Invest in Africa - Investor Readiness Training

Financial Management Training

July 2021

EY
Building a better working world

SRC
Smart Regional Consultants

Welcome!

Introductory exercise

Type in the chat box your:

- Name
- Name of your company
- Sector in which your company is in
- *What is the biggest role finance plays in your organisation?*

Given the governance training, have you changed anything in your business: Go to **www.menti.com** and use the code 4037 8937

Today's Agenda

		Time
01	**Introductions**	➢ 9.00 am - 9.20 a.m.
02	**First Session** ➢ Introduction to Financial Management ➢ Financial Policy ➢ Financial Management Systems ➢ Cash flow Management	➢ 9:20 a.m. - 10.20 a.m. 10 mins break
02	**Second Session** ➢ Working Capital Management ➢ Financial Budgeting ➢ Financial Reporting ➢ Financial Analysis	➢ 10.30 a.m. - 11.45 a.m. Questions

Polling Questions - Go to **www.menti.com** and use the code 60362793

- Does the organisation have written policies on processing transactions and reporting on financial outcomes?
- Is the operating budget prepared annually?

What you told us

65% Believe their financial policies and procedures don't reflect current practices & no training is provided on the same

41% Do not clearly indicate anticipated costs and sources of income in their budget

70% Do not have a procurement manual hence lacking any documented procedures for preventing fraud

46% Do not conduct audits annually

76% Have their financial transactions supported by documentation

69% Lack approved tools for monitoring the annual budget

49% Lack a process for managing donor financial reporting requirements

49% Do not record their fixed assets in a register or management system

1

Introduction to Financial Management

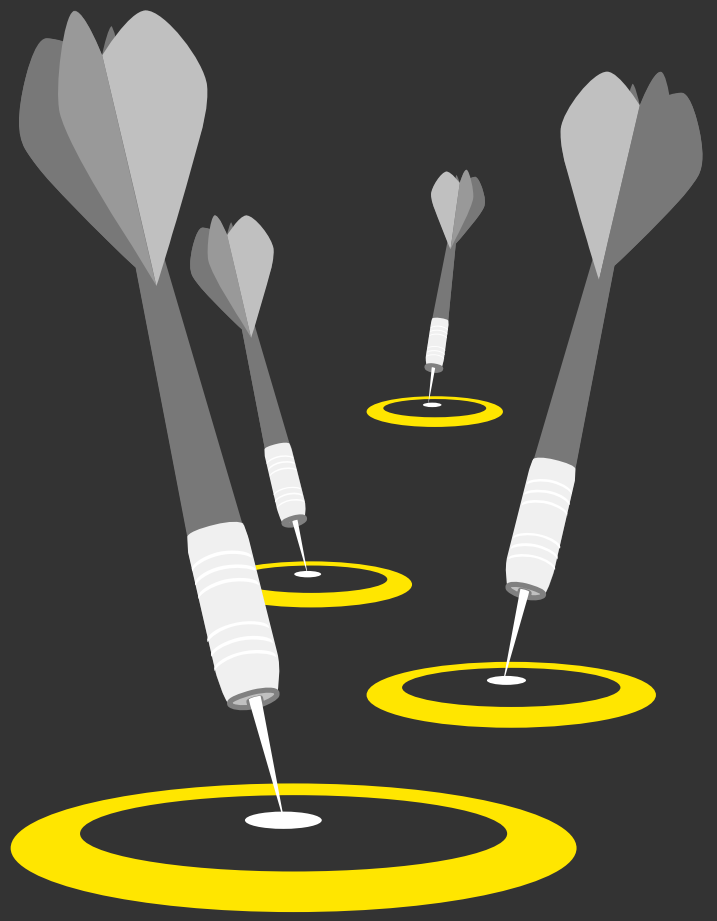
Importance of Financial Management

Helps a business owner know if they are making a profit – **Profit Maximization**

Enables planning for business growth, for diversification of product lines, or for reaching new markets

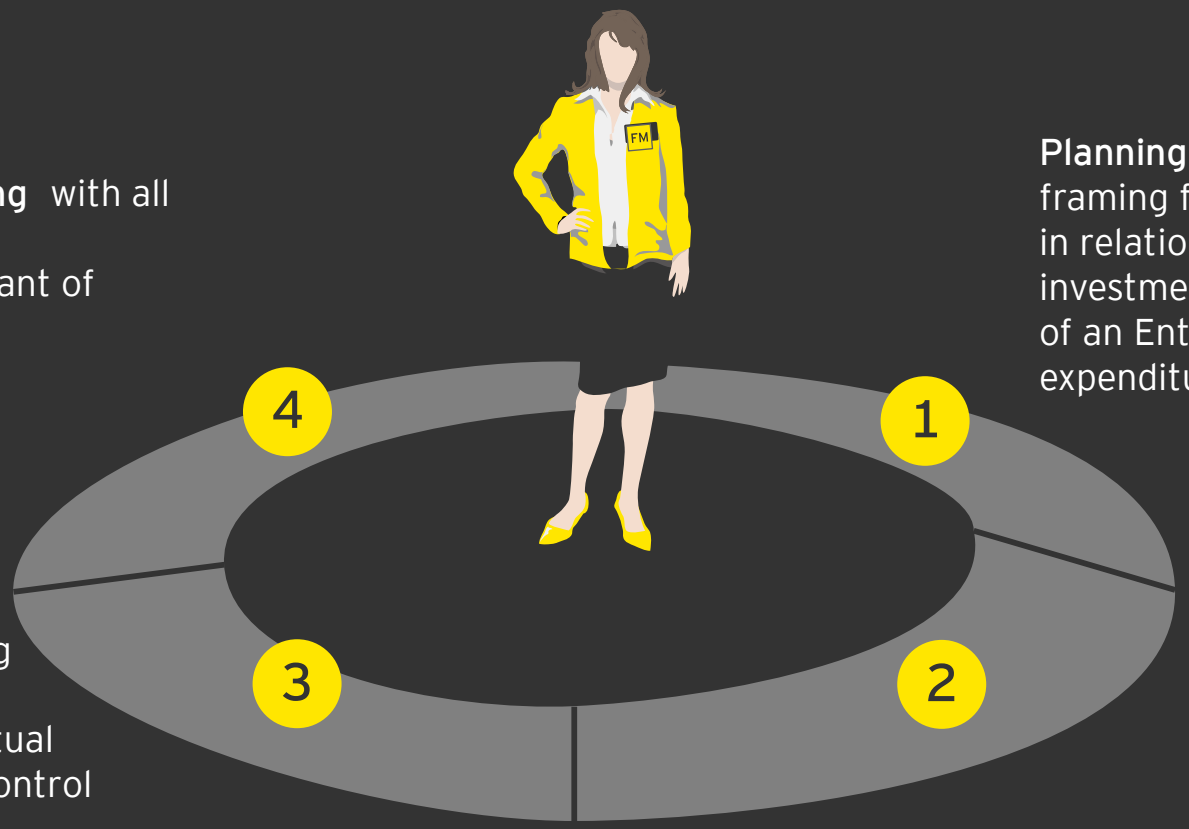
Helps a business owner decide what they can afford e.g. inventory purchases, employees, and equipment.

Helps in acquiring financing (Equity, loans, or grants)



Responsibilities of A Modern Financial Manager

Negotiating and coordinating with all other department so that no department suffers for want of funds.



Planning - Involves the process of framing financial policies in relation to procurement and investment and administration of funds of an Enterprise including capital expenditure and distribution of profit

Controlling – Involves setting financial standards of performance, comparing actual with standards to exercise control on differences, and applying techniques of budgetary control through a system of collecting and analysing information.

Organising- Involves creating and monitoring proper organisational structure of finance looking to the needs of organisation.

2

Financial Policy

Definition and characteristics of a good Financial Policy

A financial policy clarifies the roles, authority, and responsibilities for essential financial management activities and decisions

Written in clear and plain language and easy to comprehend

Adjustable and be amended to fit organisational cultural change

Linked to the business strategy and has clear objective

Collaborative approach is undertaken during development stages

What are the contents of a Financial Policy?

Roles and Responsibilities

- Preparation of annual operational plans
- Budget approvals
- Development of controls
- Grants and reserves
- How to handle conflict of interests.

Expenditure control

- Various responsibilities of employees
- Tender estimates
- Approvals required when undertaking capital expenditure
- The purchase orders
- The mandates of associated banks and credit cards
- How handle petty cash

Delegation of authority

- Delegated authority must match responsibility
- Job descriptions and duties be clearly written down and communicated to all staff in different cadres
- Clear authority boundaries and repercussions of noncompliance be communicated as well
- Key financial controls such as clear bank account signatories and reconciliation

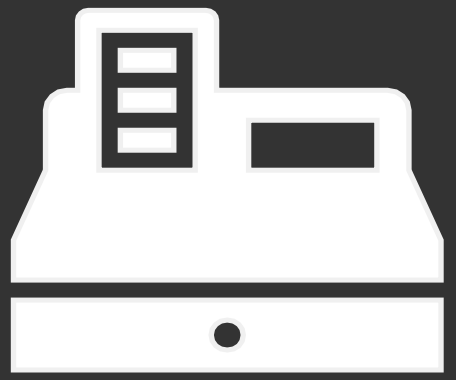
3

Financial Management Systems

What you told us

Do you record your transactions using either a manual or an electronic system?

OR



65.5%

34.5%

Benefits of financial management systems

A financial management system (FMS) is the software and processes an organisation uses to manage assets, income and expenses, with the objectives of maximising profits and ensuring efficiency

1. Eliminates accounting errors and minimises record-keeping redundancy
2. Ensures compliance with tax and accounting regulations
3. Supports budget preparation and making of strategic decisions
4. Supports timely financial reporting
5. Ensures connection, accumulation and processing of data
6. Enhances internal control in an organisation

Types of financial systems

Creating a specific system tailored for the company's needs is what sets these systems apart from others. A small business will not have the same needs as a much larger organisation in terms of financial management

Small business financial systems contain:

- General ledger accounting applications

Large businesses financial systems contain:

- General ledger accounting applications
- Budgeting
- Cash and bank management
- Debt obligations management
- Assets and liability management
- Accounts receivable
- Accounts payable
- Payroll
- Procurement and purchasing
- Revenue management
- Audit trails

Emerging trends in Finance

Data Certification

Traditionally, poor data quality, limited communication and attribute gaps (fit for use) from data providers to the enterprise cause multiple data validations, reconciliations and reduced confidence in reported numbers (garbage in / garbage out).

Now, companies must validate, certify and process expanded, more granular data requirements

Move to Cloud

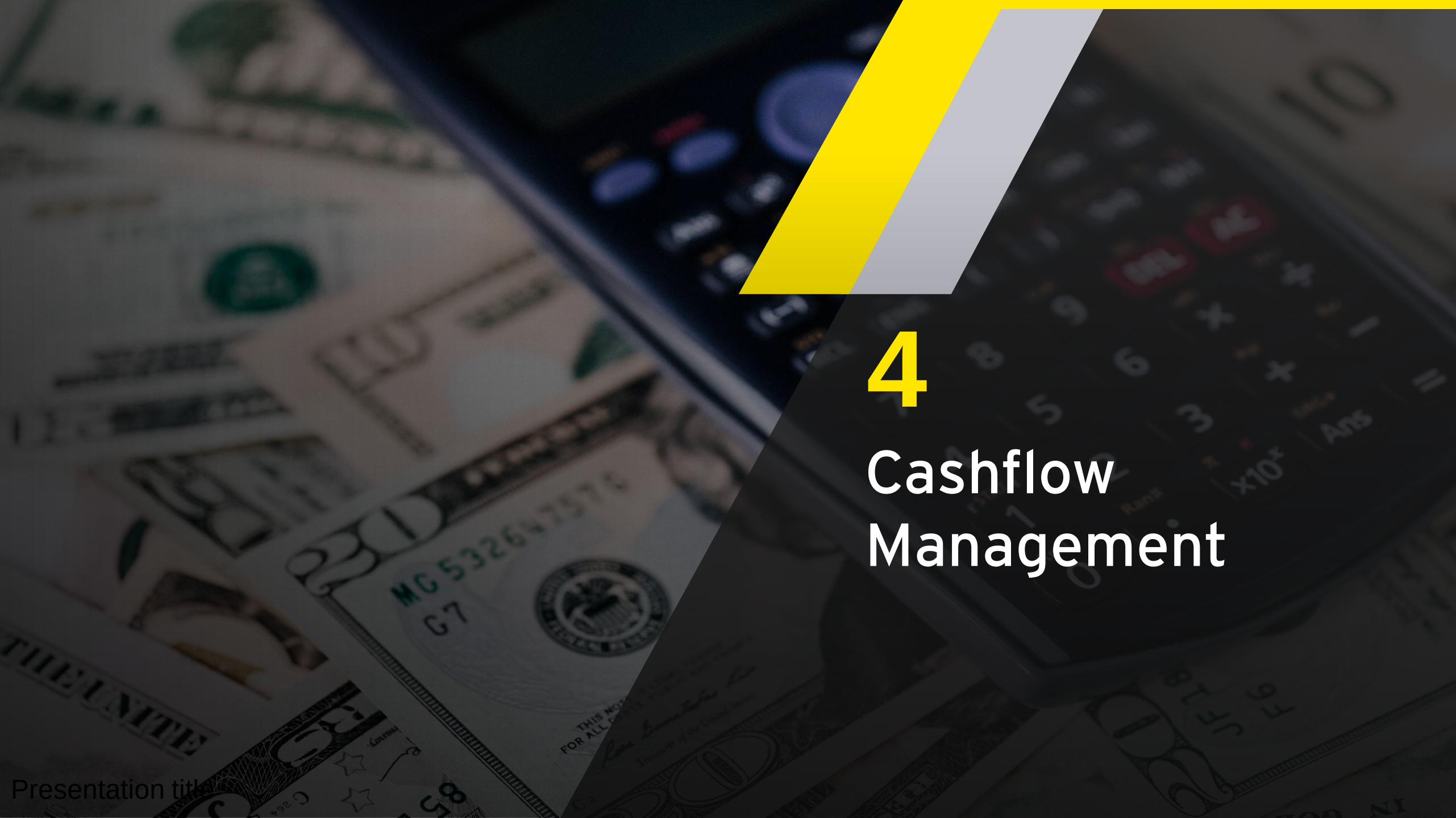
The cloud is advancing steadily into the enterprise, but many ERP users have been reluctant to place the company's crown jewels into the cloud. These reservations are evaporating as advantages of cloud become apparent.

organisations realize cost efficiencies and standards provided by cloud (private and multi-tenant) applications and infrastructure.

Automation

organisations are standardizing and automating processes to achieve efficiencies, improve controls and allocate scarce resources leveraging a spectrum of automation technologies.

To get the most out of automation investments, organisations that take an E2E process approach realize efficiencies, rather than those that take a technology driven approach.



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Cashflow Management

Q & A - Go to www.menti.com use code 8389 2686

Is your business currently facing any cash flow problems

a) Yes
b) No

How much cash does your business currently hold

a) Our cash holding is not adequate to cover one month of operations
b) Our cash holding is adequate cover one month of operations
c) Our cash holding is adequate to cover three months of operations
d) Our cash holding is adequate to cover six months of operations
e) Our cash holding is adequate to cover more than one year of operations

Q & A - Go to **www.menti.com** use code 7992 4027

Does your business monitor cash flow?

a) Yes

b) No

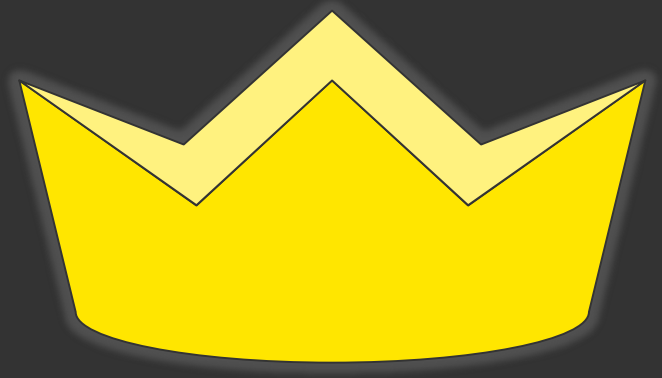
How often does your business monitor cash flow

a) Daily

b) Weekly

c) Monthly

d) We don't monitor cash flow



Cash is King

A cash management plan that considers all available opportunities to conserve cash and manage working capital

Crisis management

- Ensure cashflow management is linked to you crisis management response
  - Crisis management team and stakeholders
  - Cashflow forecast reporting is fed in to the management forums
- Evaluate different cashflow scenarios and exposures
- Prepare crisis communication for employee infections (internal and publicly)

Implement organisational set-up to help you manage cash going forward

Short-term cash management

- Identify available cash and due payments
- Keep track on demand indicators (travel bookings & cancellations)
- Obtain and update cash flow forecast and prepare active cash-steering
- Prepare and enact immediate "stop-the-bleeding" measures, e.g.
  - working capital measures,
  - flexible work arrangements for employees,
  - temporary interruption of service

Rapidly gain transparency on the liquidity situation and implement countermeasures

Cash tax management

- Understand Government stimulus measures you can rely on
- tax levers are available to you to maximize cash, e.g. tax credits and incentives, repayments of overpaid tax collected
- Assess options to defer cash tax payments, e.g. through available deductions, use of tax attributes, assessment of outbound payments
- Identify cash savings from realigned forecasts e.g. due to disruptions in supply chain and work force or updated operational effectiveness

Effectively utilise tax levers to support short-term cash management

EY teams 3 Day Quick Check

- Set-up of crisis management teams with focus on cash transparency and emergency measures
- Rapidly identify material cash risk areas and assess potential impact
- Define necessary actions focusing on short-term liquidity management, cash tax management and overall crisis management to adequately respond to the challenges of the Corona crisis

There are three key areas to focus on quickly, getting control of you cash, putting actions in place to manage cash

Cash Management Office

- Rapidly creating transparency
- Establishing of cash-office including a cash desk (approval of each payment)
- Cash and burn rate monitoring
- Reliable cash-forecast (e.g. on a 13-week basis)
- Active cash-steering

Gain visibility of your forecast cash position and establish governance control over cash decision making

Spend Reduction

Opex

- Review all expenditure and categorise its criticality and ability to defer or cancel
- Cancel, reduce or defer non-essential expenditure
- Change delegations policy – CFO now require to approve all expenditure above lower threshold
- Implement immediate controls on overtime, temps labour, stationery etc
- Recall or cancel p-cards
- Access government programs (eg. Apprentice funding)

Capex

- Cancel, reduce or defer all capital projects
- Confirm milestone payments are in cash-forecast – delay if possible

Develop concrete actions with cash impacts, daily check lists and clear accountabilities

Debt facilities

- Review cashflow forecasts for financial covenant breaches
- Assess whether current bank facilities provide sufficient liquidity
- Draw unused facilities and mitigate the risk of financiers cancelling limits
- Commence communication with financiers. Early communication is critical given heavy workloads and bottlenecks in credit decisioning
- Seek covenant and amortisation waivers
- Consider alternative funding solutions; supply chain and asset finance, sale and leaseback, subordinated debt and convertible loan note instruments
- Understand what government assistance may be available for your business

Enter targeted discussions with relevant financiers to secure portfolio company survival

10 tips to improve robustness of short term cash flow forecast

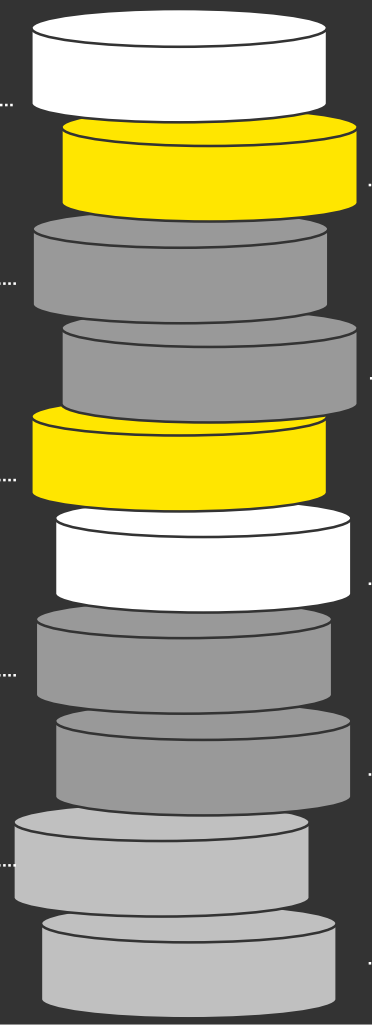
Understand cash flow contributions of specific product lines/business units

Encourage debate with key stakeholders such as sales and procurement leads when planning the forecasts

Identify and quantify risks and opportunities in the forecast

Renew assumptions on a timely basis

Recognise sponsor's requirements



Accountability-involve all those who will be accountable for delivering a robust STCF

Identify and communicate KPIs

Monitor on a weekly and if appropriate daily basis

Effective communication

Explore operating efficiencies and cash generating initiatives

A typical 'weekly forecasting routine'

	Friday	Monday	Tuesday
Business teams provide data (eg sales, HR, advertising)	Send data forecast schedules to the Forecaster		
Forecaster (Typically a member of the finance team at each subsidiary)		1. Receive forecast data 2. Update template for 7 days 'actual' data 3. Prepare forecast using template and data from the business. 4. Submit draft forecast for review 5. Prepare variance analysis (AvF and FvF)	
General (and) Finance Manager		1. Review and sign forecast 2. Review and sign variance analysis	
Group Treasury			Prepare consolidated group forecast report

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Working Capital Management

Q & A - Go to **www.menti.com** use code 9744 3514

Does your organisation face any working capital challenges?

a) Yes
b) No

On average how long do your **key** customers take to pay?

a) Cash
b) 30 days
c) Over 30 days

Q & A - Go to **www.menti.com** use code 4190 2770

What credit terms do you receive from your **key** suppliers

a) Cash on delivery
b) 30 days credit
c) Over 30 days credit

On average how long do you take to pay your **key** suppliers?

a) Cash
b) 30 days
c) Over 30 days

Definition and Metrics

Net working capital = Current assets - Current Liabilities

- ✓ Trade receivables
- Other receivables
- ✓ Inventory
- ✓ Prepayments to suppliers
- Other prepaid expenses

- ✓ Trade payables
- Other payables
- ✓ Customer prepayments
- Deferred revenue

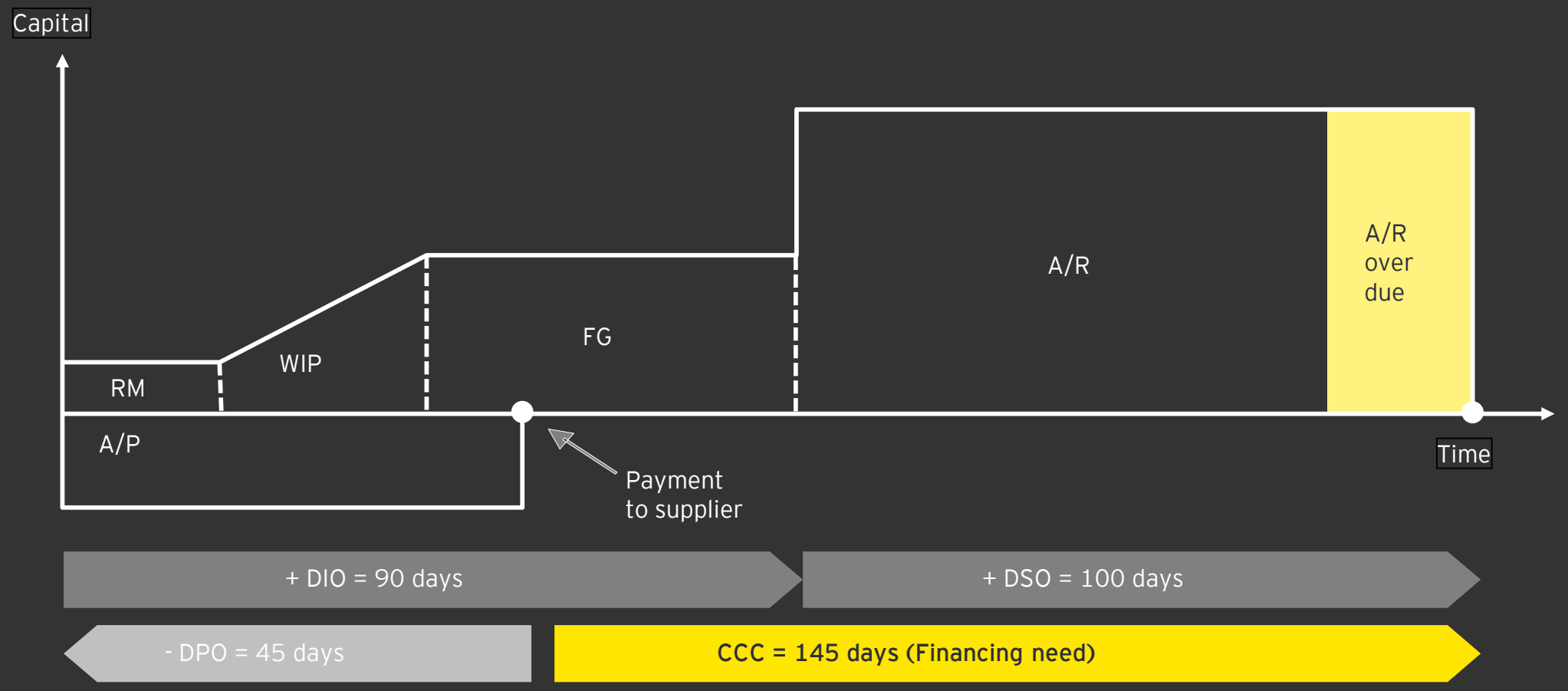
Trade working capital = Trade receivables + Inventory + Prepayments to suppliers - Trade payables - Customer prepayments

Cash Conversion Cycle	=	Inventory conversion period	+	Receivables conversion period	-	Payables conversion period
CCC	=	DIO	+	DSO	-	DPO

Inventory	Receivables	Payables
COGS/365	Sales/365	COGS/365

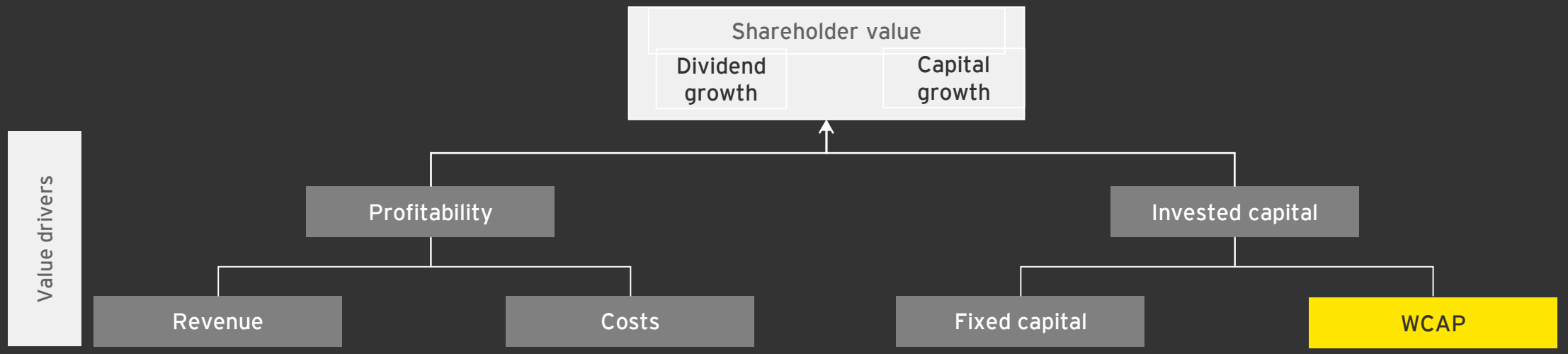
Cash conversion cycle has significant impact on the level of borrowing required to finance working capital

Cash conversion cycle (CCC)



In our markets the CCC cycle remains long, thus significant room for improvement

Working capital is a key component of the value chain and can have a clear impact on shareholder value



Process improvements

- New products
- New distribution and sales channels
- Pricing
- Enhanced customer service

- Lower COGS, transportation, distribution and warehousing costs
- Reduce cost of capital
- Minimize margin erosion
- Best structure (e.g., SSC – preventing duplication)

- Improved physical asset performance
- Sale and lease back
- Outsourcing

- Improving processes in:
  - Forecast to fulfill
  - Order to cash
  - Purchase to pay

Working capital is influenced by people across the organisation

Performance indicator	Meaning	Main people in charge	Comments
Days of sales outstanding (DSO)	Average time a receivable remains on the balance sheet, measured as the number of days sales represented by the AR balance **How long does it takes to get paid?**	▸ Sales ▸ Customer Service ▸ Credit ▸ Collections	▸ Driven by payment terms ▸ Timeliness of payment ▸ Eliminating issues that cause later payment
+			
Days of inventory outstanding (DIO)	Inventory in terms of number of days of sales/usage **How long will it take to consume the inventory?**	▸ Sales/Marketing ▸ Customer Service ▸ Manufacturing ▸ Supply Chain ▸ Distribution	▸ Buffer between supply and demand ▸ Forecast accuracy ▸ Manufacturing strategy
−			
Days of payables outstanding (DPO)	Value of the creditor balance in terms of number of average days of purchases. **How long does it take to pay?**	▸ Purchasing ▸ Finance ▸ Distribution	▸ Driven by payment terms (leverage) ▸ Payment triggers ▸ Payment clock ▸ Payment methods
=			
Days of net working capital (CCC)	Value of the NWC in terms of number of average days of sales. **How many days of sales do we carry as working capital to run the business?**	▸ Everyone	▸ The lower the better

The perception and reality of working capital

Working capital perception

- It is a finance issue
- It is a balance sheet item
- It is improved only with systems implementation or strategic changes
- It has a negative impact on customer service (collect early, pay late, push products out)
- It creates small benefits

Working capital reality

- It is an operational issue
- It also impacts P&L
- It is improved with new policies, processes and metrics among others
- It has a positive impact on customer service (pay, deliver and collect as agreed)
- It creates significant benefits

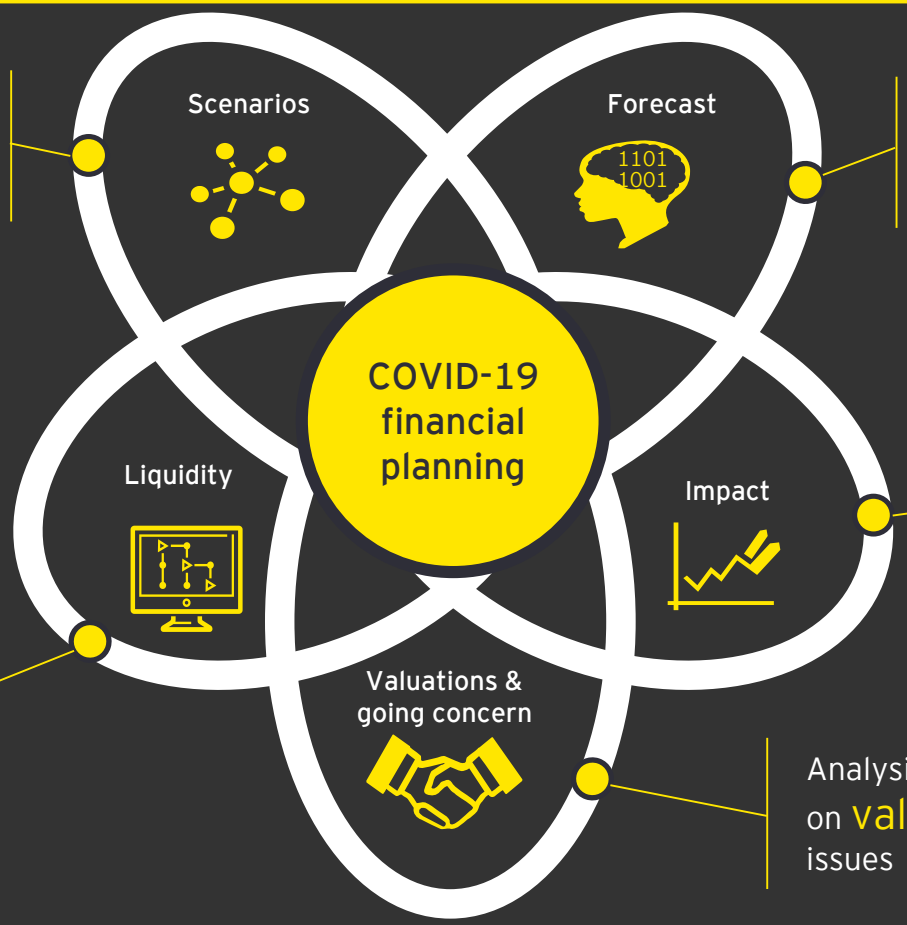
6

Financial Budgeting

Call for Action: Get ready for post-COVID-19!
EY Advice: Build-in COVID-19 Business Scenarios & Financial Plan

Definition of possible scenarios taking into account up-to-date global political and macroeconomic developments

Development of an ad-hoc financial forecast to derive possible liquidity shortages based on defined future scenarios



Presentation and simulation of COVID-19 impact on financial KPIs and financing covenants

Development of a daily liquidity forecast (13-week-forecast) based on a short-term cash flow model taking into account defined future scenarios

Analysis of the COVID-19 impact on valuations and going concern issues

Prepare business plan, liquidity forecast and scenario analysis to prepare informed decision making based on Post-COVID-19 Financial Scenario Planning and Strategic Portfolio Optimization!

7

Financial Reporting

Key Financial Statements Investors require

The Balance Sheet

Key Features:

- It is broken into three categories assets, liabilities, and shareholders' equity
- Shows the financial position of a business
- Expressed as a "snapshot" or financial picture of the company at a specified point in time (e.g., as of June 30, 2020)

The Balance Sheet Formula

Assets= (Liabilities + Owner's Equity)

The Income Statement

Key Features:

- Shows the revenues and expenses of a business
- Expressed over a period of time (i.e., 1 year, 1 quarter, Year-to-Date, etc.)
- Uses accounting principles such as matching and accruals to represent figures (not presented on a cash basis)
- Used to assess profitability

Income Statement Formula

Net Income= (Revenue – Expenses)

The Cash Flow Statement

Key Features:

- Shows the increases and decreases in cash
- Expressed over a period of time, an accounting period (i.e., 1 year, 1 quarter, Year-to-Date, etc.)
- Undoes all accounting principles to show pure cash movements
- Has three sections: cash from operations, cash used in investing, and cash from financing
- Shows the net change in the cash balance from start to end of the period

8

Resource Mobilisation

Resource Mobilisation

1. Consider the funding needs of the company in light of business plan and strategic goals, capital expenditure requirements and working capital needs

2. Debt sustainability should be assessed not only in terms of serviceability, but also in terms of a company's credit rating. The rating is a function of preference, peers, risk appetite and strategic plans

3. Assess the funding sources by examining equity, debt and hybrid instruments against criteria to determine the optimal sources

4. The capital requirements should factor in regulatory frameworks and an internal safety buffer.

Pros and cons of funding options

Option	Description	Pros	Cons
Mezzanine funding	▸ Hybrid of debt and equity financing that gives the lender the right to convert to an equity interest in the company	▸ No dilution ▸ More manageable than other debt structures	▸ Expensive ▸ High risk
Debt	▸ Raising money for working capital or capital expenditures by selling debt instruments to individuals and/or institutional investors	▸ Control maintained ▸ Provides funding at lower rates than equity financing	▸ Locked into payment schedule ▸ Borrower to adhere to covenants
Equity (minority stake sale)	▸ Process of raising capital through the sale of shares in an enterprise. It refers to the sale of an ownership interest to raise funds for business purposes. Minority stake sale refers to a sale of less than 50% ownership	▸ Control maintained ▸ Value addition in both experience and capital	▸ Valuation outcome maybe impacted ▸ Misalignment in business goals, values will be costly
Equity (majority stake sale)	▸ Same as above but majority stake sale refers a sale of more than 50% ownership in the business	▸ Better valuation outcome ▸ Value addition in both experience and capital	▸ Control lost ▸ Misalignment in business goals, values will be costly

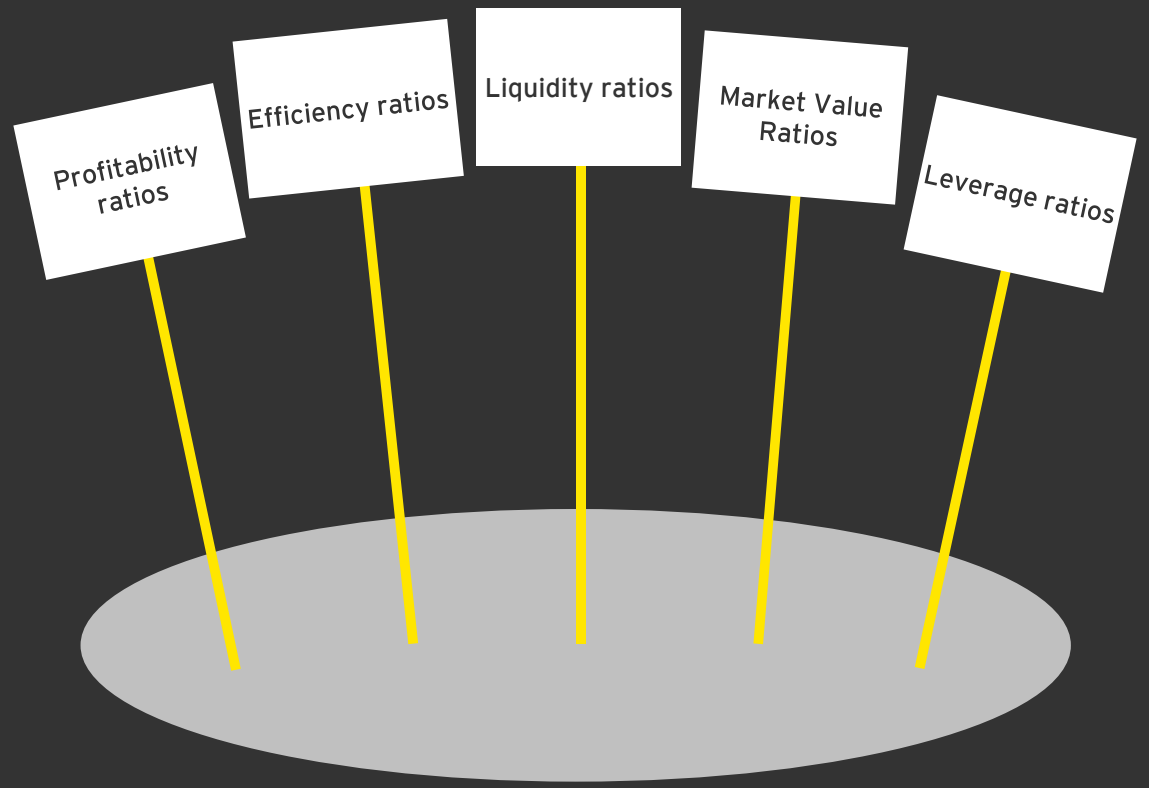
9

Financial Analysis

Key financial ratios for investor readiness

Financial ratios are prepared by extracting information from financial statements such as cashflow statements, balance sheet and income statement. They are used to examine the company's liquidity, leverage, profitability and rate of return on investment

They are grouped in 5 categories



Q & A