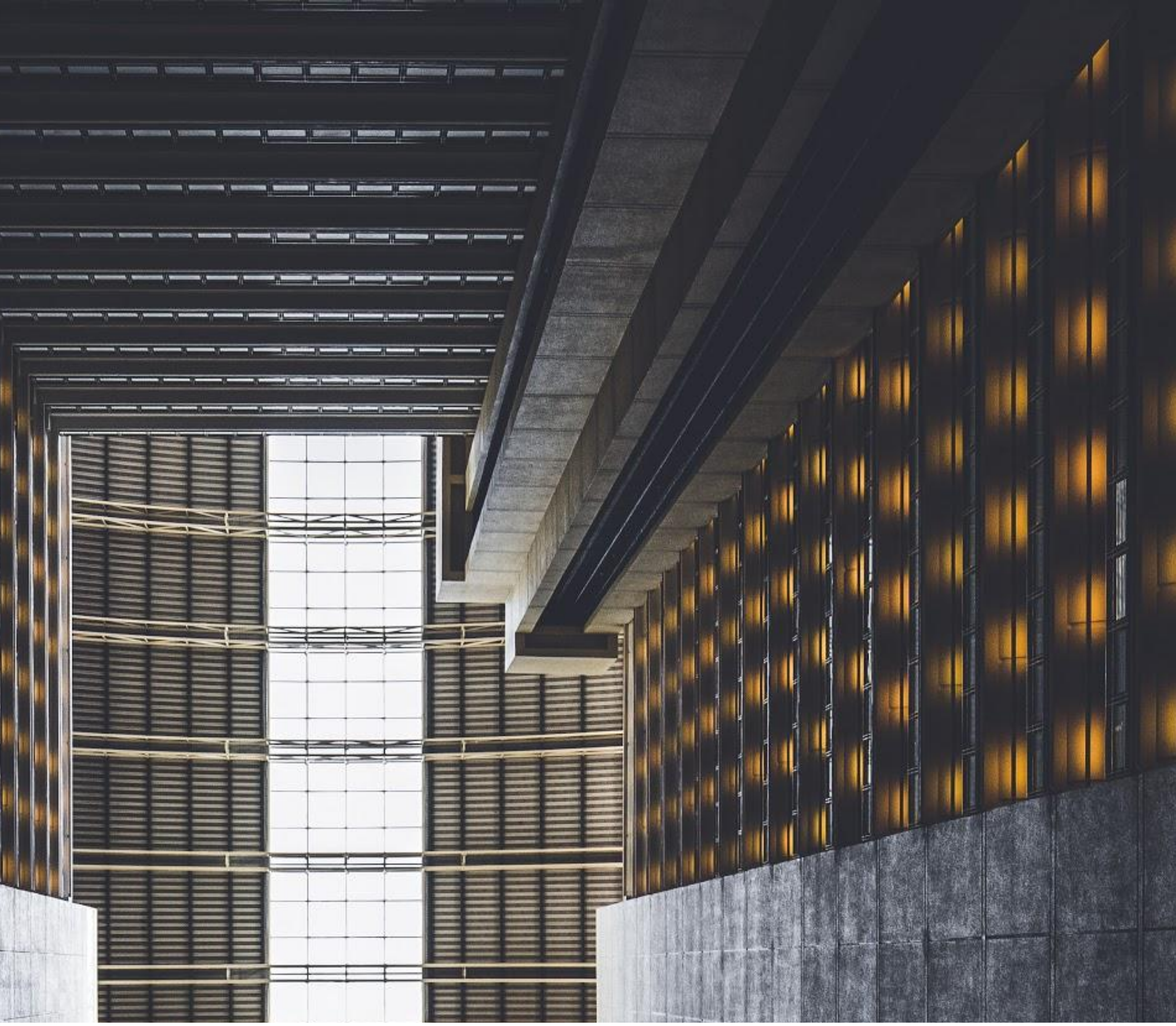


# Effective liquidity management techniques in uncertain times

June 2020

pwc

The pace of change in the business environment is having an unprecedented impact on our economy and business community. Globally and locally, central banks and governments are providing stimulus packages through all-time low interest rate settings, cash to support the financial system and huge fiscal responses. The challenge is to pre-emptively offset the negative economic impact from the supply and demand disruptions and enable the economy to bounce back more effectively as conditions normalise.

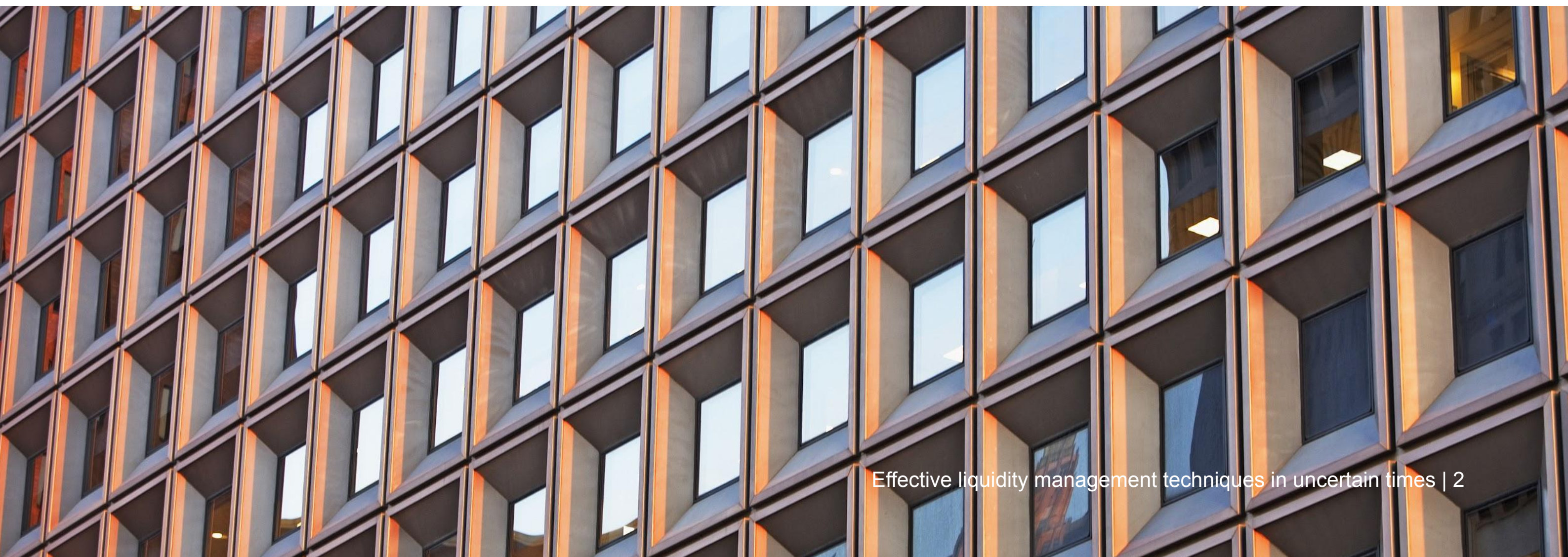
**Here are some tips that can be applied to businesses as they chart their way through this uncertain economic and business environment.**

## 1. Have a robust business cash flow forecast

- Understand your current cash position and cash flow forecasts. It is vital to make informed decisions. Cash is king so it is appropriate to keep cash close.
- Scenario test cash flow forecasts with appropriately conservative assumptions around revenue, costs and the cash conversion cycle. Be as realistic as possible with assumptions in these uncertain times. Have a ‘best case’ and ‘worst case’ scenario and include all the costs of each scenario.
- Start with a detailed rolling (weekly) 13-week cash flow forecast and then expand the term out to at least twelve months.

  Closely analyse each line item, test and challenge the forecast accuracy. Note any judgements and uncertainties within the assumptions. Compare actual outcomes to forecast assumptions. Review daily and change/adapt over time.

  Think through what the business will look like in six to twelve months’ time as it transitions from its current state, and when the underlying market demand picks up. This includes financial considerations and other resources that the business will need to be able to meet the expected increase in demand.
- Ensure strong visibility of your accounts payable and accounts receivable ledgers. Communicate with your procurement and sales teams to ensure that you’re getting better information during this period.
- Success comes from the timeliness, accuracy and ownership of information inputs from across the whole organisation. Given these uncertain times, how have the directors and management satisfied themselves as to the reliability of your cash flow forecasts, and the reasonableness of the actions required to maintain cash and access to liquidity?



## 2. Identify cash and liquidity requirements

An accurate cash flow forecast is vital and provides confidence in making key cash and liquidity management decisions.

How do you respond to periodic cash flow deficits and funding gaps? What is the impact on bank financial covenants? Focus on earnings-based ratios such as interest coverage and Debt/EBITDA measures and stress test these against your worst case forecast scenarios.

Identify which cash flow levers you can use within the business to preserve cash, release cash and defer cash costs. Efficiencies that can be gained will minimise the use of existing committed debt facilities and reduce the need for new facilities.

What techniques can be employed around your variable cost base, capital expenditure programme, and working capital management systems? Importantly, do you have adequate committed bank facilities in both amount and term? Amidst the uncertainties, seek to ensure that current bank facilities have a minimum term beyond 18 months that can provide sufficient headroom for worst case scenarios contained within your cash flow modelling.

Stakeholders want to know how mature an organisation is in understanding the additional committed liquidity needs and the nature of discussions with bank debt providers. How committed is your access to these facilities in support of your liquidity needs? Uncommitted or on-demand facilities such as overdrafts do not provide certainty of access to cash and could be withdrawn by your bank at any stage; a heightened risk in these uncertain times.

## 3. Maintain and strengthen bank relationships

Banks will be encouraged if they know that forward liquidity, cash flow positioning and forecasting is being proactively managed, along with any potential impact upon financial covenants.

It is best to approach your bank when you are in a strong position and can plan for an adverse scenario, rather than approaching your bank providers at a later stage. We encourage you to have early conversations with your bank regarding risks to your cash position and any potential covenant breaches, in anticipation of support from banks if any breaches were to occur. They will want to know the amount and term of any additional committed liquidity facilities. Be open and honest with banking providers; surprising lenders with covenant breaches that could have been anticipated will not be viewed favourably.

Recognise that the bank's credit allocation to your business is finite. Therefore use this credit allocation wisely, promoting access to liquidity above other forms of treasury needs. Clearly understand the total amount of credit allocation available, how it is currently utilised and how remaining capacity can best be applied.

## 4. Practical tips that could be applied to enhance cash and liquidity

**Below are mechanisms that could be applied to enhance the cash and liquidity position. Any decision would be considered against a business' unique features and be consistent with its short to medium term strategy. Other matters such as the accounting and taxation impact would need to be clearly understood. We recommend consulting with your advisors before implementing any changes**

### Borrowing

- There may be the potential to consider capitalising interest for a time on certain debt obligations and structures.
- Similarly, there is potential within amortising loans for a temporary period of interest-only servicing, with principal repayment obligations deferred to future periods.
- We are also mindful of keeping additional debt being raised for liquidity purposes in shorter terms but with these terms also being balanced (i.e. not too short). The consideration is the need for a temporary period of potentially disruptive liquidity, instead of a permanent need to increase banking facility headroom.
- Formalise your bank discussions on additional liquidity requirements with executed documents and any financial covenant waivers or modifications.

### Treasury investments

- In our view, bank term deposit investments should be invested at call or for a term no greater than 30 days, to maintain liquidity during uncertain times.

### Hedging portfolio

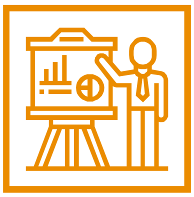
- Within policy parameters, monetise (cash in) any existing foreign currency contracts with a favourable market valuation. These contracts were put in place to manage an adverse movement in the foreign exchange rate, and that movement may have happened.
- Interest rate swap restructures. A number of different restructures could be employed that defer interest costs to another time period. These techniques can be useful when considering interest coverage ratios or reducing interest payment cash flows. Interest costs are better matched to future periods when earnings are expected to improve. Existing swaps can be cancelled and restarted at a future date or swap contract terms can be extended. Both strategies could relieve near term cash use and interest cost amounts.
- Both foreign currency and interest rate strategies need to be transacted with the existing bank counterparty with the assumption that there is credit appetite and capacity to allow strategies to be implemented. Use this credit allocation wisely.

## Other techniques

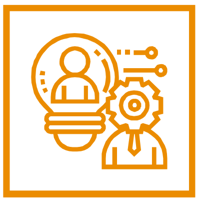
- **Reduction in capacity** - These are tough decisions but may be needed to ensure sustainability of the business. Options like “4 Day” work weeks are being used to keep your team employed, reducing excess capacity and associated costs.
- **Suspension or deferral of discretionary capital and operational expenditure** - As this expenditure can be discretionary for some projects, there is an opportunity to reset and restart projects at a later date to provide some near term cash and debt funding relief.
- **Suspension or deferral of dividends and other shareholder payments (interest and principal)** - Completed in liaison with shareholders and relevant stakeholders (i.e. bank) in which the immediate underlying credit profile and liquidity position can be improved through non-payment or deferral.
- **Utilisation of tax credits** - Application can be made to utilise tax credits against the instalment payments or balance of tax payable due in the current year. This can help to reduce the cash outflow to the Inland Revenue Board (IRB) or the Royal Malaysian Customs Department (RMCD) in meeting on-going tax obligations.
- **Application of refunds** - Application can be made to the IRB/ RMCD to expedite the refunds of tax credits. This will improve the cash flow position of companies.
- **Deferment of tax instalment payments** - Based on the incentives introduced by the government, companies are allowed to revise their tax estimates in the 3rd instalment month, provided that the instalment falls within the Year 2020. This can help companies to manage their corporate tax payments and redirect funds to critical areas of the business. Companies in tourism related businesses are allowed to defer the tax instalments up to a maximum of 6 months, from April 2020 to September 2020.
- **Utilisation of eligible tax incentives and tax exemptions** - These include special tax deductions, accelerated capital allowance, tax and duty exemptions as stipulated by the tax authorities.

## Summary

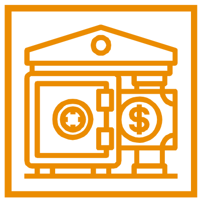
**In summary our key points are:**



Providing a realistic position of the business and cash flow forecasts is the key to success.



Be fast and agile at making decisions but keep the medium term in mind. Test all decisions to ensure they support both the short and medium term objectives of the business and reduce the potential regret factor. Decisions need to be supportive of the business as economic conditions improve.



Bank credit allocation is finite, use it wisely for liquidity and debt management. Proactively keep your bank relationship manager informed as they don’t like surprises.

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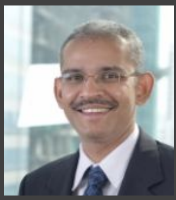

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