HSBC's Guide to Cash, Supply Chain and Treasury Management in Asia Pacific 2012

Efficient Accounts Payable Process: A Challenge to Overcome

- While there is a strong treasury focus on accounts receivable (A/R) to help meet the goal of effective cash management, a similar focus is needed on accounts payable (A/P).
- Several internal and external challenges must be dealt with to make the process more efficient, which can be addressed by various A/P management strategies.
- The key to a more effective A/P process may lie in building a strategic partnership among corporates, banks and vendors.
- Value-added services from banks to help corporates manage their A/P would streamline the process while maximising value and minimising cost.

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Corporate treasurers consider accounts payable (A/P) and accounts receivable (A/R) core partner departments. The primary task for a treasurer is the effective utilisation of surplus cash – in other words, effective cash management to improve operations. Treasurers focus on various ways to improve cash value by considering various investment mechanisms such as fixed deposits. While there is a strong focus on A/R to help meet this goal, a similar focus is needed on A/P to make the process more efficient and cost effective. As corporates expand their business operations from one vertical industry to another, it is essential that they look at possible ways to streamline their processes and create strategic partnerships with banks and vendors. This article examines how the A/P process can be made more effective by building a strategic partnership among vendors, banks and corporates.

The Need for Streamlining A/P

The corporate A/P department expends considerable effort to accomplish tasks such as receiving, entering, validating and processing invoices. These distinct steps increase maintenance costs while making organisations lose out on the benefits of early payment to vendors. This can be attributed to several factors such as heavy paper invoice management, lack of standardisation across invoices provided by vendors and loose integration of internal systems. While e-invoicing helps significantly in modernising the process, there are areas that can be streamlined to avoid process gaps and minimise late fees and processing costs. As organisations expand their operations and adapt to changing market conditions to remain competitive, the areas of financial controls and compliance require attention.

There are numerous roadblocks hindering the effectiveness of A/P, within the organisation and in its dealings with vendors and banking partners.

Challenges Within the Organisation

- The A/P department receives inputs from various key departments such as infrastructure, payroll and internal tax teams. A lack of system integration might enable these departments to report A/P information at their convenience, an inefficiency that leads to improper cash flow analysis by the treasury department. Non-integrated systems also add to the complexity of the process and the unavailability of cash information from multiple departments negatively affects the A/P department's ability to report expected payment information to treasury in a timely manner.
- If streamlining of internal processes is not a priority for management, this impacts the effectiveness of A/P as well.
- Often, too much time is spent on processes such as matching invoices with purchase orders (POs) to identify payments that don't relate to any PO or user department, causing an approval delay for invoices.
- Sometimes defective goods and short supplies are paid for in advance, or an outage in supply occurs because of unintentional non-payment.

Disconnect Between Corporates and Vendors

- Most organisations pay vendors by advising their banks about payment dates and payment amounts to be made via wire transfers. Not many efforts are made by organisations or banks to analyse the incentives provided by vendors for early payments, charges for late payments or the cost of using cash for other investments.
- Multiple departments of the organisation may be sending data to the same vendor using multiple invoices, resulting in the loss of volume pricing benefits.

Banking Inefficiencies

The lack of offerings provided by partner banks can be a limitation to look into for improving the A/P process. To deal with these challenges, it is crucial that organisations take measures to strategically standardise their processes. From an A/P perspective, the focus areas could be:

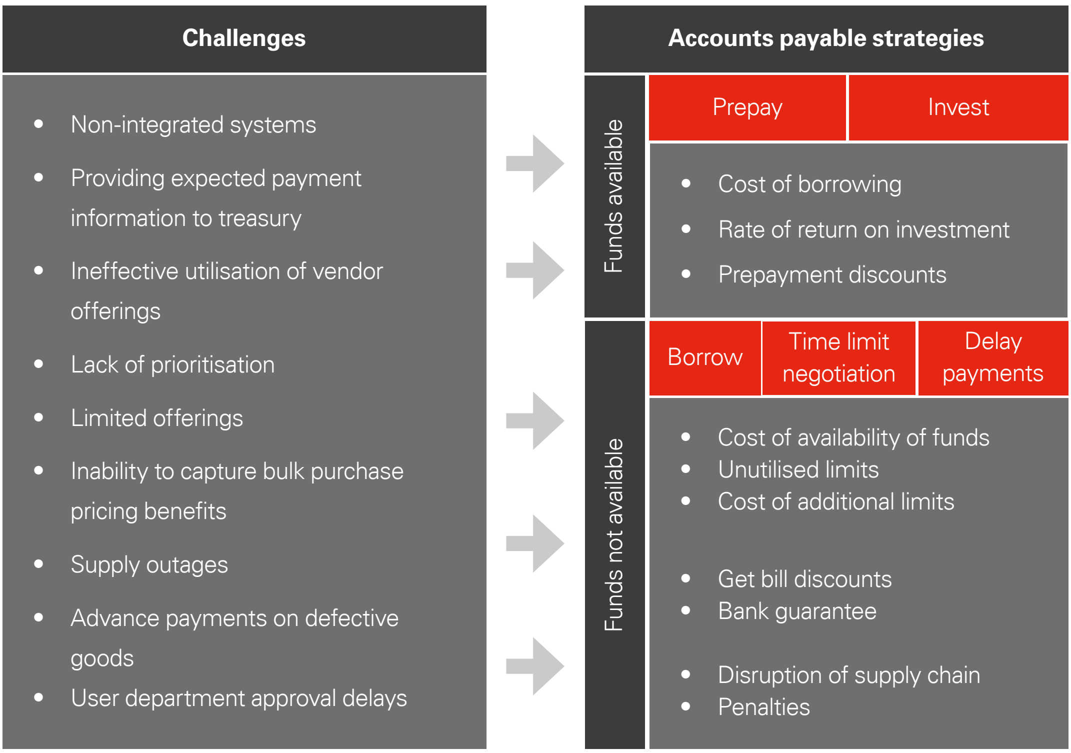
- Internal department alignment: Alignment of departments reporting to A/P so that expected payments or the pipeline created by them can be visible to A/P and treasury in real-time.
- Process optimisation and automation: Breaking down business processes into sub-processes for each department with all personnel involved to help identify time-consuming procedures. It could then be considered whether outsourcing is a viable option, such as opting for electronic invoice storage.
- Matrix-driven system: Developing a clear-cut view about the input and output of each department in terms of attributes could help to build suitable monitoring solutions, which might lead to the consideration of alternative payment options.

The Solution: A Strategic Approach

With the growing number of vendor options to choose from, corporates might be interested in various tools to manage their A/P process more smoothly. They could look to third-party vendors or to their partner banks to provide these services on top of existing offerings. To improve the A/P process, corporates might also look for services that facilitate decision-making or offer advice with regard to certain kinds of payments. The need for streamlining A/P functions varies from organisation to organisation. Some of the factors to be considered are:

- Sufficient cash for payments: A corporate may be in a situation where it has excess cash that can be used either to settle payables or to invest in the short term. The returns on short-term investment versus prepayment benefits would be a top consideration in this case.
- Insufficient cash for payments: If the corporate's cash flow is inadequate to settle payables, the alternative is to borrow to cover the shortfall or to delay payment, else incur a penalty, and even the risk of being blacklisted. Much will depend on considering the cost of funds, conducting a penalty analysis, and reviewing the long-term implications of delaying payments on the supply chain.
- Looking at receivables: Sometimes vendors' limited offerings can prevent corporates from benefiting from the most effective solutions. An alternative may be to increase early payment discounts for current A/R to encourage additional cash flow and bridge the gap.

Figure 1: Accounts Payable Management Strategies



Source: Infosys Limited

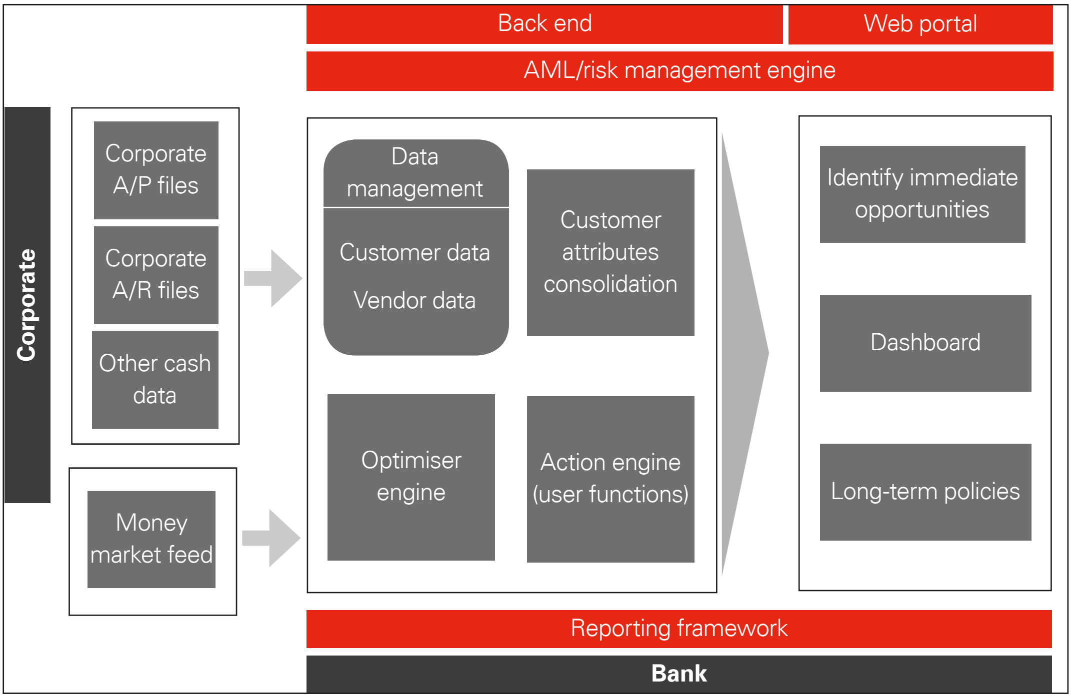
Figure 1 shows various options and recommended approaches that can be considered while deciding on a particular course of action. All the alternatives need to be examined to arrive at an optimal solution that will help maximise value and minimise cost for the corporate in its attempt to manage payables.

These offerings can be built by the organisation itself as in-house tools or they can be purchased from a third party. Another option is for banks to provide these services as a focused offering in a more sophisticated manner. One reason for this is that much of the information needed for optimising the management of payables (apart from information about the account itself) is easily available to banks. If organisations wish to use services based on their specific needs following a "use and pay" method, there is a strong possibility that they will be interested in receiving these services from a partner bank as part of their other existing offerings.

How Banks Can Help

Banks that are interested in providing such services to round out their core offerings can look at ways to develop these services so that they provide more value to their clients. Several offerings can be created within the A/P framework (see Figure 2) including:

Figure 2: Accounts Payable Management Framework



Source: Infosys Limited

Better Payment Terms from Vendors

A careful approach to managing payables includes getting better credit limits from vendors by involving the corporate's bank in offering non-borrowing limits such as bank guarantees or letters of credit (LCs).

These can be used to negotiate longer repayment tenors and larger limits with vendors. This focused activity will help to achieve better payment terms between the vender and the corporate during the LC renewal process.

Discounting Limits for Vendors

Banks can consider ways to offer discounting limits for organisations' vendors based on the creditworthiness of the organisation and its track record of prompt payments to vendors. This will encourage vendors to offer better terms to organisations that don't have cash flow problems because vendors can use the discounting facilities of organisations instead of their own banking limits. Banks can choose required corporate attributes to arrive at offer limits to vendors.

Analytical Tools for Organisations

Analytical tools such as financial cost/benefit calculators can be made available, which can calculate the trade-off between paying off payables on time versus prepaying to get discounts for early payments versus delaying payments and incurring penalties against the cost of borrowing funds to pay. These calculators can look at individual payments and take a portfolio view of payments over a specified period, and give a recommendation based on optimisation of an A/P portfolio. An individual view is more appropriate for one-off or infrequent larger payments, whereas the portfolio view would take care of a large number of smaller payments. A dashboard can monitor various payments due, changes in the money market, and alert the organisation to moneymaking opportunities or a reduction in the cost of funds.

Key Considerations

Organisations and banks should consider various inputs while deciding if A/P software packages provided by banks are justified by cost savings. With the changing regulatory environment, it may be worthwhile using these offerings on a trial basis, and revisiting the options based on long-term and short-term goals.

Organisations' Role

Organisations should take a holistic view of cash management and working capital management and consider A/P as an integral component in cost reduction. Additionally, willingness on the corporates' part to share A/P data with banks is required to make this initiative fruitful.

Banks' Role

The ability of banks to offer A/P services using secure channels and to keep customer information confidential are key considerations to selling these offerings. Banks can leverage their own risk management processes – anti-money laundering (AML) programs, for example – to secure client data, and subject them to the same level of scrutiny such as checking with AML blacklists to provide an added level of security.

Banks should consider a pre-packaged set of reports based on their own experiences in managing cash for multiple corporates. A bank can share best practices on A/P management with any organisation by making them available as part of the offerings. Based on data from several organisations, banks can provide useful comparative analyses of how an organisation is managing its A/P versus others in the industry. Banks can bring in their own high standards of security and control for the benefit of the corporate. By introducing such services, banks can increase their basket of offerings and strengthen their roles as a one-stop shop for the financial needs of corporates.

Conclusion

Today, most banks offer A/P solutions to their corporate clients in the form of a one-stop shop for making payments anywhere in the world. While this is a valuable service, it leaves little ground for differentiating a bank's cash management offerings from that of its competitors. A bank can distinguish itself if it increases the efficiency of the A/P process by providing services that enable organisations to better manage their A/P portfolios and maximise a defined value such as cost of borrowing or rate of return on investment.

The bank can co-create such a value-added service with an IT partner and use cloud computing to streamline time to market with minimal upfront investment. Corporates would benefit from more effective payables management and a reduction in overall working capital costs without the overhead of IT infrastructure investment. The IT vendor could leverage the co-created intellectual property (IP) to service other clients and share the IP revenue with the bank. Such a mutually beneficial partnership would create a win-win situation for all concerned.