

basware

# How to Improve Your Cash Management and Forecasting, by Automating Purchase to Pay

a special report for CFOs



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## Executive Summary

This white paper asks the question: How can CFOs improve their cash management and forecasting?

Poor cash management and forecasting cost money and multiply risk. They depress shareholder confidence and cut market capitalization. Yet most enterprises do a poor job of them, by their own admission.

The three main causes of poor cash flow forecasting are paper, people and processing. Paper still swamps most businesses, which makes extracting data difficult. People too often work in separate silos with no overview. And most enterprises lack the automation that CFOs need to optimize their cash management and pull together precise and far-seeing forecasts.

In particular, invoice processing cries out for automation. Without gaining better visibility into AP requirements, cash forecasting will always be fuzzy. This paper provides benchmarks for two key AP metrics to help develop a baseline for measuring improvements, and lists the many benefits of automating AP.

And it includes three success stories from companies that gained major savings by automating their paper-based invoice processes. CFOs need to push back the veil of darkness over AP to uncover hidden treasure and light the way to far-seeing cash forecasting.



**CFOs need to push back the veil of darkness over AP to uncover hidden treasure and light the way to far-seeing forecasts.**

## A Critical Challenge for CFOs

- How much cash do we have on hand?
- How much cash is coming in?
- How much cash is going out, and when is it due?

These simple questions are repeated every day, every week and every month in every enterprise. These questions define cash management and forecasting. But not many enterprises do a good job of answering them.

In fact, research from KPMG International shows that “cash flow forecasting remains a key weakness for most organizations” with 72% admitting that they missed their forecasts for the past year. Almost one in four were off by 20% or more.<sup>1</sup>

The fallout can be grim. Poor cash management and forecasting lead to overall less efficient operations, which can take many forms:

- inadequate capacity planning
- unbalanced supply chain (too much capital tied up in inventory)
- wasteful procurement (rush purchases and extra delivery fees)
- less agility to deal with sudden events
- missed opportunities
- loss of investor confidence.



Without strong cash management, a business is wasting money. Without good forecasts, it is fumbling in the dark.

Every item on this list costs money and multiplies risk.

Enterprises that do poorly on these critical functions are punished in the marketplace. In another KPMG study, executives estimated that their shortcomings in these areas depressed their share prices by 6%.<sup>2</sup>

Investors sense that without strong cash management, the business is wasting money; without good forecasts, it is fumbling in the dark.

## The Long and the Short of It

Why aren't companies doing better at cash management and forecasting? There's a short answer, and a longer answer to this.

The short answer is this: There is often a disconnect between Procurement and Finance, between the people creating cash obligations – making purchases and issuing POs – and the people accounting for them when the invoices flow in. In between lies a vast land of shadows, where **most CFOs have no visibility into the enterprise's obligations... yet are still expected to forecast them.**

## Paper, People and Processing

The longer answer to the riddle of why enterprises don't do better at cash forecasting has three parts: paper, people and processing. And all three problems directly afflict the AP function.

### Paper means slow, incomplete and unreliable data

Almost 35 years after the arrival of the PC, businesses are still swamped with paper. For example, Aberdeen Group reports that the average enterprise is still handling “roughly the same level of paper invoices (83%) today as it did four years ago.”<sup>3</sup> Nothing has changed in the interim.

As you know, it's difficult and time-consuming to extract the data you need for cash management and forecasting from a flurry of invoices. Information trapped on paper is not accessible. It's hidden in the shadows.

The shadow first falls when a CFO cannot see into the order base of POs issued for items not yet received or invoiced. And the shadow deepens over the indirect spend: all the items and services purchased with no PO at all.

“Across all companies, on average only 50% of purchasing processes are automated and just 42% of indirect spend is captured by PO systems,” concluded a recent study of 550 enterprises by two business schools. “This means that more than half of spend is ‘in the wild’ not measured or managed in any real sense.”<sup>4</sup>

Not only is data missing, but what's there can't be trusted. For example, in a recent KPMG study, almost half the finance executives who were polled admitted they consider the data they use “merely adequate or worse.”<sup>5</sup>

How would you rate YOUR financial data? Is it as timely, complete and accurate as you would like? Or are there shadows blocking your visibility into some critical areas?



The British poet and Nobel Prize winner T. S. Eliot once wrote, “Between the idea And the reality Between the motion And the act Falls the Shadow.”

With apologies, we could revise this to, “Between the purchase and the payment, between the PO and the invoice, falls the shadow.”

Eliot would understand. After all, he worked for years for a bank in London.

## People work in separate silos

*With close to 2,000 trucks on the road, FFE Transportation Services has to keep things moving.*

*To streamline handling 120,000 non-PO invoices a year, the company automated its AP processing with Basware.*

*In the first year, FFE reduced AP labor by 50% and achieved an ROI of 130% for a net gain.*

Any forecast relies on deep insights into projected cash outlay and expected cash income. But in most enterprises, Procurement, Finance and Treasury operate in separate silos, with little shared vision of how to work together to benefit the enterprise, or much motivation to develop one.

If Finance and Procurement do not work together, this obscures the ability of Treasury to see the cash position of the enterprise.

“There is an **evident need for the Finance and Procurement functions to collaborate more effectively** to improve the quality and availability of this [spend] data,” concluded the business school study mentioned above.<sup>6</sup>

## Processing relies on antiquated systems

Then there's the software CFOs use. Sadly, much of it was designed in the 1980s, long before today's global, fast-moving business environment came into being. **These tools are no longer up to the task.**

- **Spreadsheets:** Using spreadsheets is slow, labor-intensive and prone to errors. The European Spreadsheet Risks Interest Group has even given up collecting “horror stories,” saying they just can't keep up.<sup>7</sup>
- **Accounting systems:** Like a rear-view mirror, these systems show where you've been, not where you're going. Data from an accounting system is likely to be too little, too late to help much with cash management and forecasting.
- **ERP systems:** ERP systems were designed for production control, not cash management. ERP vendors may tell you they have a wonderful new module to take care of all that. But do you really want to “bet the company” on yet another ERP project that never seems to end?

This problem is compounded in a global enterprise with various divisions running different brands, versions and releases of ERP. Rolling up all the data from incompatible ERP systems into one consolidated report can be a monumental task. Never mind asking for help to create a forward-looking cash forecast.

- **Content management systems:** Almost by accident, CMS vendors realized their systems can scan invoices too. But looking at an image of an invoice is not much better than handling it on paper. Without intelligent business rules to extract meaningful data from these images, CMS suffers the same problem: too much effort to generate reports.

**Spreadsheets, accounting, ERP and content management: All these systems require tedious efforts to generate meaningful reports**

None of these older technologies can free the invoice-processing workflow from paper-burden. None can provide a unified view above and beyond the silos where Procurement and Finance traditionally sit. None can bring a vast amount of spending out of the shadows.

And none can provide the timely, accurate and complete visibility that CFOs need to make informed decisions about cash management and create precise, far-seeing cash forecasts.

## Is Automation the Answer?

Many analysts suggest that automation can provide the remedies to all three of these problems.

“AP operations continue to present one of the most compelling opportunities for improvement through process automation within the typical enterprise,” says Aberdeen.<sup>8</sup>

If the invoice-processing workflow were effectively automated, this would shine a bright spotlight on all the spending activities that were formerly hidden by shadows.

An automated workflow imposed by the CFO would give management a higher view, beyond the traditional silos of Finance and Procurement. And it would pull people from both groups to sit at the same table and work together for the common good of the enterprise.

Best of all, the CFO would now benefit from a best-of-breed automated solution designed specifically to tackle the problems he needs to solve: more flexible cash management and more accurate cash forecasting.

And this isn't just theory.

Listen to how Aberdeen summed up the results from seven companies that each automated their AP processes with different vendors:

“In all cases, automation eliminated the paper chase and allowed AP resources to focus on more proactive activities like resolving discrepancies... Better data allows AP to review each dollar spent, closely manage supplier relationships, monitor cash flow, and maximize every discount available.”<sup>9</sup>

*Boston-based investment firm Loomis, Sayles & Company has \$124 billion under management; so they know about money.*

*By 2005, the firm wanted lower costs and better visibility into AP.*

*Automating the invoice flow with Basware freed up 40% of the AP staff for more strategic duties, and yielded an ROI in 14 months.*

## CFOs at the Crossroads

As shown in Figure 1, today's CFOs stand at a crossroads. The choice you make will determine the effectiveness of your cash management, and the accuracy of your cash flow forecasts.

**Manual processing** is shown by the red dotted line. Notice what a short span this affords until you fall into the shadows. Manual processes demand tremendous effort at end-of-month and end-of-quarter to generate reports,

and these reports cover only perhaps 30% of your actual cash obligations and receivables. With manual processing, cash forecasting will remain short-term and imprecise.

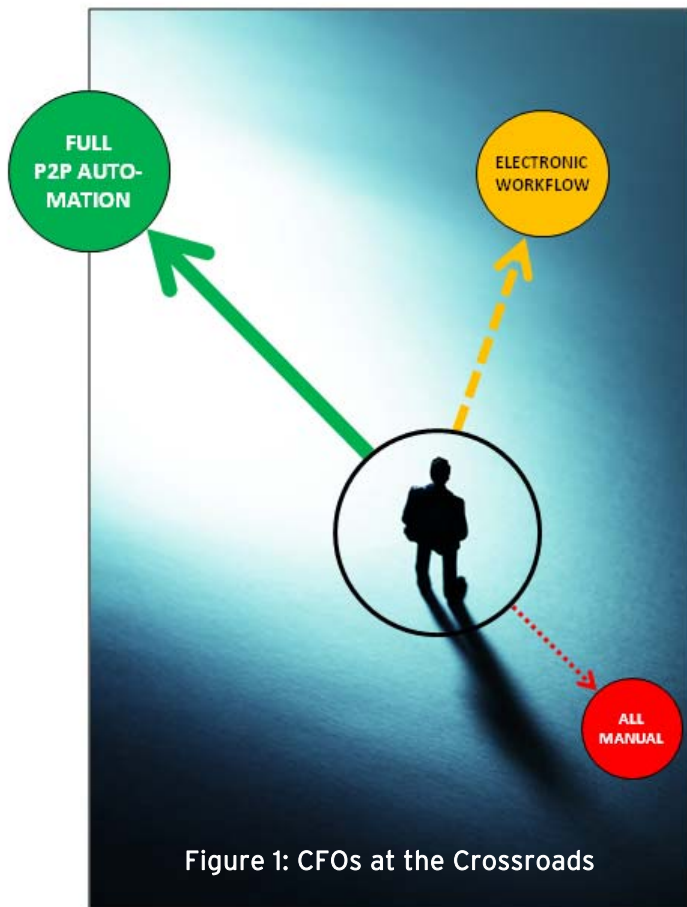
**Electronic workflow** is shown by the orange line. With an electronic workflow, reports are easier to generate and more reliable, covering perhaps 60% of your cash requirements. But some areas remain in the shadows, such as your indirect spend, which Gartner says can total as much as 40% of your total revenues.<sup>10</sup> Even with an electronic workflow, at a certain point your visibility is once again blocked by shadows.

**Fully automated purchase-to-pay (P2P) processing** is shown by the green line. With full automation, you have complete visibility into more than 90% of your cash commitments. You can see a range of detailed reports at any time, providing up-to-the-second coverage of your cash requirements in real-time. Your visibility

is extended dramatically, and your cash forecasts reach a precision you have never seen. All in all, the difference is like night and day.

### Which path will you choose?

No matter which path you choose for your enterprise, a useful first step is to benchmark your current AP performance as a baseline for measuring any future improvements.



## Benchmarking Your AP Performance

DPO is a classic metric that every CFO keeps an eye on. But this tends to indicate more of a cash management strategy (or a hopeless backlog of paperwork) than the effectiveness of the AP workflow.

Ongoing research has confirmed that the two most meaningful metrics for measuring AP performance are time and money.

There are many ways to state this performance: average invoice cycle time, average cost per invoice processed, number of invoices handled per FTE (cost-effectiveness) and even % returned for errors (quality).

The most useful metrics for benchmarking are likely invoice cycle time and average cost. Industry norms exist for each. For example, to follow up their surveys of 1,000+ AP teams during the previous 16 months, Aberdeen Group evaluated 150+ enterprises across many different industries in the fall of 2009 to develop the metrics shown in Tables 1 and 2.<sup>11</sup>

Table 1 refers to the time required to process a single invoice from receipt until payment is scheduled. Fill in your own metric in the blank column to see how your enterprise compares.

**Notice that the laggards take almost 30 days to schedule a payment.** That gives these operations little scope to plan for early-payment discounts, and no way to avoid late-payment penalties. No CFO can implement an effective payment strategy with so little time to maneuver.

**Best-in-class companies handle their invoices in only 3.5 days,** giving them ample opportunity to plan and schedule payments, take advantage of early-payment discounts and even hedge between various currencies, if desired.

|                                   | TIME<br>to process<br>an invoice | YOUR<br>CYCLE TIME |
|-----------------------------------|----------------------------------|--------------------|
| <b>Best-in-Class:<br/>Top 20%</b> | 3.5 days                         |                    |
| <b>Average:<br/>Middle 50%</b>    | 16 days                          |                    |
| <b>Laggards:<br/>Bottom 30%</b>   | 27 days                          |                    |

Source: Aberdeen Group, December 2009

**Table 1: Typical Invoice Cycle Times**



|                           | COST<br>to process<br>one invoice | YOUR<br>COST |
|---------------------------|-----------------------------------|--------------|
| Best-in-Class:<br>Top 20% | \$3.53                            |              |
| Average:<br>Middle 50%    | \$11.19                           |              |
| Laggards:<br>Bottom 30%   | \$35.56                           |              |

Source: Aberdeen Group, December 2009

**Table 2: Typical Invoice Processing Costs**

Table 2 refers to the cost required to process a single invoice from receipt through settlement. Fill in your own metric in the blank column and see how your enterprise compares.

Notice that the laggards spend more than 10 times per invoice than the best-in-class. On any volume of invoice flow, those savings are enough to generate a strong ROI on an automation project.

If you already match the best-in-class, congratulations! If not, it may be time to streamline your invoice processing. The benefits will be profound.

## The Benefits of Automating AP

- Reduce cycle time for each invoice (82.7% faster for best-in-class)
- Cut processing cost for each invoice (83% lower for best-in-class)
- Boost accuracy (51% fewer exceptions for best-in-class)
- Save labor on paper shuffling (estimated 25% to 40% reduction)
- Choose the best time for paying your invoices:
  - Take early-payment discounts (estimated up to 500% increase)<sup>12</sup>
  - Reduce late-payment penalties (50.5% fewer for best-in-class)<sup>13</sup>
  - Gain control over currency flows
- Impose stronger, more consistent cash management strategies
- With your on-time payment record, negotiate better with suppliers
- Gain visibility into more than 90% of the enterprise's cash outflows (excluding personnel costs)
- Generate more accurate, far-seeing cash forecasts
- Contribute directly to a better bottom line.

As you can see, the short-term benefits trickle up.

“Managers should recognize that performance goals of invoice processing are broader than cost per invoice and cycle time per invoice. Solutions that automate the invoice receipt process can also improve the performance of other enterprise functions... that directly affect the bottom line,” says Aberdeen.<sup>14</sup>

With better cash management and forecasting come a host of enterprise-level benefits, such as more agility to deal with sudden events and take advantage of new opportunities, more capacity to manage risk, increased shareholder confidence – and very likely a stronger share price.

Isn't that what every CFO wants: to make a real difference in your enterprise? With such a compelling benefits to be gained – and such dire consequences of inaction – isn't it high time to start looking into streamlining and automating your AP?

## What to Look for in a Solution

As you begin to evaluate vendors who can help you automate your AP, here are some criteria they should be able to meet.

- Best-of-breed solution, not an ERP bolt-on
- Out-of-the-box reports that support cash management and forecasting
- All reports available on-demand in real-time
- Automatic export to Excel and import into cash management system
- Projected ROI within 12 months
- Proven track record in your industry
- Vast installed base of satisfied clients
- Solid financial performance for a sustainable future
- Global reach to serve any region of a multi-national enterprise.



Imagine a report that shows all outstanding POs and invoices, sorted by due dates and/or currencies and/or any timeline as far into the future as you'd like

## Conclusions

Cash management and forecasting is a critical business function, yet most enterprises admit they don't do it well. This can have dire consequences for the enterprise.

The key causes are acknowledged to be paper-bound processes, lack of shared vision and communication between Finance and Procurement and antiquated software. All this adds up to very poor visibility into AP processes and commitments.

*Finnair, one of the world's oldest airlines, used to spend €40 (\$53.65) each to handle 115,000 paper invoices a year.*

*With Basware's help, the airline moved to a paperless process, from invoice receipt to approval.*

*This cut invoice-processing costs by 50% for an annual saving of more than €1 million (\$1.34 million).*

In many enterprises, this lack of visibility into AP throws a deep shadow over future cash obligations. It confounds any attempts to improve cash management and it limits the amount of meaningful data available for forecasting.

Meanwhile, cash is routinely frittered away on paper-shuffling, missed early-payment discounts, and late-payment penalties.

All this makes invoice processing a promising area for automation. **The real-life results of FFE Transportation Services, Finnair and Loomis, Sayles & Company show the tremendous cost savings and rapid ROI that a project with the right vendor can achieve.**

When the veil of shadows is pushed back from AP processes through proper automation, more timely, complete and accurate data becomes available to support both short-term cash management strategies and longer-term cash forecasting.

**To see more examples of enterprises that have improved their cash management and forecasting by automating their AP functions, please visit [www.basware.com/resources](http://www.basware.com/resources).**

Or contact our experts directly by e-mailing [info@basware.com](mailto:info@basware.com)



## About Basware

Basware is the global leader in purchase-to-pay solutions with more than 1,500 customers and 1,000,000 users in over 50 countries around the world.

With Basware, organizations can reduce the cost of buying and paying for goods and services and gain visibility and control of their entire spending process by automating manual processes, from sourcing, contract management and purchasing to supplier collaboration and invoice automation.

Basware solutions and services enable substantial cost reductions across businesses and deliver value by providing compliance and control, as well as fast return on investment. The solutions are distributed and implemented, either on site or as a service, in Europe, the US, and Asia-Pacific through an extensive network of Basware offices and business partners.

For more information, visit [www.basware.com](http://www.basware.com)

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