the sum of DSO and DIO days. Positive change in payable days indicate that DPO days increased, i.e. it took longer for companies to pay their suppliers.
Source(s): Capital IQ, Gain.pro, Company.info

At sub-sector level, several working capital winners and losers have emerged this year.

The **TMT** sector saw a noteworthy increase in asset days, accompanied by a decrease in payable days. This trend can be attributed to growing inventory levels in **technology hardware & equipment, semiconductors & semiconductor equipment, media & entertainment** companies in response to increasing demand, as well as a reduction in supplier payment days in **software and services**. The sector is characterised by different working capital dynamics, as is visible in the large spread between top and bottom performers, with software companies essentially having a negative cash conversion cycle while hardware and semiconductor companies have significant inventory requirements, driving CCC days up.

The **automobile** sector demonstrated an overall increase in working capital requirements, with **automobile dealers** being squeezed by large manufacturers for faster payments to secure stock while **automobile and components manufacturers** were able to benefit from stronger negotiating power which compensated for growing inventory positions up to some extent.

Healthcare companies including **pharmaceutical, biotechnology and life sciences,** as well as **healthcare equipment & services** companies experienced an increase in asset days compared to the pre-pandemic period, primarily driven by increasing inventory due to Covid-19 and global supply challenges.

Although the **consumer & retail** sector witnessed an overall decrease in asset days, sub-sectors such as **consumer discretionary distribution & retail, consumer durables & apparel** experienced an increase. This was driven by higher inventory levels due to changes in consumer demand and spending as high inflation rates redirected consumer spending away from durables and apparel and towards essentials such as food, beverage and staples.

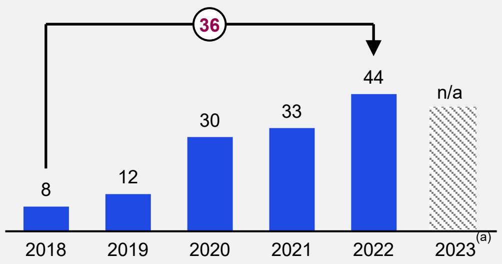
03
Selected sectors deep dives

The largest working capital deterioration came in the TMT sector, driven by post-pandemic and supply chain effects

Technology, media, and telecom (TMT)

The sector experienced a significant increase of 36 days in CCC from 2018 to 2022, mainly due to a 30-day increase in DIO. The sector was largely impacted in 2022 as demand slowed down post-pandemic and supply chain disruptions resulted in delays in obtaining tools and components. With high inflation putting pressure on customer demand for end-products such as smartphones and consumer electronics, the normalisation of inventory levels may take some time as inventory drawdown is expected to happen slowly, indicating the importance for companies to take proactive measures to optimise their working capital.

Cash conversion cycle, days



2022 WC metrics, days

Variance from 2018: # days

Semiconductors and semiconductor equipment

CCC deteriorated by 20 days between 2018 and 2022 driven by an 11-day increase in DSO and a decline of 10 days in DPO over the period. The global scarcity of components put the semiconductor industry in a tight spot with payment terms shortened, most likely due to suppliers requiring faster payments to provide the necessary parts in a shortage market. This was exacerbated by customers delaying payments and even cancelling orders during 2022.

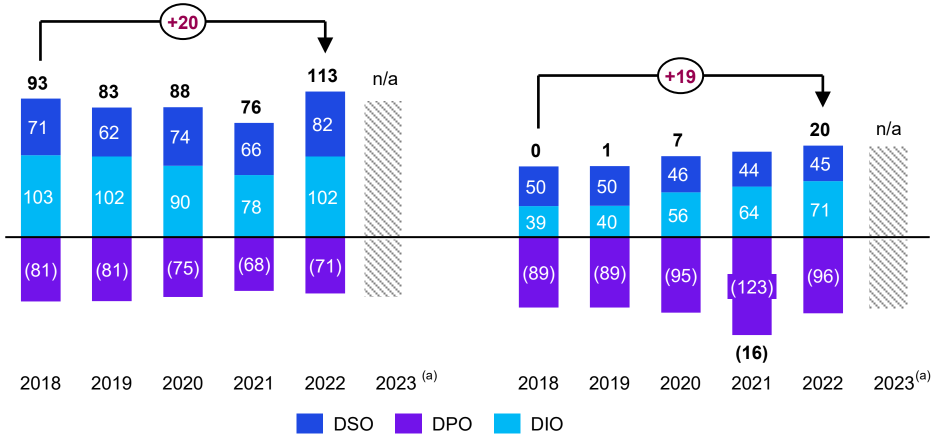
Technology hardware and equipment

CCC worsened by 19 days, with a significant increase in DIO of 32 days, while DSO and DPO improved by 5 and 7 days respectively. This sub-sector was significantly impacted by global chip shortages, leading companies to consciously increase inventory to plan for potential supply disruptions. This may have led companies to focus on improved cash collectability and better payment management to partly offset negative inventory impacts.

CCC by sub-sector, days

Semiconductors and semiconductor equipment

Technology hardware and equipment



"Industry leaders in the technology hardware and semiconductor sub-sectors feel that currently the industry has reached its peak in terms of excess inventory. Only a year ago companies were still stocking up to avoid inventory shortages for fear of losing revenue. Currently leaders are optimistic that accelerating technologies like AI are slowly restoring the balance between supply and demand. The industry is cyclical, and it has swung from a dynamic of constraints to softer demand. To navigate the cycle and get back on top, leaders have more recently set their priorities as reducing inventory and increasing the geographical diversity of their supply chains."

Bas Smits
Director
KPMG Netherlands

Note(s): (a) Due to limited data availability for 2023, the 2023 figures are excluded from the analysis on this sector.
Source(s): Capital IQ, Gain.pro, Company.info

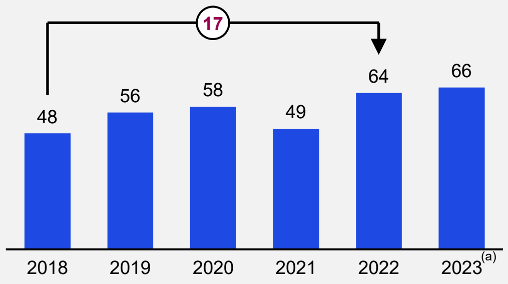
Driven by the need to secure stock, the automobile sector performance has worsened

Automobile

The sector experienced an increase of 17 days in CCC, largely due to automobile dealers making early payments to car manufacturers to secure stock.

The two automobile sub-sectors experienced similar CCC but opposing DPO developments, with large manufacturers improving their DPO by 10 days due to significant negotiating power with smaller suppliers, which somewhat compensated for the growth in both inventory and DIO. On the other hand, automobile dealers were pressured by the same large manufacturers to pay earlier in order to secure stock.

Cash conversion cycle, days



2022 WC metrics, days

Variance from 2018: # days

Automobile and components manufacturers

In this sub-sector, the DPO saw an improvement of 10 days compared to 2018 as large OEMs were able to delay payments to smaller parts suppliers due to their negotiating power. This somewhat compensated for the growing DIO due to the persistent challenge of inventory pressure, particularly in the electric vehicle (EV) market where demand has declined. In the short-term inventory is expected to increase further as manufacturers are shifting from global to regional supply chains because of rising tariffs on Chinese imports.

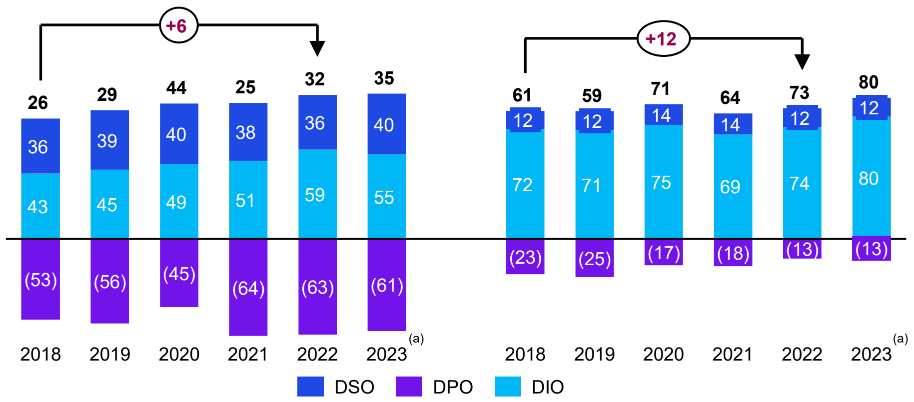
Automobile dealers

CCC lengthened by 12 days due to early payments to suppliers in order to secure stock while DIO and DSO remained rather stable up to 2022.

CCC by sub-sector, days

Automobile and components manufacturers

Automobile dealers



"As we have seen in the last few years, large OEMs are vulnerable to global supply shortages. Rising tariffs on Chinese imports are pushing OEMs to reconsider their business and distribution models and shift from global to regional supply chains. These changes will lead to inventory build-up in the short-term as companies are relocating manufacturing."

Stijn de Groen
Director
KPMG Netherlands

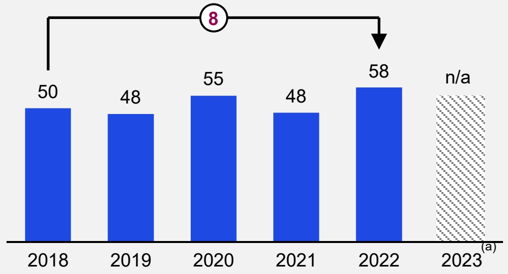
Note(s): (a) 2023 trend is based on analysis of 33 companies of the total of 65 companies analysed for the period of 2018 to 2022 due to limited data availability
Source(s): Capital IQ, Gain.pro, Company.info

Global supply challenges, preference policy and equipment shortages have led to a deterioration of CCC in healthcare

Healthcare

The sector saw its average CCC days go up 8 days mostly due to high inventory levels driving up the working capital requirements. Both healthcare sub-sectors were impacted by multiple supply chain headwinds in 2022 including cost inflation, global shortages and a tighter labour market. These disruptions led healthcare companies to keep additional inventory buffers to guard against supply shortages.

Cash conversion cycle, days



2022 WC metrics, days

Variance from 2018: # days

Pharmaceuticals, biotechnology and life sciences

The sub-sector experienced a deterioration of 19 days in CCC driven by increasing inventory and late collections from customers. It appears that large companies focused on better financial administration and stricter cash collection amid the pandemic and global supply challenges.

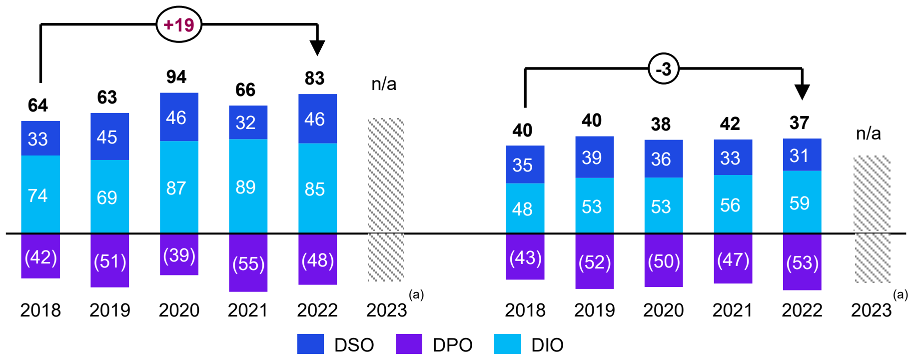
A particularity of the Dutch system with the new legislation called preference policy ("*preferentiebeleid*" in Dutch) implies that pharmacies are only allowed to purchase generic medicines from a selection of suppliers on a preference list determined by insurers. Aggravated by the medicine (including active pharmaceutical ingredients) shortages, this has led to a recalibration of the inventory positions, where stock levels of some medicines were strategically increased whilst other medicines could not be obtained due to the market-wide scarcity and/or are not considered preferred.

DSO slightly decreased post-pandemic (in 2021) as customers tended to pay earlier to secure their access to the required products.

Healthcare equipment, products and services

Although companies in this sub-sector witnessed a decrease of 3 days in cash conversion cycle, DIO increased by 11 days from 2018 to 2022 as shortages of equipment and products in the market led many companies to order more stock in advance to ensure they were able to meet their contractual obligations.

CCC by sub-sector, days



"Multiple global and local challenges have impacted the healthcare sector in recent years, particularly with respect to inventory management. With the Covid-19 pandemic coming to an end and global supply challenges slowly easing, we see that healthcare organisations are slowly taking back control of their stock. 2023 seems to have been a 'reset' year when companies could put a brake on the excessive orders to secure equipment and medicines, while the supply challenges slowly eased. With new trends developing in the healthcare landscape (e.g. new legislation like preference policy, shortages of medicines, declining prices for raw materials after significant increases over 2022-2023), we expect repositioning of inventory management strategies."

Tatiana Leunissen
Director
KPMG Netherlands

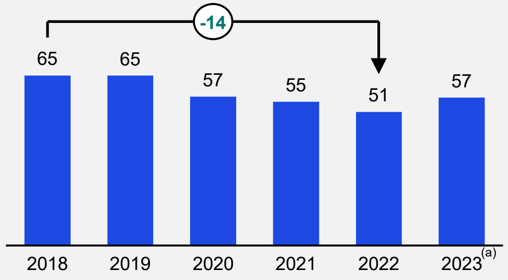
Note(s): (a) Due to limited data availability for 2023, the 2023 figures are excluded from the analysis on this sector.
Source(s): Capital IQ, Gain.pro, Company.info

Although consumer and retail CCC improved, inventory levels remain an issue within the sector

Consumer & retail

The sector improved its cash conversion cycle by 14 days, mainly driven by longer DPO days as large producers and retailers in the Netherlands were able to extend payment terms in response to growing inventory levels. DIO increased by 6 days in most sub-sectors as customer demand returned to normal levels post-pandemic, while labour and shipping container shortages resulted in delayed deliveries and forced companies to pre-order their inventory. The CCC trends observed started to reverse in 2023 with DPO returning towards pre-pandemic levels, driven by increasing focus on large companies to ensure they pay small suppliers in time, in line with EU and Dutch legislation.

Cash conversion cycle, days



2022 WC metrics, days

Variance from 2018: # days

Food, beverage and tobacco

The sub-sector experienced an improvement of 13 days in CCC driven by longer supplier payments and faster collections from customers. It appears that large companies focused on better financial administration and stricter cash collection amid the pandemic and global supply challenges.

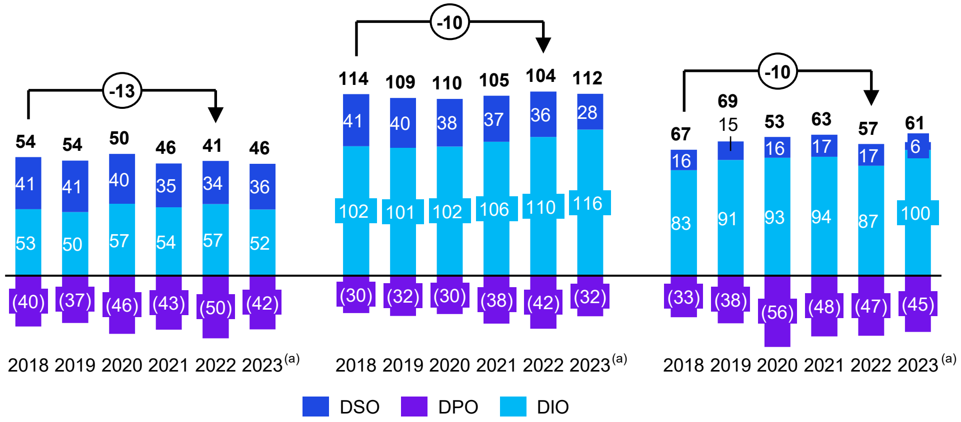
Consumer durables and apparel

CCC shortened by 10 days from 2018 to 2022 despite the rise in DIO of 8 days. Longer DPO of 12 days was the key driver of the improvement, potentially driven by stricter financial administration implemented by large companies in response to growing inventory levels. The CCC trend seems to reverse in 2023 with DPO going back to pre-pandemic levels.

Consumer discretionary distribution and retail

CCC days witnessed an improvement of 10 days driven by an increasing DPO. DIO increased by 4 days up to 2022 and has grown by another 13 days in 2023 alone, as high inflation negatively affected consumer discretionary spending, resulting in lower inventory turnover.

CCC by sub-sector, days



"C&R companies saw significant increases of slow-moving stocks because of the pandemic, global supply shortages, and Russia's war on Ukraine and the resulting energy crisis. To cope operationally, companies focused on improved financial administration, by making sure customers paid on time while supplier payments were stretched when possible. However, because of the higher focus on cash, key underlying areas were missed, such as the persistent challenges of integrating business planning and resolving the problem of slow-moving stocks. With so many issues at stake, these underlying areas will become more urgent and lead to a worsening of working capital in the near future."

Bart le Clef
Partner
KPMG Netherlands

Note(s): (a) 2023 trend is based on analysis of 165 companies of the total of 369 companies analysed for the period of 2018 to 2022 due to limited data availability
Source(s): Capital IQ, Gain.pro, Company.info

04

Considerations to create competitive advantage

Considerations to create competitive advantage in 2024

After the last few turbulent years, resulting in disrupted supply chains and inventory build-ups, companies cite that focusing on efficient working capital management is one of their top priorities for 2024. Private equity (PE) firms across global markets are holding assets for longer. In 2023, the majority of PE assets sold were the best performing ones.

In addition, we have observed that companies looking to be sold demonstrate a disconnect between their actual historical trends and the ambition reflected in their business plans. In the current economic environment, PEs realise that the best preparation for the exit readiness, and to prepare for investor scrutiny, is to focus on value creation, by growing revenue, improving profitability and operational leverage, and managing cash flows. The pandemic brought a renewed focus on working capital efficiency. This should continue and be amplified given the global dynamics today. Companies are starting to realise that working capital encompasses more than the management of accounts receivable and payable. Instead, it is the interplay of risks, costs, and opportunities between all the components of current assets and liabilities.

01 Improve cash culture by putting in place a stronger cash flow process, which includes liquidity risk checks and KPIs that are monitored regularly.

Working capital accountability should be adopted by all parties within an organisation that influence it. Companies should drive an organisation-wide approach that embeds the cost of working capital into decisions impacting financial and operational processes, resulting in a stronger cash culture that puts working capital opportunities and costs at the heart of all decisions.

To achieve this, companies should implement measurable key performance indicators (KPIs) that are relevant and data-driven. Traditional KPIs include DSO, DPO and DIO. Additional KPIs can be implemented such as dispute resolution days, KPIs around slow-moving and aged inventory, cash conversion efficiency (CCE), overdue receivables as a percentage of total receivables, weighted average days to pay and cash-to-cash cycle time. Key stakeholders across the organisation should be responsible for implementing, tracking and acting upon these KPIs. This will ensure that stakeholders are aligned with shared goals and working capital progress can be measured efficiently.

In addition, companies should focus on risk management to address business volatility and ensure a holistic approach to better assess and mitigate the variety of risks their businesses face. Liquidity stress testing methodologies similar to those deployed at banks should be implemented, leading to companies being better prepared for unforeseen events and making better decisions that protect the business. Examples include running detailed scenarios for business and market conditions under various stress tests to assess potential outcomes and their impact on cash flow, balance sheet, supply chain disruptions and customer credit losses. Finally, regular reviews and adjustments to the process should be implemented to respond promptly to evolving business and market conditions.

02 Establish suitable customer and supplier terms in line with sector- and country-specific norms and eliminate early payments to promote efficiency and fairness across the supply chain.

Industry norms and benchmarks often reveal opportunities to improve or harmonise payment terms. Consider the rates at which you pay your suppliers versus the rates at which you receive cash from your customers and eliminate unfavourable misalignments by renegotiating terms. For customers, the best approach is to agree on the right payment terms at the outset, rather than renegotiating them later. For example, if standard customer terms are 30 days but sales teams frequently offer 60 days, understand why this is happening and act accordingly. When contracts are due for renewal, look to realign existing terms or, at the very least, maintain them.

Additionally, it is recommended to review terms for different customer categories / segments and assess the best strategy for each based on both commercial perspective and profitability. By categorising customers based on their purchasing habits, volume, and profitability, you can tailor payment terms to optimise working capital. This could involve offering more favorable terms to high-volume or highly profitable customers, while implementing stricter terms for low-volume or low-margin customers to ensure a balance between maximising cash flow and maintaining profitability.

03 Identify inefficiencies and improve the forecast-to-deliver (F2D) process with the help of technology.

Various quick wins are available in the F2D process. Using the 9-box inventory segmentation model allows companies to monitor items with infrequent or volatile demand. This can help inform make-to-order or make-to-stock strategies.

Stock keeping unit (SKU) rationalisation can drive simplicity in an organisation by focusing on a smaller set of high-demand, profitable SKUs. This helps improve bottom line performance and available cash on the balance sheet.

By employing technology, a large part of the F2D process can be automated, leaving more space and time for data-driven decision-making. Amongst the emerging solutions that Gen AI offers are the following:

- Distributed order fulfilment that optimises picking, packing and delivery routes via real-time analysis, enhancing efficiency and customer satisfaction; and
- AI-enhanced quality management: Use of AI can revolutionise quality control, automating documentation and facilitating real-time anomaly detection for improved efficiency and product reliability.

As a response to the Covid-19 pandemic and recent economic and geopolitical developments, companies across most sectors increased their safety stocks. Many company leaders believe that by 2023 they had excess inventory. To succeed and improve cash cultures in the short term, companies need to reconsider just-in-case inventory strategies. The top emerging uses of Gen AI which can support organisations in this are:

- Intelligent demand & network optimisation: Use of AI for precise demand forecasting, replenishment planning, safety stock optimisation, segment analytics, cost-to-serve insights, strategic network and inventory optimisation, enabling real-time adaptability and transparency[1].

Source: (1) KPMG – AI & generative AI in functional transformation, 2024.

04 Deploy automation and intelligence to plan customer collection cycles and implement strict regular reviews for customer default risk.

Companies are already utilising AI and machine learning in various internal order-to-cash (O2C) processes, including invoice generation and distribution, automatic payment tracking, automated reminders and collections and reconciliation automation. The main challenge in the O2C cycle remains the ability to efficiently collect on customer invoices. Amongst the top emerging Gen AI uses which can support organisations in this challenge are:

- Contract generation and review: Generating standard contracts with preferred terms and wording, monitoring and reviewing risk and profit of existing non-standard contracts;
- Optimising quote to cash: Analysing large volume datasets to identify patterns and trends for customer behaviour, accounts receivable aging and default rates;
- Financial risk management: Improving financial crime compliance by aggregating data and creating an accurate portrait of each customer[2].

05 Employ analytics and AI to eliminate inefficiencies and enhance decision-making in the purchase-to-pay (P2P) process.

Companies need to ensure they have suitable payment processes based on their geographies and industries. Especially companies with global operations need to adjust their policies based on local norms and legislation to ensure fair supplier treatment and prompt payment whilst optimising working capital performance.

When asked which technologies will have the greatest impact on their firm's procurement function over the coming year, senior procurement specialists ranked Gen AI and predictive analytics as number one and two, respectively. Limited data and insights were cited as the top internal challenge faced, indicating an urgent need to invest in this area[1].

Generative AI has the potential to automate, optimise and transform the P2P process, driving enhanced efficiency and strategic decision-making. Amongst the top emerging Gen AI uses in the P2P process are:

- Automating the RFx processes in procurement, streamlining requirement generation, RFx creation, supplier evaluation, and decision-making;
- Dynamic contract lifecycle management: Automating supplier contract creation, negotiation support, compliance verification, risk detection, performance tracking, and renewal processes;
- Streamlining user procurement: Product discovery, simplification of the buying journey, and guidance towards compliant suppliers;
- Revolutionising financial procurement: Optimising invoice processing, payment schedules, reconciliation and cash management, with predictive insights; and
- AI-enhanced supply chain visibility: Mapping multi-tier supplier networks, assigning risk scores, integrating regulatory requirements, and enhancing visibility on inherited and concentrated risks[2].

Source: (1) KPMG – Future of procurement, 2024.
(2) KPMG – AI & generative AI in functional transformation, 2024.

06 Explore working capital financing to optimise the cash cycle.

A recent study of European growth companies[1] found most top performers in the healthcare and mobility sectors used external working capital solutions to successfully improve operational efficiency in 2023. The key uses of solutions varied between industries. Both healthcare and mobility companies used external WC financing, primarily for strategic growth investments such as capital investments in company assets and organic business expansion. The most used solutions in 2023 were working capital loans and overdraft facilities.

Among the top benefits of WC solutions cited by CFOs were securing a favourable cost of capital when prioritising new business initiatives and new partnerships and building better relationships with customers and partners. CFOs mentioned that having access to external capital solutions allowed them to better meet customer demand and take advantage of business opportunities and they were able to improve their buyer/supplier relationships by accessing these financing solutions.

Less used solutions (approximately 10% of the companies in the abovementioned study), that also offer benefits for both buyers and suppliers are receivables and payables financing.

Receivables finance accelerates the cash conversion cycle through financial products such as factoring solutions, invoice discounting, portfolio-based financing and securitisations. At their core, all these solutions offer the company (seller) financing capital related to a portion of its accounts receivable. The financing agreements can be structured in multiple ways, usually with the basis as either an asset sale or a loan. Which product is best for a company will depend on the customer portfolio (e.g. whether the company has a concentrated or diverse pool of customers).

Payables finance offers an alternative source of financing, benefiting both buyers and sellers. Typical solutions include reverse factoring (also known as supply chain financing) and dynamic discounting. Both solutions provide suppliers with the option of receiving early payment in exchange for a discount on their invoice, but reverse factoring includes a third-party financial institution while dynamic discounting involves no such third party. When using a third party, its software is typically connected to the buyer's ERP system, allowing for an automated process. Both financing options offer benefits for buyers and sellers. While suppliers gain quicker access to cash, buyers get more time to pay off their balances.

Another option is inventory financing which functions as a type of short-term loan which uses companies' existing inventory as collateral when purchasing new inventory for their production cycle. Benefits of inventory financing include improved capital and operations management, particularly in terms of cash flow optimisation. Current inventory is transformed into working capital, allowing greater financial flexibility such as the possibility to negotiate better supplier terms, thereby reducing costs and streamlining operations.

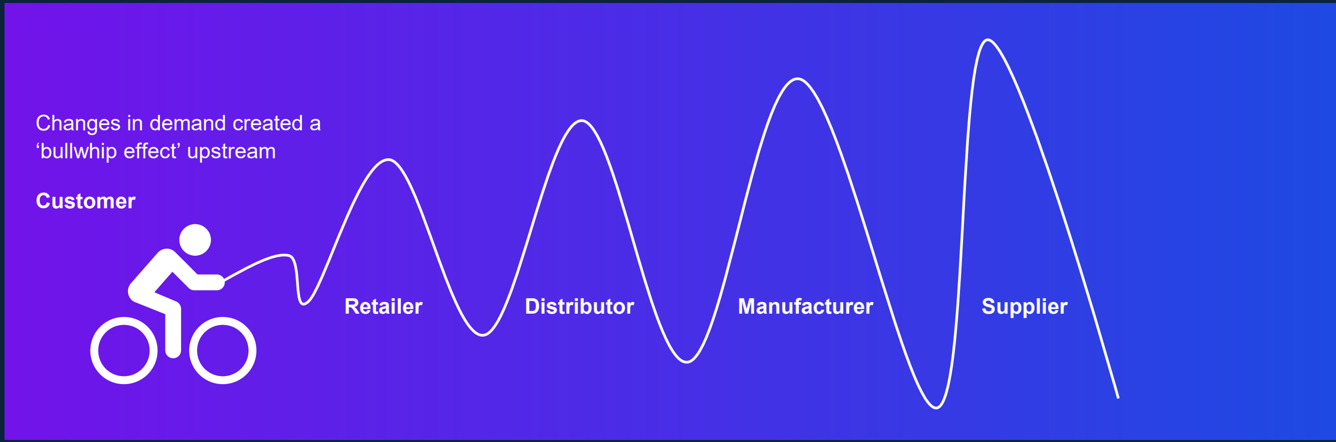
We recommend assessing the best available working capital financing options taking into account both EBIT(DA) and cash cycle impacts. Additionally, accurate and favourable SPA treatment in a potential M&A context, including perceptive on recurring nature of these solutions requires careful consideration.

Source: (1) VISA – Growth corporates working capital index, Europe edition, 2024.

05

A look at the bicycle industry

The cycle of recovery: A look at the impact of Covid-19 on the bicycle industry and the path towards recovery



Bicycle industry growth fuelled by Covid-19

While cycling has long been popular in the Netherlands, Covid-19 caused a surge in demand for bicycles as people searched for outdoor activities and new methods of transport. In each of the two years prior to Covid-19, there were an estimated 1.05-1.06m bikes sold in the Netherlands before the figure jumped to 1.18m in 2020[1]. This increase brought the market to an estimated EUR1.88bn (EUR0.46bn increase from the prior year), although it is expected to increase to EUR1.96bn in 2024[1]. This increase is mainly attributed to the popularity of e-bikes, which are substantially more expensive than conventional bikes. E-bikes represented 46% of bicycles sold in the Netherlands in 2020, and this is expected to continue to grow towards 53% in 2024[1].

The focus on the industry also extended to M&A, with the number of transactions in the industry doubling and financial investors increasing their share from 43% to nearly 59% worldwide[2].The explosive growth in the bicycle industry, and the ensuing inventory issues faced by leading companies, offers insights into the importance of working capital governance and preparedness for factors outside a company's control.

Navigating the shaky ground of increased demand

With a large and sudden uptick in demand, it is no wonder the bicycle industry has had trouble finding its footing in the past few years. Demand issues, however, are only part of the problem facing the industry. The increase in demand also set off a 'bullwhip effect', where the increase in consumer demand is met by order increases by retailers and production increases by manufacturers and suppliers. As part of the sudden increase in consumer demand for bicycles was temporary, once the demand diminished, retailers found themselves with excessive stock.

Further down the supply chain, manufacturers and suppliers ramped up production capabilities to meet the demand growth they saw as sustainable. On the contrary, however, the growth was unsustainable and the resulting impact on inventory levels was disguised by companies seeking out multiple suppliers to mitigate supply chain risks exacerbated by Covid-19. The popularity of e-bikes added to the complexity, as they include specialist, expensive parts that regularly need repairs.

Although the bicycle industry has been engulfed in the 'bullwhip effect' since 2020, there is hope that it is coming out the other end. As stock returns to normal levels and supply chain issues fade away, bicycle companies are looking towards their future. Still, there are lessons to be learned from Covid-19 and the impact it had on this important industry.

Source: (1) KPMG – BOVAG - . (2) Bike Industry M&A Study (hl.com)

Shifting gears towards improved working capital management

The bicycle industry, like many industries emerging from the shadows of Covid-19, is poised to regain its equilibrium in the coming year. To do so, the industry must learn from past mistakes and focus on three core areas that will increase stability and minimise the chances of disruption in the future:

1. **Improving demand forecasting**

Especially considering the rise in e-bikes, with their expensive components, there is a need for retailers to improve their ability to accurately assess consumer demand. Improved forecasting powered by deep data analytics will limit the possibility that inventory levels will explode due to one-off circumstances, while also reducing lead times as the production and inventory of manufacturers and suppliers return to normal levels;

2. **Increasing supply chain alignment**

Demand forecasting improvement is one way of increasing coordination throughout the supply chain, but it is not the only way. Retailers can partner with manufacturers through increased information-sharing, establishing KPIs and incentives, and refining contracts to consider volume flexibility, dynamic discounting or shared risk management. Closer collaboration throughout the supply chain remains possible and all players will reap the benefits;

3. **Professionalising working capital management**

The importance of working capital governance and applying best practice is often forgotten until issues arise. Instead, companies in the bicycle industry should focus on establishing clear governance and conduct regular analyses to assess their working capital positioning. Continuous review of the key working capital metrics, as well as more detailed analyses (e.g. ABC analysis, payment terms optimisation, etc.), will ensure companies are not left behind in the future.

"Lower demand has remained longer than expected, yet the most dire straits are behind us. The shake-out is likely to continue for a while, and manufacturers/OEMs need to consider strategic adjustments."

Joeri Jägers
Partner
KPMG Netherlands

06
How we can help

We help transform working capital performance at speed using a technology-enabled approach

At first sight, it can be challenging to see where opportunities exist to release cash from working capital. Understanding where the opportunities lie and unlocking that value can bring significant benefits, from better cash flow to more funds for M&A, debt reduction or investment.

KPMG brings a fresh perspective to help organisations find and free up the cash from working capital within their business.

We look at people, processes, systems and culture to find and unlock cash and working capital value. We take a hypothesis-driven approach, which combines data-intensive analytics with targeted discussions to identify and validate opportunities.

Our working capital advisors are highly skilled, specialised professionals. We partner with clients to drive fast and tangible value, often working shoulder-to-shoulder with their team.

We draw on the support of KPMG's vast array of dedicated subject matter experts. We can also tap into KPMG's global working capital advisory network to gain perspectives on strategies that are working in other geographies and align with the latest thinking on global best practice.

We help a wide variety of corporations and private equity clients to rapidly identify and deliver quick wins and sustainable working capital improvement.

01 Rapid cash and working capital improvement diagnostics that enable us to quickly identify sources of upside and the steps needed to achieve this value.

02 Implementation support to help our clients define, develop and implement practical changes to their business.

03 Working capital improvement through end-to-end project management.

04 A suite of digital tools which can help our clients proactively identify and address working capital issues.

Working capital optimisation helps companies in a deal context get compensated for their value up front if the business is divested

Business owners often reach a point where they start to contemplate the sale of the business they have built, whether to cash out value and free themselves up for the next challenge, or to bring in private equity (PE) investment to provide additional capital alongside support to drive growth under the PE house's part ownership.

One aspect of estimating the value of the business lies in its cash flow conversion i.e. how do profits from the business convert into cash, for future investment in growth? The focus on cash conversion has increased in recent times as economic conditions have tightened.

In addition, the compensation which owners will receive when selling their business is not only the company value based on its earnings potential. The company value will be adjusted to be free of debt and cash, and with a normal level of working capital.

We help companies throughout the sale process, and we provide working capital diagnostics which can be deployed in a deal context, benefitting both the organisation and the deal process through:

01 Controlled equity story

Preparation is everything in a sales process. Data-backed stress tested initiatives strengthen the equity story, and ease potential investor concerns, establishing a clear path for further value.

02 Improved deal speed

Substantiated and quantified value upside measures and implementation roadmap will improve transparency and accelerate any potential buyers' assessment.

03 Increased deal value

Robust and evidenced value upsides and business plan measures increase bidders' confidence in the plans provided and will drive deal value.

07
Appendix

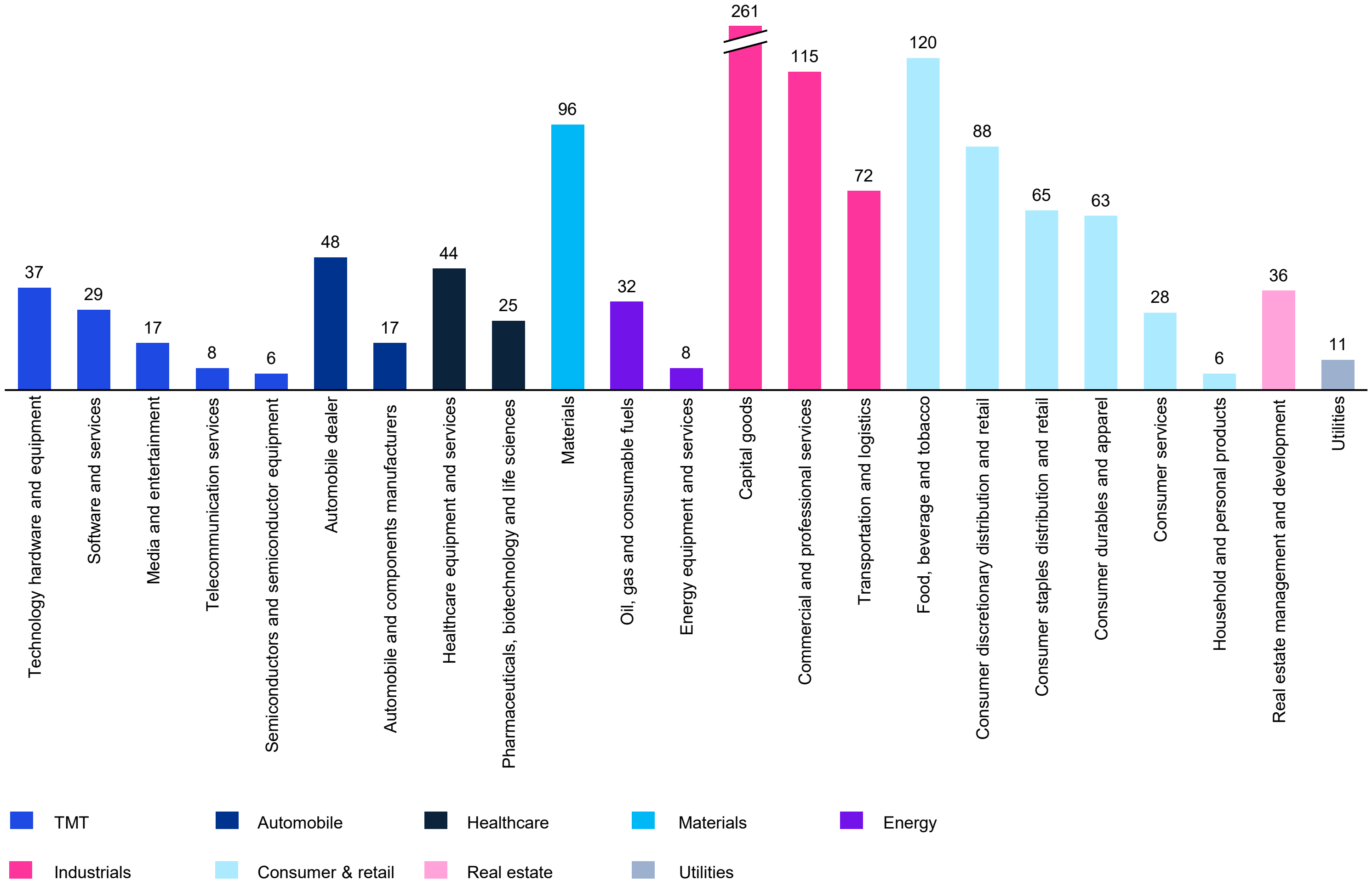
Basis of preparation

We analysed the financials and working capital performance of Dutch companies with data publicly available as of July 2024. Our analysis includes over 1,200 companies for which data was available consistently over the period 2018 until 2022.

For these companies we also obtained data for 2023. However, as of this date, not all companies have published financials for 2023. The number of companies with financials for 2023 in our database is approximately 610. Because of this, in some analysis on sector and sub-sector level, the 2023 data has not been presented as the number of companies would be too small to bring reliable insights. The specific analysis where 2023 is excluded is indicated on the respective pages throughout the document.

The full database used in this study covers all business sectors in the Netherlands. However, to provide further sector insights, this study focuses on four key sectors: TMT, Automobile, Healthcare and Consumer & retail. These sectors were selected because KPMG has extensive expertise in these specific sectors and because these sectors showed the most significant movements over the period under scope in the study.

Working capital metrics specified in this study are median metrics of respective sector / industry unless stated otherwise.



Note(s): Based on analysis of 1,232 companies with data available for all 5 years (2018 to 2022)
Source(s): Capital IQ, Gain.pro, Company.info

Glossary and contributors

Glossary

bn	Billion
CCC	Cash conversion cycle
CCE	Cash conversion efficiency
CFO	Chief financial officer
C&R	Consumer and retail
DIO	Days inventory outstanding
DPO	Days payable outstanding
DSO	Days sales outstanding
F2D	Forecast-to-deliver
Gen AI	Generative artificial intelligence
HICP	Harmonised index of consumer prices
KPMG, we, us	KPMG Advisory NV
m	Million
NWC	Net working capital
O2C	Order-to-cash
OEM	Original equipment manufacturer
P2P	Purchase-to-pay
SKU	Stock keeping unit
TMT	Technology, media, and telecommunications
WC	Working capital

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