Improving Working Capital Management and Cash Flow Intelligence
Contents

Project Personnel and Copyright 2
Participant Information 4
Prologue 5
Executive Summary 8
Study Scope 10
Overview of Best-Practice Organizations 11
Overview of Subject Matter Expertise 14
Acknowledgments 15
About Protiviti 15
Best Practices 17
Results 44
Call to Action 46
Methodology 48
Case Study: General Mills, Inc. 50
Case Study: Owens-Illinois, Inc 60
Case Study: Zappos.com, Inc 71
Improving Working Capital Management and Cash Flow Intelligence

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STATEMENT OF PURPOSE

The purpose of publishing this report is to provide a reference point for and insight into the processes and practices associated with certain issues. It should be used as an educational learning tool and is not a “recipe” or step-by-step procedure to be copied or duplicated in any way. This report may not represent current organizational processes, policies, or practices because changes may have occurred since the completion of the study.
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Prologue

Working capital management (WCM) has become a hot topic for organizations of all sizes. As the impact of the recent economic downturn has hit, senior executives have looked for ways to do more with less. Many have come to realize that they make a significant investment in their working capital, and some of this investment may not be necessary if working capital management can be improved. In this study we examined three major firms to see how they handle their working capital and what general conclusions can be drawn from their approaches.

All three organizations clearly consider effective working capital management as a necessary component of their growth and profitability. By turning to their working capital as a source of funds, each organization actively reaps the benefits from efficient, streamlined working capital management. Each organization actively manages its working capital, but with differences in approach due to the nature of the companies’ business lines as well as the relative importance of one area of working capital.

Common to each organization is a cross-functional approach to working capital management. These companies do not wait for problems to occur; they anticipate them and make adjustments in near real time. Tapping into companywide systems, such as enterprise resource planning, allows organizations to disseminate information faster than by using more conventional means (e.g., written reports). The accumulation and use of data are hallmarks of an effective working capital management system.

Finally, nothing brings working capital management to a halt more than senior management indifference. The successful track records of the three best-practice companies in this study show that senior management was anything but indifferent. Each company in its own way took steps to engage managers across organizational levels. This active support from top to bottom is clearly effective, as these firms’ improvements in working capital management show. All in all, these companies have much to share.

—Ken Parkinson, Managing Director, Treasury Information Services, and Study Special Adviser
The prevailing view of working capital management is being transformed in the wake of the worst economic downturn since the Great Depression. As a result, more and more companies are deploying WCM processes to harvest value on a continuous and long-term basis, regardless of market conditions.

This was rarely the case in recent years. The traditional approach held that working capital management represented an activity that organizations largely overlooked during periods of growth and then scrambled to resuscitate when economic conditions deteriorated.

Today, a new perspective on working capital management is emerging. Corporate executives—and, indeed, members of corporate boards of directors—now view working capital management in more strategic, holistic, and sustainable terms. Cash is always king in tough times. Yet, as the economy shows signs of improvement, leading companies have made it clear that their reign over cash management will continue over the long term.

A growing number of organizations are treating working capital management as a) one of the three key pillars of cash management (along with cash flow forecasting and liquidity management), and b) an integral component of enterprise risk management programs (which, increasingly, are being integrated with performance management processes conducted on a daily basis).

Protiviti’s collaboration with companies worldwide that are embracing best practices in working capital management indicates that more CFOs, controllers, and treasurers are putting in place new processes, expertise, and supporting technology to reduce working capital requirements across the three primary drivers, including accounts payable, accounts receivable, and inventory. Additionally, this focus and expertise are extending into areas such as procurement, sales, customer service, and supply chain. These efforts, in turn, are freeing up cash to fund strategic investments while delivering higher-than-expected results to their shareholders.

Leading working capital programs, including those executed by the three companies benchmarked in this report, drive sustainable value in the form of additional cash return on invested capital. As these companies are demonstrating, delivering this value requires a holistic view across multiple processes and business cycles, value drivers, and systems within an enterprise.

General Mills’ commitment to cross-functional collaboration and benchmarking, for example, has enabled the Fortune 500 food products company to monitor and manage each business unit’s individual working capital and fixed-asset performance for the purpose of managing return on capital more effectively.

Owens-Illinois, the world’s largest producer of glass containers, has defined a clear vision and strategy through the use of continuous improvement and Lean Six Sigma methodologies in its working capital management process, which has been largely automated and is tracked on a daily basis. By effectively linking working capital to
operational excellence, one of O-I’s four strategic objectives, the company has been able to maintain a multiyear sustainable focus on working capital measurement and improvement across the organization. This linkage of O-I’s working capital objectives to its corporate strategy has helped ensure ongoing senior executive support, a common theme across each of the best-practice companies in this study.

Meanwhile, shoe and accessory retailer Zappos.com strives to foster a culture that understands the impact of working capital on profitability and infuses daily activities and decision making based upon its working capital management analysis. Zappos.com executes these activities through a distinct focus on cross-functional communication and change management to drive and maximize working capital performance. Zappos.com has also developed training courses to impart working capital management principles to all employees.

This drive to weave working capital management into the fabric of organizational culture as well as daily decision making reflects the growing importance of cash management—and all forms of risk management—in an increasingly dynamic global economy. By understanding and implementing, where appropriate, the leading practices identified in this report’s key findings, organizations can transform their working capital management program from a bulwark against tough times to a source of value in all times.

Thanks to the credit crunch and the historic economic downturn it sparked, most companies during the past 24 months have invested significant time, attention, and resources in their working capital management processes. The extent to which these investments bear fruit over the long term will depend on the degree to which organizations treat working capital management as a sustainable, rather than cyclical, endeavor.

_By training and educating the entire workforce on the value of sustainable working capital management capabilities, organizations will no longer need to scramble to plant corn, or free up working capital, the next time a credit crisis or a recession emerges._

—Christopher Monk, Director, Supply Chain, and Brad Rachmiel, Director, Protiviti
Executive Summary

During the Great Recession of 2008–09, CFOs and their teams proved to be very adept at slashing costs and liberating cash otherwise trapped in operations. By the middle of 2010, U.S. companies were holding close to $2 trillion in cash on their balance sheets. “That is about 40 percent more in cash and cash equivalents, relative to revenues, than four years ago,” noted Charles Mulford, professor of accounting and director of the financial analysis lab at the Georgia Institute of Technology.

How did they raise all that cash? They stopped spending on people, capital equipment, and business services. Many of the largest cash-laden companies rode the yield curve down and refinanced their debt. Wherever possible, companies cut overhead, some making moves such as shifting from unionized to non-unionized plants in North America. A host of big companies sought authorizations to execute share repurchase programs, but in reality they did buybacks slowly and carefully. Most invested in better working capital management and sought ways to accelerate the cash conversion cycle.

In early 2009, when the specter of recession was deeply troubling senior management teams, the financial management research team at APQC began studying what large organizations were doing to increase their free cash flow margins. It may be hard to imagine now, but when storied Wall Street banks such as Lehman Brothers collapsed, a number of CFOs and treasurers worried about whether their access to external capital might be blocked for some undeterminable time. To protect their shareholders’ investments, they began to raise cash from operations with a fervor not seen in the past 30 years. In essence, they created a safety blanket of vast liquidity.

And, what now? According to APQC research conducted parallel to this collaborative study, CFOs will not stop harvesting unproductive cash from operations in the future—even when the skies are completely clear and it’s time to aggressively ramp up growth investments. An APQC survey that involved senior finance executives at 355 large organizations indicates that improving working capital management is a goal that CFOs now want to pursue continuously (Figure 1, page 9). In short, the effort to raise liquidity during the recession delivered some astonishing “lessons learned.” The most compelling is this: Strong disciplines in working capital management lead to strong disciplines in operations—and that is what drives significant gains in resource productivity and, by extension, economic profit growth. Beyond that, after spending tremendous effort to raise cash levels—and learning what works and what doesn’t when it comes to driving meaningful gains in process performance—CFOs tell us it would be folly to let bad habits slide back in.
We Feel a Sustainable Commitment to Improving Working Capital Management Would Offer Clear Operating Benefits

Figure 1

The report that follows is APQC’s further effort to examine what leading companies are doing to ensure that they drive continuous improvement in working capital management and generate high-quality cash flow intelligence.

APQC benchmarked three organizations with leading approaches to working capital management. This report details the best practices derived from these organizations. A list of the study’s key findings, detailed throughout this report with supporting examples, follows.

1. Best-practice organizations align overall operational processes with stated strategic intent.
2. Best-practice organizations engage executive-level support for and involvement in working capital optimization as a prerequisite for reducing the amount of cash invested in their operations.
3. Best-practice organizations centralize and standardize financial transaction processing to drive maximum efficiency and to draw meaningful insights out of underlying data.
4. Best-practice organizations take a cross-functional approach to working capital accountability and continuous improvement of receivables and payables processes.
5. Best-practice organizations use data from an ERP system to inform daily credit and collection activities.
6. Best-practice organizations conduct real-time analysis of cash flow drivers to ensure reliable forecasts and optimize spare cash.
7. Best-practice organizations analyze, measure, and advise operating units on how to increase the return on working capital invested in operations.
8. Best-practice organizations design custom measures of working capital management that are relevant to their business models.
9. Best-practice organizations apply quality and productivity tools to process improvement efforts in finance.
11. Best-practice organizations identify and resolve data discrepancies on the front end of the process.
14. Best-practice organizations conduct transactions electronically whenever possible and work with vendors so they can do the same.

STUDY SCOPE

Many organizations today are carefully re-examining their working capital metrics and where cash on the balance sheet is invested. These organizations wish to avoid punishing customers and suppliers while improving their cash flow. More specifically, CFOs, controllers, and treasurers are seeking new procedures and systems that provide fast, actionable information about current and future cash flows and working capital requirements. And they are increasingly eager to leverage information management and network/platform innovations that can help them be opportunistic with cash flows.

Optimizing working capital management and cash flow planning capabilities is both a challenge and a necessity for organizations. Concerns such as demand volatility, access to bank credit, and customer payment defaults/delays make working capital management and cash flow intelligence key strategic issues. This study was designed to help study participants address these and similar concerns.
OVERVIEW OF BEST-PRACTICE ORGANIZATIONS

The best-practices organizations selected for in-depth review have developed varied, successful approaches to working capital management that reflect their unique cultures and strategic concerns. A snapshot of each one follows, and a detailed case study was written for each.

General Mills, Inc.

Minnesota-based General Mills is a Fortune 500 company that specializes in food products manufacturing, sales, and distribution. With 33,000 employees, it operates globally and has offices in 30 countries. In 2009 the organization reported $14.7 billion in revenue from its portfolio of brands, including Betty Crocker, Pillsbury, Green Giant, Nature Valley, Yoplait, Häagen-Dazs, and Cheerios.

General Mills considers its top three working capital management processes to be: 1) its efficient accounts receivable (AR) processes and customer risk management, 2) its supply chain finance approach, and 3) its integrated working capital review process for setting objectives and reviewing results.

One of the key visions for General Mills in terms of working capital management is a commitment to cross-functional collaboration. General Mills holds monthly meetings with its working capital management team composed of its corporate controller, treasurer, vice president of finance for supply chain, vice president of the retail sales organization, and director of global business services. These meetings assess upcoming changes in working capital requirements and levels, as well as identify problem areas.

In terms of analytics and measures, General Mills tracks its days sales outstanding (DSO), days payables outstanding (DPO), and days of sales (inventory). Also, as an extension of its cross-functional collaboration efforts, the organization communicates and dissects the drivers of return on capital (ROC), and it isolates, to the extent practical, working capital and fixed-assets management performance for each business unit. The point is to continually educate operating people on the critical nature of working capital efficiency and to discuss ways that key performance drivers can be influenced proactively. By emphasizing that ill-conceived deployment of working capital carries a cost that should be avoided, the cross-functional management team shows how profitability can be impacted when working capital is sub-optimized.

To assess the progress of its working capital management improvements over time, General Mills annually benchmarks peers’ working capital management processes. This benchmarking exercise covers a variety of measures and processes within finance.

Through the implementation of several technologies, General Mills has automated more than 70 percent of its processing (e.g., invoice processing and transaction processing). Much of the treasury function at General Mills is automated. General
Mills uses sophisticated cash flow forecasting tools as a result of the automated data inputs.

**Owens-Illinois, Inc.**

Ohio-based Owens-Illinois is the world’s largest producer of glass containers, with more than 22,000 employees and more than 80 factories in 21 countries. Serving primarily the food and beverage industries, Owens-Illinois has been on the Fortune 500 list since its inception in the 1950s, with revenues of $7.1 billion in 2009 and with the bulk of business occurring outside of North America.

Owens-Illinois implemented Lean Six Sigma to transform its operations, which affected working capital by improving processes and promoting better cross-functional collaboration. Lean Six Sigma also helped assimilate the company’s financial shared services organization and its mission into the culture of the organization. Owens-Illinois reinforces this collaborative environment through meetings, training, and Lean Six Sigma events.

Owens-Illinois has key performance metrics for each working capital management process. These metrics are generated and reported automatically and tracked daily. Clearly designated owners immediately act on any underperformers.

Owens-Illinois annually benchmarks working capital management as part of its process improvement efforts. Finance executives understand the need for continued improvement and are committed to exploring new tools and techniques to facilitate better process controls and growth.

Owens-Illinois’ finance team uses a report writing tool to generate metric data and process performance results. The tool is independent of IT support, and the team is virtually self-sufficient in its use. Owens-Illinois also has automated many of its working capital management processes through SAP. Lastly, its working capital management owners have developed simple tools for vendors, sales representatives, logistics personnel, and customers to use. These tools facilitate better decisions about factors that may affect working capital.

**Zappos.com, Inc.**

Nevada-based Zappos.com is one of the largest shoe and accessory retailers online, with more than 2,000 employees in its family of companies and more than $1 billion in yearly gross sales. The company was purchased by Amazon.com in 2009. An independently operated subsidiary, Zappos.com is currently adopting many of Amazon’s processes and expanding sales to include apparel, housewares, and beauty products. The acquisition has transformed Zappos.com from a net borrower to a net investor.

Zappos.com is committed to cross-functional collaboration throughout its working capital processes. The organization holds a training course to expose all employees to working capital management principles and explain the impact of working capital.
on overall profitability. Its working capital management team has developed tools to enable staff outside of the finance function to make better decisions that will affect working capital.

The organization tracks key performance indicators on a weekly basis, as well as provides sales figures to the entire organization daily. Its operational control committee oversees the measures and helps to identify any areas in need of improvement. This process of weekly reviews helps to make working capital management decision makers aware of potential issues before they become problems.

Zappos.com holds monthly manager meetings to assess its financial performance. Managers from across the organization meet to discuss actual performance results relative to forecasts. When there are shortfalls in performance, these meetings serve as a platform to discuss improving operational efficiencies. The monthly managers meetings keep cash flow goals at the forefront of managers’ minds throughout the organization.

To bolster its controls on working capital management, Zappos.com developed an online vendor portal for supplier communication. Additionally, Zappos.com uses Oracle Workflow to track all steps in the payables process. Zappos.com is also implementing an organization-wide system that will create real-time visibility of all exception data.
SUBJECT MATTER EXPERTISE

Mary Driscoll, Senior Research Fellow, Financial Management, APQC

Mary Driscoll is an author, an editor, and a lecturer with expertise in corporate finance and business management. She serves as senior research fellow at APQC, where she leads the new financial management best practices research initiative. Previously, she was president of CFO Research, the research services arm of CFO magazine. She also spent seven years as a senior editor at CFO, developing features on topics ranging from finance transformation and capital markets to financial management information systems and leadership development. Ms. Driscoll has written several business books, including the professional reference guide Cash Management: Corporate Strategies for Profit (John Wiley & Sons). She has won journalism awards on corporate finance, treasury operations, and personal financial planning topics. She currently serves on the advisory boards of three technology startups.

Ken Parkinson, Principal, Treasury Information Services (TIS)

Ken Parkinson is a principal at TIS. He is an experienced consultant, educator, writer, and financial manager. His experience as a consultant and as a corporate treasury manager includes the development and implementation of major treasury systems in both mainframe and PC environments. As a treasury manager, he evaluated and selected treasury services from commercial and investment banks and other providers worldwide. As a treasury consultant, he has worked closely with clients to select appropriate banking services, evaluate bank service charges, and design effective treasury systems.

Mr. Parkinson has been a visiting/adjunct professor of finance at the Stern School of Business at New York University for more than a decade. He has taught undergraduate and graduate courses in introductory finance, working capital management, financial e-commerce, and (long-term) corporate finance. In addition to his teaching at Stern/NYU, he has also taught at and trained executives at Duke University, University of North Carolina, New York Institute of Technology, Fairleigh Dickinson University, American Institute of Certified Public Accountants and state CPA societies across the country, American Management Association, Association for Financial Professionals (with its predecessor groups), Treasury Management Association of Canada, regional treasury management associations across the United States and in Canada, National Association of Credit Management, Operations Research Society of America/The Institute of Management Science, Business International, and IBC (London, UK).

Mr. Parkinson has authored, coauthored, or made major contributions to more than a dozen books on treasury management, including RFP Questionnaires for Financial Services, Preparing for Treasury Management Certification, How to Prepare an RFP for Treasury Services, Corporate Cash Management Handbook, Managing Bank Relations, Corporate Liquidity, Cash Management Templates, Essentials of Cash Management (2nd and 3rd eds.), and Treasury Manager’s Guide to the Internet. He
has served as editor-in-chief of the Journal of Cash Management, technology editor and contributing editor of Corporate Cashflow magazine, senior editor of Business Credit magazine, and co-editor of The Treasury Pro, a monthly newsletter.

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Again, APQC would like to thank General Mills, Owens-Illinois, and Zappos.com for sharing their internal strategies and practices for improving working capital management and cash flow intelligence with their fellow study participants.

ABOUT APQC

APQC is a member-based nonprofit and one of the leading proponents of benchmarking and best practice business research. Working with more than 500 organizations worldwide in all industries, APQC focuses on providing organizations with the information they need to work smarter, faster, and with confidence. Every day we uncover the processes and practices that push organizations from good to great. Visit us at www.apqc.org and learn how you can make best practices your practices.

ABOUT PROTIVITI

Protiviti (www.protiviti.com) is a global business consulting and internal audit firm composed of experts specializing in risk, advisory, and transaction services. The firm helps solve problems in finance and transactions, operations, technology, litigation, governance, risk, and compliance. Protiviti’s highly trained, results-oriented professionals provide a unique perspective on a wide range of critical business issues for clients in the Americas, Asia-Pacific, Europe, and the Middle East.
Protiviti has more than 60 locations worldwide and is a wholly owned subsidiary of Robert Half International Inc. (NYSE symbol: RHI). Founded in 1948, Robert Half International is a member of the S&P 500 index.

Protiviti helps client executives improve working capital and cash flow, control and optimize costs, and manage risk in their operations. The firm helps drive performance within the finance function and across an organization’s supply chain through process improvements, strategic sourcing strategies, inventory and contract management, and enhancements to working capital. Protiviti also assists client executives with improving their control over major capital and construction projects, creating more reliable project timelines and reducing exposure to cost overruns.

Protiviti’s Cost and Working Capital Optimization team is able to work with companies to improve process capabilities, cut costs, and recover lost funds. We advocate a four-step proactive approach to improving the management of working capital.

1. Uncover Sources of Uncertainty
   Companies should begin by determining what new and existing risks they face, and determine how those risks will impact demands on working capital.

2. Conduct a “Working Capital Diagnostic”
   Companies can assess working capital effectively by analyzing data about their operations and benchmarking to peers.

3. Reassess Working Capital Policy
   Determining working capital policy is a function of an organization’s business model and risk tolerance to determine whether current risks allow for an aggressive, moderate, or conservative policy.

4. Optimize Working Capital
   Opportunities to optimize working capital exist in areas including cash and marketable securities, sourcing, procurement, AR, AP, and inventory.

For further information about Protiviti’s Cost and Working Capital Optimization Solution, please contact:

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Best Practices

VISION AND STRATEGY FOR IMPROVING WORKING CAPITAL MANAGEMENT

Finding 1: The primary driver for working capital improvement at best-practice organizations is to align overall operational processes with stated strategic intent.

Working capital management has bottom-line impact. The best-practice organizations in this study found quantifiable economic benefits from improving working capital processes at the operational level. Obviously related to that, the organizations also found strategic benefits to improving back-end finance processes. That is, by affecting operating discipline, working capital management helped these organizations reach their strategic goals. For all of the best-practice organizations in this study, working capital improvements were driven by customer-centric, overarching strategies.

Owens-Illinois maintains an aggressive growth strategy to expand production capabilities worldwide and to grow more stable and saturated markets through the introduction of new glass container concepts. Its focus on continuous expansion and improvement is supported by four strategic priorities: strategic and profitable growth, marketing glass, market innovations and technology, and operational excellence (Figure 2, page 18).

In the realm of payables and receivables management, Joan Channell, global director of shared services, has helped to support these priorities through standardization, benchmarking, key metrics, and the implementation of Lean Six Sigma. Her team set targets for investments in receivables and payables to balance these two efforts and developed predictive metrics to find signs of deterioration in customer payment patterns. Ed White, Owens-Illinois CFO, said, “With good working capital management, we’ve freed up cash to grow the company instead of just maintain what we have.”
The overarching strategy at Zappos.com is to provide superior customer service. A key part of this mission involves stocking everything at the fulfillment center in Kentucky rather than drop-shipping goods, to enable control over the entire customer experience. Developing a sound strategy for working capital has helped Zappos.com expand its business by supporting customer service while minimizing the necessary inventory investment for its fulfillment approach.

General Mills also has a growth-focused strategy, with directives to innovate, build brands, lead customer growth, expand internationally, and expand holistic margins (protecting its margins by eliminating costs that do not add value). Senior management believes working capital management supports this growth through the cycle detailed in Figure 3 on page 19. Thus, capital utilization is a strategic focus for the organization’s finance function (along with business performance management, globalization, and portfolio management).

General Mills leverages working capital management to treat suppliers strategically and strengthen customer relationships, for example, through supply chain finance techniques such as payables factoring and dynamic discounting. This has allowed the organization to extend its payment terms without punishing suppliers.

Its focus also requires the organization to set inventory strategy in light of capital spending targets. For instance, the finance function assesses plans for new product launches and gauges excess capacity that may be needed to build up new product inventory before the rollout date arrives. The goal is to get just the right amount
while avoiding investment in extra capacity to the extent possible. This helps General Mills meet demand from retailers and optimize inventory, especially for food products with short shelf lives. Obviously, the goal is to avoid spoilage and write-offs—but a side benefit is a focused discipline around working capital efficiency and overall profitability.

**Finding 2:** Executive-level support for and involvement in working capital optimization are prerequisites for reducing the amount of cash invested in operations.

Senior management support and involvement are necessary in any change management initiative. A finance function needs the clout provided by senior management to reduce the amount of cash invested in operations. Within the best-practice organizations, this involvement is driven by the correlation between working capital management and overall strategic objectives. These organizations’
executives act as sponsors and are involved in the design of improvement efforts and ongoing monitoring of key metrics.

The treasury team holds ultimate responsibility for working capital management at Zappos.com. The team is aided by the senior treasury manager, who oversees both treasury and accounts payable. This dual role provides him with a holistic view of the company’s cash flow position, including payables, check runs, and Automated Clearing House (ACH) runs.

The senior treasury manager reports to the financial controller of the organization. Other key players in working capital management at Zappos.com include the financial planning and analysis (FP&A) team, the merchandising team, and an operational control committee (composed of executives at the director level and above) that reviews key organizational performance metrics.

At General Mills, senior management sets goals, establishes accountability, guides business decisions, and measures results—all to continuously improve the return on capital and ultimately fund growth. The vice president of supply chain, finance, focuses intensely on working capital, and the CFO and controller are ultimately responsible for working capital management. Operating responsibility falls to the:

- corporate controller—coordination and metrics;
- treasurer—cash management;
- vice president of sales finance—accounts receivable;
- vice president of supply chain, finance—accounts payable, inventory, and fixed assets; and
- shared services director—accounts payable processing.

These individuals—along with the director of global business services, who oversees transaction processing within a shared services group—come together for monthly working capital review meetings. At these meetings, participants review the balance sheet, drivers of desired change, and domestic/international working capital metrics.

At Owens-Illinois, the CFO is the champion for working capital and operational excellence in finance. The organization employed a seven-aspect improvement plan to guide its global expansion since 2003:

1. Ownership of the balance sheet value
2. Customer/vendor relationships
3. Visibility of owners
4. Performance metrics
5. Easy goals for early success
6. Public recognition
7. Continuous process improvement
The global director of shared services at Owens-Illinois has worked for years to drive continuous process improvement, particularly in the realms of payables and receivables management. She is certain that senior management support has been pivotal. She said, “The global shared services team gets 100 percent support from the business on working capital management.”

Finding 3: Best-practice organizations centralize and standardize financial transaction processing to drive maximum efficiency and to draw meaningful insights out of underlying data.

When processing is standardized and transactions are maintained in a centralized system, the quality of the information improves. All three best-practice organizations have centralized functions and standardized systems to manage working capital effectively and maintain a customer service mentality.

General Mills focuses daily on collection efforts through dedicated staff in credit and customer service. Cash application and other routine accounts receivable transactions are sourced to a captive in India.

In addition, the organization outsources accounts payable invoice processing to a vendor in India. This outsourcing arrangement:

▶ includes invoice indexing, processing, and issue resolution;
▶ closely integrates with the General Mills global accounts payable processing team in Minneapolis;
▶ consistently meets or exceeds service level agreements;
▶ digitalizes copies of invoices in Minneapolis and routes them for processing and approvals via Workflow (OpenText integrated with SAP); and
▶ standardizes approval matrices within SAP.

The remaining finance operations occur in Minneapolis.

Owens-Illinois has a centralized corporate shared services center, as well as a global shared services group including Europe, Australia, Latin America, and soon an office in China. These centers have high visibility, and the organization works to ensure that center employees consider themselves an integral part of operations. The company has moved to a single point of accountability model, where one staff member is assigned to each account and serves as the source for all details regarding activity on the account.
Finding 4: Best-practice organizations take a cross-functional approach to working capital accountability and continuous improvement of receivables and payables processes.

Working capital management cannot be relegated to a single function. Yet many organizations struggle to break down barriers that prevent functions from working together on process improvements. This study’s best-practice organizations take a cross-functional approach to accountability and have successfully instilled the necessary collaborative cultures. Such an approach often involves the sales, supply chain, treasury, and finance functions.

Zappos.com ensures collaboration and calibration on working capital management through weekly cross-functional management meetings and monthly data meetings involving treasury, financial planning and analysis, and accounting. The operational control committee (composed of executives at the director level and above) meets weekly to discuss and review key operational metrics. This committee maintains oversight of corporate performance metrics and then identifies improvement areas.

On the fourth week of each month, treasury, FP&A, and accounting meet to compare and triangulate their financial data (forecasted cash inflows and outflows versus actual month to date). FP&A prepares monthly reforecasts by meeting with the various department leaders and reviewing the prior month budget versus actual, looking at prior month sales and accounts payable (AP) timing, and adjusting the remainder of the plan year. This comparison helps treasury determine what the final payment runs need to be to hit the monthly free cash flow goal, taking into consideration any sales upside or downside.

The credit, sales, and customer service functions at General Mills collaborate to deliver consistent performance, as well as quickly address issues. The organization also has an experienced, cross-functional team focused on risk management. And in terms of external collaboration, General Mills works with suppliers and customers across its value chain.

Owens-Illinois asserts that cross-functional collaboration and communication are critical for its process improvement efforts. Its shared service centers foster cross-functional collaboration among the accounts receivable, sales, accounts payable, and procurement functions through regular meetings, education and training opportunities, and Lean Six Sigma events. In addition, the organization conducts Lean Six Sigma–driven Kaizen events in which a cross-functional team maps out a business process in order to improve it. These events also help to break down silos by allowing teams to understand the total process.
One example of the success of an internal Kaizen event focused on customer discount controls. Through Lean Six Sigma collaboration, the team was able to conduct a deep-dive analysis of the existing process to understand the root causes of problems and identify opportunities to re-engineer and improve the process. Thanks to the efforts of this team, the organization was able to save $1 million.

The CFO at Owens-Illinois attributes its working capital management successes in large part to transparent cross-functional communication that is data-driven and fact-based.

**PROTIVITI RESEARCH CHAMPION PERSPECTIVE**

Leading working capital management practices exhibit: a healthy alignment between strategy and process, executive-level support, centralized and standardized financial transaction processing, and cross-functional engagement. The findings detailed in this section make perfect sense, as these four qualities also define most other successful business processes. What qualifies as surprising, however, is how important these elements become in practice.

As pressure mounts on organizations to adjust their working capital management policies and processes in the face of economic and marketplace difficulties, a well-defined working capital management strategy executed via well-aligned operational processes becomes of paramount importance.

From 2008 to 2010, the credit crunch and lingering recession leveled historic pressure on most working capital management efforts. Many organizations reacted, almost reflexively, by pushing out payment terms 15 or even 30 days. Although these moves delivered short-term relief, they were neither strategic nor sustainable. Even worse, this particular short-term reaction can cause painful side effects, such as costly supply chain disruptions.

The question, for most organizations, is: How can we create working capital management capabilities that enable us to respond rather than to react?

The organizations whose capabilities are deconstructed in this report serve as valuable role models of ongoing working capital management improvement. Organizations intent on launching similar improvement efforts should begin by developing a working capital management strategy and implementation plan. This strategy, created with cross-functional input, should establish a long-term vision to balance the need for immediate action (e.g., extending payable terms to all suppliers) with the need for responses that generate more sustainable benefits and value.

Once a working capital management strategy is in place, executives should ensure operational processes align with strategic intent and champions should focus on change and project management. For example, organizations should identify which stakeholders will be most affected by new working capital management processes, as well as which stakeholders are most (or least) supportive of the change. Those who
are highly affected and highly supportive can serve as change agents; those who are highly affected but not sold on the change can become the focal points of communications efforts. These nuts-and-bolts considerations—as well as the vision and strategy examples provided in this section of the report—can help transform working capital management concepts into processes that generate sustainable value.

ANALYTICS AND MEASURES

Finding 5: Best-practice organizations use data from an ERP system to inform daily credit and collection activities.

An enterprise resource planning system can significantly improve an organization’s ability to accelerate cash inflow. For example, Owens-Illinois uses a global ERP system to make day-to-day decisions about customers and credit. Its shared services team participated in ERP training to become self-sufficient in data access and report generation and then adopted a global ERP system to ensure immediate access to the data needed to make critical decisions. SAP allows Owens-Illinois to accumulate information globally and provides a cross-functional view of a customer’s history with insight into its payment habits. The standardized ERP also eliminates the challenges that come with each region being on a disparate system; data can now be measured globally and consistently.

Owens-Illinois’ finance team also uses a Business Objects report writing tool to generate information that helps credit and collections staff prioritize their analyses and interventions when customer payment patterns signal trouble. The team uses the tool without IT support and is able to create simple reports that can be refreshed in real time. The ability to have up-to-date data helps when teams interact with sales managers and with customers.

Owens-Illinois uses these tools to raise working capital intelligence throughout the organization and to facilitate better decisions that may affect working capital.

Finding 6: Best-practice organizations conduct real-time analysis of cash flow drivers to ensure reliable forecasts and optimize spare cash.

Too many organizations confine their cash flow forecasting routines to the annual planning process and fail to cascade actual cash flow patterns that are (or could be) extracted and analyzed from monthly or shorter-term views of financial
performance. They miss the opportunity for early and predictive diagnosis of potential problems and ultimate financial outcomes.

As discussed above, Zappos.com employees from treasury, FP&A, and accounting meet monthly to compare and compile their financial data (forecasted cash inflows and outflows versus actual, such as free cash flow per unit sold). Forecasts are then adjusted accordingly based on this review.

Free cash flow is an important measure to Zappos.com and to its parent company, Amazon. The financial planning and analysis team establishes a financial plan at the beginning of the year, monitors the progress toward cash flow goals each month, and finally adjusts the forecast based on daily sales receipts and cash outflow data. The treasury department prepares daily cash positioning snapshot reports every morning to ensure senior executives are aware of the status of operating cash and investments.

**Finding 7: Best-practice organizations measure, analyze, and advise operating units on how to increase the return on working capital invested in operations.**

Finance staff are the primary people in any organization that are typically the most concerned about working capital and cash flow, but all functions across an organization affect the current and future patterns for capital and cash flow. The best-practice organizations in this study measure performance among their functions, look for opportunities to improve, and educate employees on their roles in working capital management.

General Mills educates its business units on how efficiently they use their working capital. The finance function calculates the return on capital by incorporating both working capital and a unit’s fixed asset investments. More specifically, the accounting metric allocates working capital, productive assets, and physical assets by business unit and then calculates the quarterly return on capital based on expected reported profit. This allows the function to illustrate working capital utilization costs and advise those units on how to improve their returns. The results are useful to corporate and the business units, although the organization realizes that the profit piece of the equation overshadows changes in working capital. Because of that, General Mills wants to help inform its business units through additional metrics that measure each business unit’s inventory, management effectiveness concerning inventories, and prediction accuracy for necessary capital expenditures.

Owens-Illinois realized that some of its management team members, who were not finance professionals by training, did not fully understand the dynamics of working capital. For example, one operating manager assumed that working capital could be
optimized if he merely ordered factories under his control to invoice customers for inventory at the end of a month. Soon thereafter, the finance team developed an easy-to-understand training curriculum to ensure that all employees understand this concept and how they affect working capital. The organization used a simple format to explain working capital (e.g., pie charts by region and the use of analogies to describe the details) and tied it to financial incentives to drive employees’ desires to understand the concept.

Zappos.com has identified five key cross-functional business drivers that ensure organizational success and ultimately translate into optimal working capital levels. For example, one measure of the health of organizational culture is a net promoter score that ultimately affects revenue. In addition, the organization also closely tracks site downtime. Other key business drivers include profit margins and pricing, merchandising stock-out rates, and shipping costs and operating expenses as a percentage of sales. These key business drivers are reviewed closely during the weekly operational control committee meetings and communicated throughout the organization.

Zappos.com also conducts monthly manager meetings (for executive, senior, and middle managers and occasionally supervisors) to assess financial performance, review forecast and actual performance, review sales plans, discuss anticipated shortfalls, and analyze cross-functional metrics. These meetings align managers with overall financial goals and encourage managers to share the key themes and information with their teams in a meaningful way. In addition to a financial and sales discussion, these meetings organize “Pipeline Classes” (directed to potential future leaders) that help managers communicate financial goals, metrics, and their alignment with organizational strategy to their teams.

Finding 8: Best-practice organizations design custom measures of working capital that are relevant to their business models.

This study found seven building blocks to successfully measure and manage working capital:

1. defined metrics,
2. a timely reporting schedule,
3. accountability for results,
4. a cross-functional perspective,
5. frequent summaries for executives,
6. automated systems for reporting and analytics, and
7. benchmarks for process performance.

This finding details best practices for each of these seven building blocks.
In terms of defined metrics, Owens-Illinois has key ones such as DSO that it keeps simple in order to assess the performance of each process involved in working capital management. Examples follow.

- Average days deficient—DSO, or days sales outstanding, is oftentimes dictated by the business and markets. O-I tends to focus more intently on average days deficient (ADD), which allows the company to evaluate how many of its receivables are deficient at the end of each month. ADD is the difference between the DSO and best possible DSO, which is when all customers pay consistent with the contractual terms. From a finance perspective, it is an easy metric to understand; however, the challenge for the sales organization is to take ownership. Despite this challenge, the company has made a lot of progress in this area and has successfully met its goal of keeping ADD to less than one day. Figure 4 shows the steady decline in ADD from just over four and half days in 2006 to less than one day in 2010.

![Owens-Illinois Measure of Average Days Deficient](image)

Figure 4
Past-due invoices—To track the amount of past due invoices, Owens-Illinois created the percent past due metric. O-I sets out to make its metrics fair to customers and its goals attainable. For example, O-I realizes that, at times, invoice processing and payment by customers can be hampered by delays in processing credits. For this reason, O-I initiates corrective actions only when three days have passed since the invoice due date. This three-day window accounts for the weekend, as well as delivery and shipping time. Credit analysts are measured on the number of invoices more than three days past due. Moreover, the accounts receivable team communicates closely and regularly with sales managers to understand what’s occurring and intervene if a key customer’s payment patterns are deteriorating.

Days beyond terms—The final component on the KPI report for accounts receivable is the customer metric days beyond terms (DBT). This metric was created to provide each general manager and his or her senior sales managers with visibility into the top 10 customers, their terms, and how they are paying against those terms.

Procurement card percentage of spend—Owens-Illinois tries to work in a collaborative, win-win mode with its supply base. Several programs were rolled out to facilitate this. For instance, the procurement team implemented a procurement card program through which purchases are paid for with a credit card (P-card) or invoices are paid directly by JPMorgan. The benefit to O-I is increased processing efficiencies and reduction in processing costs (because there are fewer invoices to process). When O-I uses JP Morgan to pay invoices, O-I is billed; this process increases its cash flow and provides a cash incentive paid as annual spend targets are achieved. Although this program accounts for only 3.5 percent of the company’s total spend, the team continues to seek additional partners to join the program. With the right controls in place and a quick setup process, Owens-Illinois is confident that it can trust employees with P-card procurement privileges.

Zappos.com makes an effort to fully scrutinize its AP matching process and drill down into drivers of variances and issues concerning three-way matches and receivables. Figure 5 on page 29 summarizes results for some of the working capital metrics the operational control committee reviews on a regular basis.
Zappos.com Key Performance Indicators

<table>
<thead>
<tr>
<th>Key Performance Indicator</th>
<th>Jan-10</th>
<th>Feb-10</th>
<th>Mar-10</th>
<th>Apr-10</th>
<th>May-10</th>
<th>Jun-10</th>
</tr>
</thead>
<tbody>
<tr>
<td>Inventory Turn</td>
<td>2.69</td>
<td>2.38</td>
<td>2.56</td>
<td>2.39</td>
<td>2.66</td>
<td>2.30</td>
</tr>
<tr>
<td>DIO-Days of Inventory Out</td>
<td>136</td>
<td>141</td>
<td>151</td>
<td>154</td>
<td>138</td>
<td>154</td>
</tr>
<tr>
<td>DSO-Days of Sales Out</td>
<td>3</td>
<td>5</td>
<td>2</td>
<td>3</td>
<td>5</td>
<td>4</td>
</tr>
<tr>
<td>DPO-Days of Payables Out</td>
<td>46</td>
<td>52</td>
<td>59</td>
<td>55</td>
<td>53</td>
<td>56</td>
</tr>
</tbody>
</table>

Figure 5

- Inventory turn—Considering that the company warehouses everything it sells online, this ratio helps monitor the health and aging of inventory at a high level and as a measure of year-over-year improvement. Merchandising closely monitors more in-depth product category and LPN (unit) aging.

- Days of inventory out (DIO)—Zappos.com has improved remarkably over the last year on this metric (in June 2009 DIO was 200-plus days), largely because of the success of its liquidation channel 6pm.com. Because it sells discounted and aged inventory, 6pm.com has a very different business model than Zappos.com does. For instance, it charges customers for shipping and has a 30-day return policy. Prior to the acquisition by Amazon.com, the aging of inventory and DIO was a significant concern for Zappos.com because it was a net borrower and depended on a revolving line of credit secured on the liquidation value of inventory as collateral. Because Zappos.com’s sales are cyclical, with most sales occurring in the fourth-quarter holiday season, the organization tended to have a shortage of cash during the second- and third-quarter inventory ramp-up every year, so it relied heavily on the revolving line of credit. Since the acquisition by Amazon.com, however, Zappos.com has become a net investor, and DIO is not nearly as much of a concern today. The organization still strives to maintain a healthy level of inventory, though, and not let it age too much.

- Days of sales outstanding (DSO)—Zappos.com naturally has a low DSO because most of its payments are made by credit card and alternate methods like PayPal and Bill MeLater. Zappos.com has a large focus on charge-backs and a team dedicated to maintaining or keeping track of charge-back volume. This team also monitors fraud statistics/fraud detection rates. Each week it provides the status of orders reviewed and, of those orders reviewed, orders that were...
cancelled because they were deemed high-risk. Currently, the charge-back volume is below 0.2 percent of gross sales; industry norm is approx 0.5 percent.

- Days of payables outstanding (DPO)—Zappos.com focuses on this metric much more than on DSO. The organization purchases in advance everything that it sells on the Web site.

General Mills reports return on capital metrics at the divisional level to help divisional leaders make better business decisions and drive home the impact that the divisions have on overall corporate working capital levels. An advantage of this approach is that the divisional ROC metrics offer a complete measure of performance related to the overall corporate return on capital. On the other hand, divisional ROC metrics are more responsive to changes in profit generation and fixed asset investment than to changes in working capital and are difficult to report more frequently than quarterly because of the complex calculations.

To drive more actionable behavior at the business unit level, finance also monitors and measures controllable working capital (e.g., inventory) along with capital expenditures (investment balance) at the divisional level. Each division can directly impact the controllable working capital metric, and General Mills has found that the metric helps the divisions understand their influence on working capital levels. The controllable working capital metric is then combined with a capital expenditure metric to give the divisions the equivalent of an “investment balance,” or the overall capital at play in the division. The investment balance metric highlights a cash flow trade-off: Divisions that lower their working capital levels and inventory could potentially have more capital expenditures at their disposal (e.g., less inventory means more capital spent, and vice versa). These measures motivate the divisions to pay close attention to inventory levels, and they are built into their divisional performance measures and reported as part of the supply chain results.

In terms of a timely reporting schedule, Zappos.com maintains weekly accounts payable metrics, including invoice count, paper versus electronic data interchange (EDI), weekly invoice parked/posted volumes, new vendor setups, and three-way match metrics. Figure 6 on page 31 summarizes some of the company’s key accounts payable metrics. Zappos.com determines through daily and weekly monitoring of these important metrics what it needs to improve.
Zappos.com Regular Accounts Payable Metrics

<table>
<thead>
<tr>
<th>Metric</th>
<th>Expense</th>
<th>Trade</th>
<th>Manual</th>
<th>EDI</th>
</tr>
</thead>
<tbody>
<tr>
<td># of Trade Invoices Entered</td>
<td></td>
<td></td>
<td>Manual</td>
<td>EDI</td>
</tr>
<tr>
<td># of Expense Invoices Entered</td>
<td></td>
<td></td>
<td>Expense</td>
<td>Trade</td>
</tr>
<tr>
<td>Unmatched Invoices</td>
<td></td>
<td></td>
<td>Expense</td>
<td>Trade</td>
</tr>
<tr>
<td>AP Head Count</td>
<td></td>
<td></td>
<td>Expense</td>
<td>Trade</td>
</tr>
<tr>
<td>New Vendors Added</td>
<td></td>
<td></td>
<td>Expense</td>
<td>Trade</td>
</tr>
<tr>
<td>Total Vendors</td>
<td></td>
<td></td>
<td>Expense</td>
<td>Trade</td>
</tr>
<tr>
<td>Purchase Orders Created</td>
<td></td>
<td></td>
<td>Expense</td>
<td>Trade</td>
</tr>
<tr>
<td>Purchase Orders Changes</td>
<td></td>
<td></td>
<td>Expense</td>
<td>Trade</td>
</tr>
<tr>
<td>Total Purchase Orders Changes</td>
<td></td>
<td></td>
<td>Expense</td>
<td>Trade</td>
</tr>
<tr>
<td>Prior to Ship Date</td>
<td></td>
<td></td>
<td>Trade</td>
<td></td>
</tr>
<tr>
<td>After Ship/Prior to Cancel</td>
<td></td>
<td></td>
<td>Trade</td>
<td></td>
</tr>
<tr>
<td>After Cancel</td>
<td></td>
<td></td>
<td>Trade</td>
<td></td>
</tr>
<tr>
<td>Aged Unmatched and Unpaid Invoices</td>
<td></td>
<td></td>
<td>Trade</td>
<td></td>
</tr>
<tr>
<td>Units in FC Exception Area</td>
<td></td>
<td></td>
<td>Trade</td>
<td></td>
</tr>
<tr>
<td>Aged Unmatched GR</td>
<td></td>
<td></td>
<td>Trade</td>
<td></td>
</tr>
<tr>
<td>Inventory Shrink in Units</td>
<td></td>
<td></td>
<td>Trade</td>
<td></td>
</tr>
</tbody>
</table>

Figure 6

Owens-Illinois promptly reports its key performance indicators on a recurring basis (monthly and quarterly) to its management and business units to ensure working capital management is a pertinent subject for all employees. For instance, on the seventh working day after a month closes, a sales manager will receive an accounts receivable trends report. Owens-Illinois’ adoption of P-cards has further improved the predictability of its reporting schedule and has allowed suppliers to track when payments will arrive. Its predictable schedule also allows the organization to fast-track invoices that offer discounts.

In terms of accountability for results, the best-practice organizations tie metrics into performance incentives and hold employees and business units financially accountable.

For example, General Mills aligns management incentive metrics with these value drivers:

- net sales growth,
- segment operating profit growth,
- diluted earnings per share growth, and
- return on capital improvement.
Performance metrics are important to Owens-Illinois. It holds all levels accountable for working capital. For example, if there is a three-way-match failure (because, for instance, purchase order data disagrees with data shown on shipping documents or on an invoice), then the organization charges the amount of the lost discount back to the responsible operating unit. This level of accountability has resulted in a 91 percent salvage rate, as the locations are motivated to avoid charge-backs.

In addition, general managers and sales staff receive a one-page performance report; if any measure underperforms, this report alerts owners to immediately remedy the issue.

As shown in Figure 7, Owens-Illinois employees are held accountable for reaching their goals; they communicate the issues to management ahead of time because they are being measured. The emphasis on measures helps the organization stay in control and active in correcting issues. Owens-Illinois sets goals that are achievable, easy to understand, and relevant for the markets. Initially, the North American team was not able to review invoices more than three days past due, so it set a reasonable measure to review invoices based on a declining number of days. This allows the region to have early successes because the goal makes sense for its environment, and it can impact the results.

![Owens-Illinois Individual Measures of Past Due Over Three Days](image)

**Figure 7**

Past Due Invoices > 3 Days/Accounts Receivable Balance

<table>
<thead>
<tr>
<th></th>
<th>Amy</th>
<th>Nancy</th>
<th>Susan</th>
<th>Lisa</th>
<th>Rila</th>
</tr>
</thead>
<tbody>
<tr>
<td>JUN 08</td>
<td>5.0%</td>
<td>2.9%</td>
<td>5.3%</td>
<td>3.0%</td>
<td>3.2%</td>
</tr>
<tr>
<td>DEC 09</td>
<td>3.8%</td>
<td>3.8%</td>
<td>2.1%</td>
<td>4.7%</td>
<td>2.2%</td>
</tr>
<tr>
<td>JUN 10</td>
<td>2.8%</td>
<td>1.3%</td>
<td>1.8%</td>
<td>2.9%</td>
<td>1.5%</td>
</tr>
<tr>
<td>GOAL</td>
<td>4.0%</td>
<td>2.5%</td>
<td>3.4%</td>
<td>3.0%</td>
<td>2.1%</td>
</tr>
</tbody>
</table>
In terms of a cross-functional perspective, the best-practice organizations highlight key metrics for business units and identify cross-functional drivers that can affect working capital. When it comes to senior management reports, the organizations succinctly summarize the most pertinent and accurate working capital metrics for executives to review frequently.

For example, the treasury department at Zappos.com prepares daily cash positioning snapshot reports for senior executives to review the status of operating cash and investments. And executives review key performance indicators—such as net promoter scores, site downtime, profit margins and pricing, merchandising stock-out rates, and shipping costs and operating expenses as a percentage of sales—during the weekly operational control committee meetings.

Owens-Illinois also generates monthly one-page reports detailing key performance indicators for processes such as accounts receivable (Figure 8). This simple format helps managers quickly assess the full picture.

### Owens-Illinois Accounts Receivable Report

<table>
<thead>
<tr>
<th>2010 AR TRENDS</th>
<th>DEC 2009</th>
<th>JAN</th>
<th>FEB</th>
<th>MAR</th>
<th>APR</th>
<th>MAY</th>
<th>JUN</th>
</tr>
</thead>
<tbody>
<tr>
<td>DSO</td>
<td>10.2</td>
<td>15.3</td>
<td>16.2</td>
<td>16.4</td>
<td>16.3</td>
<td>16.9</td>
<td>18.0</td>
</tr>
<tr>
<td>BPDSO Best Possible DSO</td>
<td>9.6</td>
<td>15.6</td>
<td>15.2</td>
<td>16.4</td>
<td>16.7</td>
<td>16.5</td>
<td>17.6</td>
</tr>
<tr>
<td>ADD Average Days Deficient</td>
<td>0.5</td>
<td>(0.5)</td>
<td>1.0</td>
<td>0.1</td>
<td>(0.4)</td>
<td>0.5</td>
<td>0.4</td>
</tr>
<tr>
<td>SMM</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sales</td>
<td>131.0</td>
<td>127.5</td>
<td>123.7</td>
<td>142.2</td>
<td>142.1</td>
<td>153.9</td>
<td>157.1</td>
</tr>
<tr>
<td>Receivable Balance*</td>
<td>46.1</td>
<td>66.0</td>
<td>67.9</td>
<td>72.9</td>
<td>77.4</td>
<td>82.2</td>
<td>93.2</td>
</tr>
<tr>
<td>Past Due Invoices &gt; 3 Days</td>
<td>0.9</td>
<td>1.6</td>
<td>2.9</td>
<td>1.2</td>
<td>0.7</td>
<td>1.5</td>
<td>2.1</td>
</tr>
<tr>
<td>% Past Due Invoices &gt; 3 Days</td>
<td>2.0%</td>
<td>2.7%</td>
<td>4.2%</td>
<td>1.7%</td>
<td>0.9%</td>
<td>1.7%</td>
<td>2.2%</td>
</tr>
<tr>
<td>Customer Deductions</td>
<td>0.6</td>
<td>0.8</td>
<td>1.2</td>
<td>0.8</td>
<td>1.0</td>
<td>1.3</td>
<td>1.5</td>
</tr>
<tr>
<td>% Customer Deductions</td>
<td>1.4%</td>
<td>1.2%</td>
<td>1.6%</td>
<td>1.1%</td>
<td>1.3%</td>
<td>1.6%</td>
<td>1.6%</td>
</tr>
</tbody>
</table>

*Trade Receivables Only

---

**Figure 8**
Zappos.com provides an excellent example of automated systems for reporting and analytics through its PEHZ (purchase exception handling at Zappos.com) project.

A metrics review at Zappos.com indicated a spike in the volume of three-way match discrepancies and failures. These occurrences were disturbing the warehouse’s work flows and causing delays in selling products online. They also were increasing the warehouse labor required to handle the exceptions, since the exceptions had to be diverted from the receiving dock onto an exception lane. The organization found that these exceptions were ultimately a driving factor in the treasury group’s inability to effectively forecast and manage cash flow. In response, Zappos.com initiated the PEHZ project to:

- implement an automated work flow to communicate and expedite the early resolution of purchasing, receiving, and invoicing exceptions;
- enhance buyer tools used in the purchasing process by providing up-to-date information;
- introduce new EDI transactions (e.g., purchase order acknowledgement and change orders) to improve communications between the buyer and the vendor for the purchase-to-pay cycle and to address mismatch problems early; and
- improve roles, access, and security controls for the vendor portal, thus allowing vendors and sales representatives to view their sales volumes, accounts payable invoices, and exceptions data.

The new EDI transactions shift the negotiations and “sync-ups” between the vendor and Zappos.com upfront, while the purchase is being created, which should help the organization more effectively manage cash flow. Ultimately, Zappos.com anticipates that the PEHZ project will reduce the quantity of purchasing and receiving exceptions by 75 percent. In addition, as part of the PEHZ project, Zappos.com is able to automate the sending of purchase and change orders through e-mail, EDI, and the vendor portal. (This involves vendors earlier in the exception resolution process, rather than the resolution falling primarily on Zappos.com finance and warehouse receiving staff.) The PEHZ project should also improve the invoice reconciliation process by 85 percent, which significantly affects the accounts payable process. Improved communications and resolution of three-way match discrepancies via the automated work flow, as well as implementation of processes for addressing exceptions upstream, will cause the number of unmatched goods receipts to drop. This will allow invoices to be processed faster and reduce “stock-outs” on the Web site.

Finally, best-practice organizations in this study regularly benchmark for process performance. Benchmarking and competitive intelligence capabilities help these organizations regularly measure their working capital management processes against their peers'.
Owens-Illinois annually benchmarks its processes in hopes of learning new and innovative techniques for working capital management. It understands the need for continued improvement and is committed to exploring new tools and techniques to facilitate better process controls and growth. Owens-Illinois at one stage invited a third-party AP auditor to review its payables process quality.

As part of its continuous process improvement efforts, General Mills benchmarks its overall working capital performance against that of its peer set and the S&P 500 Food Group peers. It also reviews trends on an annual basis. Ideally, the company likes to see at least a 50 basis point improvement in ROC from year to year. The results are used to develop working capital targets for the following year and to set process improvement action plans. Finance constructs the peer benchmarks based on publicly available data (e.g., financial and earnings statements, earnings calls, and investment presentations) and through relationships with benchmarking data suppliers such as APQC or the Corporate Executive Board.

**PROTIVITI RESEARCH CHAMPION PERSPECTIVE**

Although all of the findings in this report are vital, those in this section warrant the lengthiest discussion, for good reason. The identification of relevant data, drivers, and measures to enable effective decision making represents the core purpose of managing working capital. This identification process also marks an area that is ripe for errors that are due, in part, to a widespread tendency to over-measure.

The organizations featured in this report took a wise approach to working capital measurements by starting small. Doing so enabled them to measure the right value drivers and then act on the results to demonstrate success before expanding their analytics efforts. To this end, the seven building blocks to successfully measuring and managing working capital (page 20) and the practical illustrations of Finding 8 (custom measures, page 29) offer particularly valuable guidance. Zappos, for example, focuses on days of payables outstanding (DPO) more so than days of sales outstanding (DSO) because it purchases and warehouses its goods in advance of sales.

Zappos’ approach underscores the importance of selecting metrics that apply to the unique aspects of each business model and value chain. Once organizations identify which measures are most relevant, they can use this information to advise operating units on how to optimize working capital invested there. For example, measures relevant to working capital invested in the order-to-cash cycle may include DSO, invoice error rates and other processing costs, unauthorized deductions, and uncollectible accounts receivable (AR).

Once these measures have been selected, the following steps should occur:

- data should be collected, normalized, and cleansed,
- business processes should be mapped and benchmarked,
- gaps and opportunities for improvement should be identified, and
working capital management champions should work with stakeholders to conduct improvements.

This type of collaboration pervades at General Mills, where the finance team regularly partners with business units on working capital improvements through an ongoing education effort focused on the value of monitoring working capital measures. The organization’s finance function allocates working capital, productive assets, and physical assets by business unit and then calculates the quarterly return on capital based on expected profit. By doing so, the finance function pinpoints opportunities to improve returns on working capital utilization costs.

The focus on relevant metrics described in this section can help all organizations, regardless of the sophistication of their working capital measurement capabilities, overcome the tendency to over-measure and, therefore, underperform.

PROCESS IMPROVEMENT AND PRACTICES

Finding 9: Best-practice organizations apply quality and productivity tools to process improvement efforts in finance.

Although it is uncommon to see Six Sigma principles applied to the finance function, Owens-Illinois applies its Lean Six Sigma model (Figure 9, page 37) to its back-office and administrative processes. Lean Six Sigma has helped the organization reduce waste and improve the performance of critical customer (internal and external) requirements that affect its working capital. A key component of the Lean Six Sigma process was the use of Kaizen events. Kaizen events allow a cross-functional team to meet in one location to map out a business process in an effort to “lean it out” and make it better. These events also help to break down silos by allowing teams to understand the total process.

Kaizen events for the accounts payable process have focused on lost discounts, matching exceptions, check printing, scanning and verification processes, and invoice processing. Kaizen events for accounts receivable have focused on unearned discounts, lockbox feasibility, and credit approval. For example, one Kaizen event focused on customer discount controls. Through Lean Six Sigma collaboration, the team was able to conduct a deep-dive analysis of the existing process to understand the root causes of problems and identify opportunities to re-engineer and improve the process. Thanks to the efforts of this team, the company was able to save $1 million.

The best-practice organizations in this study applied core change management principles—such as regular communication and training—to their efforts to improve working capital management and cash flow intelligence. Although change management principles are well-known, it is a best-practice distinction for them to be applied in a working capital context. Zappos.com provides an excellent example.

Senior leaders at Zappos.com follow the foundational principles of change management for large-scale changes such as being acquired by Amazon, as well as functional-scale changes such as the PEHZ project. In fact, the organization created a full-time senior manager of change management position. This new director was previously the senior manager of accounting operations, and this helps tie change management to finance. The change management department is housed inside of Zappos.com’s project management department.

Zappos.com endeavors to have successful processes for implementing business process improvements, change management strategies, work force training, and workplace communications and to ensure that the corporate core values are part of
each organizational change initiative. Dedicated solution analysts (similar to business or technical analysts at other organizations) fully document all steps of existing processes prior to engaging in any significant project or change effort, recognizing that the organization is rapidly growing and, therefore, processes change quickly. Zappos.com incorporates a number of activities—such as project kickoff parties, focus groups, surveys, and videos—to engage employees and secure their buy-in. In addition, the organization recognizes external project stakeholders including vendors, freight carriers, and customers.

Zappos.com also educates external subject matter experts hired for particular projects to ensure they understand their responsibilities and the duration of the project. The organization trains and communicates with affected employees to ensure that they understand and accept the reasons for the project. To this end, the senior manager of change management spends a large percentage of her time making presentations across departments on all types of projects and initiatives.

The senior manager of change management believes that employees need to understand what organizational or business goals will be achieved by the change for it to be successful. To accomplish this, the change management department works with directors and senior managers to show staff members how the change will make their jobs easier, to help them understand and accept their roles in using the new system or process, and to push them to a higher level and expose them to new opportunities.

Focusing specifically on finance, all Zappos.com employees are trained concerning their roles in and impact on working capital management. This training includes finance classes that cover the basics of financial statements and Sarbanes-Oxley. The courses also address how the business units contribute to the company’s mission and growth and how individuals can affect key business outcomes.

Finding 11: Best-practice organizations identify and resolve data discrepancies on the front end of the process.

Described in Finding 8, the PEHZ project at Zappos.com helps the organization resolve exceptions up front in its interactions with suppliers. The PEHZ project curtails three-way match discrepancies and failures through four steps:

1. Automate communications to expedite the early resolution of purchasing, receiving, and invoicing exceptions.
2. Enable the buyer to make more educated decisions and have access to up-to-date information regarding purchases.
3. Introduce new EDI transactions to improve communications between the buyer and the vendor for the purchase-to-pay cycle. These transactions
include purchase order creation, acknowledgments, and change orders; advanced shipping notices; and invoices. This will further synchronize Zappos.com and vendor systems, well before the goods are delivered to the Zappos.com docks. In the past, the organization didn’t realize it had a problem until the invoice was due and in some cases when the invoice was past due.

4. Improve roles, access, and security controls for the vendor portal. This allows vendors and sales representatives to view their sales volumes, accounts payable invoices, and exceptions data and help resolve their own exceptions.

The ultimate goal is to get the product to the shelves, sell it as quickly as possible, and provide timely payments to the vendors. For this to happen, up front resolutions with vendors are key.

**Leading Practices in Accounts Payable**

- Multiple settlement methods—This includes P-cards, evaluated receipt settlement, payables factoring, and dynamic discounting. Owens-Illinois and General Mills use P-cards for small-dollar purchases, which frees up staff to focus on larger transactions and gets vendors paid quickly.

- Discount optimization—General Mills uses a third-party to make it easy for vendors to see if their invoices have been approved for early payment in exchange for discounts, a practice that can lessen cash flow pressure on vendors while also letting the company extend its terms (a bank plays an intermediary role by paying the vendor sooner than General Mills would).

- E-payables—Zappos.com uses EDI feeds for purchase order creation, change orders, and acknowledgments; advanced shipping notices; and various electronic payment mechanisms. This helps it automate the AP work flow.

- Payables factoring—General Mills extended its payment terms and then allowed vendors to collect payment at whatever period they want at whatever applicable discount for those funds.

- Standardize supplier payments—Owens-Illinois generates checks twice a month and works to employ rational payment terms.

**Finding 12: Best-practice organizations manage working capital risk.**

Working capital and cash flow intelligence can act as a central risk management tool. The best-practice organizations in this study leverage their working capital metrics to anticipate and manage supply chain and inventory risks. General Mills provides
an excellent example of how an organization can drill down into the drivers of change in working capital.

The company conducts monthly working capital reviews, established in 2007 and led by the controller, to bring together the vice presidents and directors with working capital operating authority to discuss the company’s performance across a number of dimensions.

Example action items from the reviews are confirming progress on working capital improvement projects, revising cash flow projections that feed into treasury’s cash management strategies, and revisiting the risk balance between exceptional customer service and inventory investment. For example, there is a careful balance between having enough inventory in stock for the sales organization to be able to continuously sell and ship product to customers and having too much inventory on hand that sits idle. The monthly reviews and resulting action items generally provide enough lead time to make needed adjustments to optimize working capital management.

PRO TIVITI RESEARCH CHAMPION PERSPECTIVE

Owens-Illinois applies Lean Six Sigma principles (in a highly innovative way) to flesh out the root causes of working capital–related inefficiencies, which provides significant savings. Zappos’ change-management rigor, which includes the assignment of a full-time senior change management position, has helped all employees better understand how their individual roles and responsibilities influence working capital management. Such examples demonstrate the benefits of a disciplined and continuous approach to working capital management improvement.

These examples help translate working capital process improvements into clear terms. For example, if an organization identifies invoice error rate as a key lever of working capital management improvement within the order-to-cash cycle, then it can reduce the error rate by:

- standardizing and consolidating invoicing processes,
- automating manual processes and/or more fully utilizing existing enterprise resource planning (ERP) system functionality, and/or
- improving the data integrity of customer master files.

The process improvement examples in this report also highlight an important link between working capital management and risk management. General Mills treats working capital and cash flow intelligence as a key risk management tool by using the information to identify issues (e.g., customer payment patterns that signal likely problems). By identifying, communicating, and monitoring relevant working capital measures, the organizations in this report demonstrate the benefits of integrating working capital management with performance management.
These efforts also confirm what Protiviti recently has witnessed in the field: More organizations, regardless of where they are on their growth curves, are integrating strategy, risk management, and performance management to improve their agility amid ongoing volatility and an increasingly complex operating environment.

By effectively identifying and communicating working capital risks across the enterprise, leading organizations are better positioned to monitor, manage, and when necessary, mitigate key strategic, operational, and credit risks.

**IT STRATEGY AND APPLICATION**

**Finding 13: Best-practice organizations embrace the concept of self-service to drive efficiency.**

All of the study’s best-practice organizations leverage automation to drive efficiency in working capital management. These tools require minimal IT support and allow finance and other staff and even vendors to access the information they need when they need it.

Owens-Illinois uses a Business Objects report writing tool that allows finance staff to generate reports in real time without IT staff intervention. These reports are populated by data derived from the organization’s ERP system using its global SAP implementation.

General Mills uses a Web portal to indicate to vendors which invoices are available for early payment; vendors then select options that appeal to them. In addition, the company’s treasury function leverages self-service tools to reduce workload and increase cash management efficiency by:

- detailing current-day cash positions through SAP,
- automating delivery of electronic bank statements five times a day, and
- automating cash flow postings to its general ledger.

Zappos.com has automated working capital management through the aforementioned PEHZ project, where the organization implemented an Oracle work flow engine and internally developed applications to enable communications among facilities, vendors, employees, and staff members as the organization grows. This capability facilitates effective management and resolution of work flow action items in a self-service delivery mode.
Finding 14: Best-practice organizations conduct transactions electronically whenever possible and work with vendors so they can do the same.

EDI and e-invoice management have become commonplace among finance functions. Trends are clearly leading to electronic transactions, and these best-practice organizations work to maximize their use in a way that benefits everyone involved.

Owens-Illinois values its vendor relationships. In an effort to streamline and simplify its work with vendors, the organization is implementing an evaluated receipt settlement (ERS), which will eliminate paper invoices and reduce its matching efforts from three pieces to two. ERS is a procedure for the automatic settlement of goods receipts. The major benefits of ERS include invoice variance prevention, the elimination of non-value-added work (e.g., tasks associated with reconciliation), and the opportunity cost of error-prone cash conversion. Sixty percent of the organization’s North American customer receipts are based on the ERS two-way match, with the remaining vendors soon to be paid electronically. Currently, 70 percent of all payments worldwide are made electronically. The key to this is EDI.

Zappos.com also relies on a high percentage of vendors using EDI. This has allowed the organization to reduce the quantity of purchasing and receiving exceptions by 75 percent. Specifically, Zappos.com has:

- improved the processes and exception handling for purchase order confirmations so that vendors must confirm prior to shipment,
- improved exception handling for advanced shipping notices,
- instituted automated processes for purchase order communication, and
- involved vendors in exception reporting and the solution process for work flow action items.

At General Mills, 73 percent of cash transactions (including invoicing and payments) are electronic. The organization’s working capital processes tend to be automated and digital, with widespread vendor involvement.
PROTIVITI RESEARCH CHAMPION PERSPECTIVE

Each of the three best-practices organizations featured in this report use supporting technology to increase the efficiency of their working capital management processes. It is also notable that these organizations established sound working capital management processes before introducing automation. The working capital management software market, which includes numerous AP and AR automation tools, is brimming with vendors. As with other business software investments, buyers should develop a specific set of requirements before shopping.

Enabling technology is just that: enabling. It is important to first establish a working capital management strategy, align operational processes with strategy, identify key value drivers or metrics, and demonstrate the value of these processes before trying to introduce technology to make improvements.

Overall, the 14 key findings presented in this report cover what Protiviti views as the six elements of effective working capital management:

1. Strategies and policies that align with corporate strategy
2. Processes that align with working capital management strategy
3. Organization and people, including executive-level support
4. Management reports that are based on relevant metrics and provide real-time visibility
5. Methodologies and tools, including benchmarking and process improvement approaches
6. Systems and data that support working capital management processes

A successful working capital management approach begins with the creation of an overall strategy and vision, which in turn drives policy. Clear, well-documented and standardized processes need to be in place and understood throughout the organization. Executive support, clearly defined roles and responsibilities, and training help establish working capital management as an ongoing corporate priority—rather than a reactive exercise conducted during economic downturns—and can foster a mindset that supports the reporting of timely, relevant, and actionable information. Finally, analytical methodologies and enabling technology should be in place to maintain a focus on continuous improvement and to support a balanced, risk-savvy view of working capital needs and trading partner relationships.

As this report shows, CFOs, controllers, treasurers, and other managers who treat working capital management as a strategic priority and as an ongoing business process that integrates with performance management and risk management processes can free up cash to fund strategic investments while delivering higher-than-expected results to shareholders.
Results

OWENS-ILLINOIS
Ed White, the CFO of Owens-Illinois, is pleased that the organization weathered the recession of 2008 and 2009 with relative ease. He credits much of this to process improvements in payables and receivables management. The organization was able to reduce inventories during the downturn and avoid extending payment terms at the expense of its suppliers. White said that Owens-Illinois had record-low working capital at the end of 2009 in absolute value. The organization reduced its working capital as a percentage of sales from more than 19 percent in 2006 to 16 percent in 2009. This was achieved through process improvements, metrics, benchmarking, and a high-performance culture.

ZAPPOS.COM
Zappos.com manages its working capital to serve its overarching strategic goals. To exemplify successful working capital practices and useful cash flow intelligence, the organization established processes for change management, process improvements, workforce training, and workplace communications. Consequently, its employees understand what needs to be achieved to optimize working capital. Performance and system metrics are part of everyday work. Key performance metrics are reviewed on a firm schedule by executives and the frontline employees who directly affect them. In addition, functions across the organization work together to manage working capital.

GENERAL MILLS
General Mills has leveraged its working capital management to boost its overall profitability. That is, improving its return on capital has increased its earnings growth and the efficient use of capital. General Mills achieved this success thanks to monthly working capital reviews, metrics, accounts receivable effectiveness, accounts payable efficiency, and supply chain finance intelligence. Working capital awareness is built into routine processes such as capital investment decisions and new product launches. And decisions flow into working capital targets, forecasts, and measures. Consequently, the organization finds itself leading in industry benchmarks, such as the accounts receivable measures detailed in Figures 10 and 11, page 45. (Note: anomalies in 2008 were tied to fluctuating commodity prices.) Ultimately, the organization can use these working capital improvements to fund growth.
Improving Working Capital Management and Cash Flow Intelligence

**General Mills Working Capital as a Percentage of Sales**

![Bar chart showing General Mills working capital as a percentage of sales for years 2005 to 2010.]

**Figure 10**

**General Mills Working Capital Measures**

- **Avg. Days Delinquent**
- **Collection Effectiveness**
- **Percentage Current**

![Bar charts showing General Mills working capital measures with different quartiles.]

*Source: NFHBC Mfrs Credit Group Benchmarking, 2Q 2010 (Food Sector)*

**Figure 11**
Call to Action

To improve working capital management and strengthen cash flow intelligence, organizations need a firm understanding of the multiple value drivers that exist across the cash conversion cycle and where improvements should be made to realize potential benefits.

At the highest level, value drivers represent factors that affect an organization’s ability to execute its strategy and create economic value. At a procedural level, value drivers refer to specific components—days sales outstanding (DSO), invoice error rates, days payables outstanding (DPO), accounts payable processing costs, days inventory outstanding (DIO), and inventory write-offs, to name several examples within the realm of working capital—that companies monitor and manage to execute their processes (e.g., working capital management), manage risks and, ultimately, generate greater shareholder value.

When considered collectively, the 14 key findings presented in this report suggest that companies can derive the greatest value from their working capital management processes by treating working capital management as a key component of an integrated approach to performance management, risk management and strategic management.

Based on these findings, there are four key calls to action for executives and managers intent on strengthening their company’s working capital management capabilities:

1. Align working capital management processes with corporate strategy, centralize financial transaction processing, cultivate cross-functional engagement, and provide sufficient executive-level support.
2. Identify relevant drivers of working capital management value and risks, and then use these drivers to develop metrics that complement the unique aspects of the company’s business model;
3. Commit to continuously improving working capital management processes through cross-functional engagement (i.e., ensuring that all employees understand how their activities influence working capital, benchmarking and executive-level support (e.g., assigning responsibility for process improvement).
4. Once working capital management strategy and processes are in place, use enabling technology to increase efficiency and support-related process improvements.

These findings have been culled from best-practice working capital management programs; as such, they beg an important question: How do management teams’ intent on developing working capital management best practices get started from a practical standpoint? The answer, like the key findings of this report, also comes in a four-stage approach.
First, companies should understand their current capabilities. They then should conduct the analysis within the selected business areas. Next, companies should recommend and design improvements identified in the previous step. And finally, companies should implement these improvements and then strive to sustain these new capabilities. These stages are depicted in figure 12 below.

The risk management component is important because working capital management practices and the sourcing, partner and channel management activities these practices feed qualify as process risks that must be monitored and managed. Leading working capital management practices also produce key performance measures that help managers monitor progress toward the achievement of performance objectives aligned with organizational strategy.

Companies with the most advanced working capital management capabilities treat working capital management as an opportunity to manage performance and risks in a way that supports the execution of strategic plans. By adapting the practices identified in this report to their company’s unique business model and by following the practical implementation steps described above, managers can make valuable contributions by helping their organization more effectively manage risk and drive greater shareholder value.
Methodology

Developed in 1993, APQC’s consortium benchmarking study methodology (Figure 13) serves as one of the world’s premier methods for successful benchmarking. It was recognized by the European Center for Total Quality Management in 1995 as first among 10 leading benchmarking organizations’ models. It is an extremely powerful tool for identifying best and innovative practices and for facilitating the transfer of these practices.

**APQC’s Four-Phase Methodology**

**PHASE 1: PLAN**

The planning phase of the study began in early 2010. During this phase, APQC conducted secondary research to help identify successful organizations that might participate as best-practice partners. The APQC team conducted telephone screening interviews with a subset of these organizations to uncover best practices. These organizations were selected for their successful practices in improving working capital management and cash flow intelligence.

A study kickoff meeting was held in July 2010, during which the sponsors refined the study scope, gave input on the site visit discussion guide, and reviewed information about the candidate best-practice organizations. The sponsors confirmed three organizations they wished to continue to study as “best-practice” partners: General Mills, Inc; Owens-Illinois, Inc; and Zappos.com, Inc.

Finalizing the site visit discussion guide concluded the planning phase of the study.
PHASE 2: COLLECT

The three best-practice organizations selected for continued participation in the study hosted virtual site visits in August 2010, attended by study participants. The study team prepared a written report (case study) of each site visit and submitted it to the partner organization for approval or clarification.

PHASE 3: ANALYZE

Working with research champion Protiviti, APQC analyzed the qualitative information obtained through the virtual site visits. The analysis concentrated on examining the critical success factors and challenges that organizations face in the study scope areas.

PHASE 4: ADAPT

Adaptation and improvement, stemming from identified best practices, occur after the sponsors apply key findings to their own operations. APQC staff members are available to help sponsors create action plans appropriate for their organizations.
Case Study
General Mills, Inc.

BACKGROUND
General Mills is the world’s sixth-largest food manufacturer, with over $16 billion in sales and more than 30,000 employees as of fiscal year 2010. The organization markets products in more than 100 countries.

General Mills is composed of three business segments:
1. U.S. retail segment, $10.3 billion in sales. Includes brands such as Cheerios, Lucky Charms, Yoplait, Hamburger Helper, Progresso, and Green Giant.
2. Bakeries and food service segment, $1.8 billion in sales. Markets ingredients and finished products, including Nature Valley granola bars, Chex Mix, and Bugles.
3. International business, $3.9 billion in sales, including joint ventures. Includes internationally marketed products such as Nestle, Old El Paso, and Haagen-Dazs.

The supply chain organization is a centralized group with functions in sourcing, manufacturing, and distributing products. The vice president for finance, supply chain was the primary host of the virtual site visit. As his group is responsible for the U.S. retail and bakeries and food services segments, the primary focus of the virtual site visit summary was General Mills’ domestic business.

VISION AND STRATEGY FOR IMPROVING WORKING CAPITAL MANAGEMENT

Our vision for and the way that we communicate with employees throughout the organization about working capital is that working capital improvements can fund future growth. Our underlying objective is continuous improvement in return on capital.

—Jerry Young, Vice President for Finance, Supply Chain
Ownership and Accountability for Working Capital Management
While the CFO is ultimately responsible for overall working capital management, responsibility for its different elements is decentralized. The company’s working capital management strategy is to set goals, establish clear accountability, guide business decisions, and measure results. Effective execution of this strategy requires cross-functional collaboration and coordination among the following individuals:

- corporate controller—responsible for working capital measurement, coordination, and metrics;
- treasury—responsible for cash management;
- finance vice president, sales—responsible for accounts receivable (collection and cash application activities);
- finance vice president, supply chain—responsible for accounts payable, inventory, and fixed assets; and
- shared services director—responsible for accounts payable processing.

These individuals manage working capital in a matrixed organizational structure. Centralized functions such as the controller’s office, supply chain, and treasury provide service and guidance to the business units.

**Finance Strategic Priorities**

The General Mills finance organization is guided by five strategic priorities:

1. business performance management,
2. globalization,
3. capital utilization,
4. portfolio management, and
5. people and organization.

Working capital management is a significant component of effective capital utilization. These strategic priorities determine how General Mills engages in working capital management between business units and within the finance function itself.

**Alignment with Organizational Strategy**

General Mills’ corporate strategy for business growth focuses on five growth drivers:

1. brand building,
2. leading customer growth,
3. international expansion,
4. new product/market innovation, and
5. margin expansion.
These growth drivers impact the organization’s working capital position by changing its revenue and profit. For example, development of new products and new markets for existing products drives revenue growth, and holistic margin management drives efficiencies and generates additional profits. These profits can be reinvested into brand building, leading customer growth, and international expansion.

All of these growth drivers, and particularly international expansion and innovation, require capital investment. General Mills must demonstrate tight working capital management practices to grow its business and still drive shareholder value.

Overall, General Mills emphasizes that working capital improvements can fund business growth. The finance organization’s objective is therefore to continuously improve the company’s return on invested capital.

The link between working capital management and overall corporate growth is reinforced by the “virtuous capital cycle” (Figure 14, page 53), an educational visual shared within the treasury and finance organization.

Beginning at the top of Figure 14 on page 53 and moving clockwise, equity and credit investors provide capital to the company in various forms. General Mills uses that capital to fund international expansion, mergers and acquisitions, and other growth activities. If the company generates positive returns on its invested capital, it can return excess capital to its equity investors through share repurchases, dividends, and debt service. This leads to an increased share price for the equity investor and creates more interest among current and prospective investors for further investment in the organization. This visual is a constant reminder to the finance organization that effective capital management can fund business growth and create shareholder value, in a “virtuous” cycle of capital inflows and outflows.

**Ensuring Cross-functional Collaboration**

General Mills uses monthly controller-led reviews to ensure cross-functional collaboration in working capital management. These reviews were established in 2007 to bring together the vice presidents and directors with working capital operating authority to discuss the company’s performance, including a review of:

- working capital metrics compared with last year and the plan for the year, at domestic and international levels;
- receivables performance;
- payables performance;
- a review of business unit current assets and current liabilities;
- an overview of business performance and its impact on inventories;
- quarterly working capital implications versus targets; and
- a discussion of potential actions to achieve targets.
Improving Working Capital Management and Cash Flow Intelligence

The Virtuous Capital Cycle

Strong ROC delivers:
- Expected return to investors (WACC)
- Excess capital to return to equity investors (return in excess of WACC)

Equity and Credit Investors

Improve ROC
- Earnings growth
- Efficient use of capital

Share Repurchase
Dividends
Debt Service

Working Capital
CAPEX
M&A

GMI invests in efficient growth of business (ROC)

Equity and credit investors provide capital to GMI

Figure 14

Action items from the reviews could include confirming progress on working capital improvement projects, revising cash flow projections that impact treasury’s cash management strategies, and revisiting the risk balance between exceptional customer service and inventory investment. For example, there is a careful balance between having enough inventory to continuously sell and ship product to customers and having too much idle inventory. The monthly reviews and resulting action items generally provide enough lead time to make needed adjustments to optimize working capital management.

ANALYTICS AND MEASURES TO ENABLE BETTER WORKING CAPITAL MANAGEMENT

Management Incentive Metrics

General Mills leverages a number of working capital analytics and metrics. The vice president of finance, supply chain, believes the most important metrics relate to management incentive. Management incentive metrics align with shareholder value drivers such as net sales growth, segment operating profit growth, diluted earnings per share growth, and return on capital improvement. Managerial performance
ratings and incentive pay are tied to performance on these four metrics. The return on capital metric is a relatively recent addition to the slate of management incentive metrics. In addition to driving profit growth, it reinforces to the organization outside of finance the importance of return on capital investment.

Driving It Home at the Divisions

Finance also reports return on capital metrics at the divisional level. This helps divisional leaders make better business decisions and emphasizes the impact that the divisions have on corporate working capital levels. An advantage of this approach is that the divisional ROC metrics offer a complete measure of performance related to the overall corporate return on capital. On the other hand, divisional ROC metrics are more responsive to changes in profit generation and fixed asset investment than to changes in working capital and are difficult to report more frequently than quarterly because of the complex calculations.

To drive more action at the business unit level, finance also monitors and measures controllable working capital (e.g., inventory) along with capital expenditures (investment balance) at the divisional level. Each division has a direct impact on the controllable working capital metric, and General Mills has found the metric helps the divisions understand their influence on working capital levels. The controllable working capital metric is then combined with a capital expenditure metric to give the divisions the equivalent of an “investment balance,” or the overall capital at play in the division. The investment balance metric highlights a cash flow trade-off: divisions that lower their working capital levels and inventory could have more capital expenditures (e.g., less inventory means more capital spent, and vice versa). These metrics motivate the divisions to pay close attention to inventory levels, and they are built into divisional performance metrics and reported as part of the supply chain results.

Working Capital Implications in Analysis

Finance engages in a great deal of collaborative working capital planning and analysis. Capital investment decisions include an analysis of the impact of working capital on that investment. For example, if a proposed cost-savings initiative will reduce inventory levels, the anticipated working capital implications of the initiative are built into the net present value analysis. Similarly, if the initiative is a new product or new plant, the working capital implications of the proposed initiative are factored into the capacity and inventory planning analysis. These business decisions flow into working capital targets, forecasts, and measures. This working capital awareness of proposed initiatives is not automated; it is facilitated by finance’s participation on the business teams.
PERFORMANCE MANAGEMENT PRINCIPLES AND MEASURING PROCESS IMPROVEMENT

What works for us is the daily focus on measurement. When everyone is being measured, they have a significant incentive to make sure that things are resolved quickly and that we don’t have issues that might create a collection delinquency issue later on.

— Jerry Young, Vice President for Finance, Supply Chain

Accounts Receivable Process Improvement

General Mills regularly measures its performance on key working capital metrics against its competitive set. For example, the company has achieved first-quartile results in accounts receivable performance (average days delinquent, collection effectiveness, and percentage current), as shown in Figure 15.

General Mills’ first-quartile performance in accounts receivable is driven by a rigorous measurement focus, a collaborative approach to proactively resolve issues, an experienced team of professionals focused on identifying and mitigating risk, and the outsourcing of routine transactions. Dedicated staff in both the credit and customer service organizations monitors collection performance daily. The company also uses weekly reporting to identify potential issues; credit, the sales force, and customer service collaborate to address issues and problems in a timely manner. Each business area has specific credit and collections goals.

Figure 15
In addition, the company employs an experienced team of professionals focused on managing credit and collections risk. As a result of this team’s efforts, General Mills has historically suffered few losses from customer delinquency or bankruptcy.

Finally, the company continuously seeks opportunities to drive higher AR process performance by outsourcing routine transactions and focusing on value-added activities. For example, the company has outsourced cash applications and other routine transactions to shared services in India, to allow the collection staff to focus on trends and process performance.

**Accounts Payable Process Improvement**

Over the last few years, the finance organization at General Mills has been focused on improving accounts payable process efficiency by centralizing routine transactions, outsourcing certain transactions, leveraging technology, using standard approval matrices in SAP, leveraging a formal procurement card (P-card) program, and implementing an extended terms program administered by a third-party provider.

The shared services organization began with accounts payable, based in Minneapolis. It has since expanded to operations in India, including a third-party outsourcing operation and a captive company. Currently, cash application is handled by a captive organization located in Mumbai, and an Indian outsourcer handles invoice indexing, processing, and issue resolution. Both operations are closely integrated with the accounts payable processing shared service center in Minneapolis.

Finance has also leveraged technology to drive efficiencies in accounts payable processing. For example, the organization digitizes copies of invoices in Minneapolis and routes them for processing and approvals via Workflow, SAP’s integrated OpenText document routing and scanning.

From a control perspective, finance also leverages standardized approval matrices within SAP. The matrices allow for the automatic routing of invoices to the right individuals within SAP for approval based on the organizational hierarchy set up in the SAP HR module.

Finance has also implemented a formal procurement card program at the manufacturing plant level to improve accounts payable process efficiency. This program has eliminated a significant amount of PO activity and invoice processing and has allowed for consolidation and spend analysis of maintenance, repair parts, and other MRO operational spending by the central procurement group.

As a result of its efforts to improve accounts payable process efficiencies, the company has achieved first-quartile performance in accounts payable cost of about $1.90 per invoice, according to benchmarking data provided by the Shared Service Roundtable. Out of 1.2 million total domestic invoices totaling $7.7 billion
processed through its third-party processor, roughly 61 percent were via EDI and 73 percent were paperless transactions.

Finance continues to be challenged by days payable outstanding (DPO) performance. A practice that has helped DPO performance is a third-party service provider program that allows vendors to view their outstanding General Mills invoices on the Web, and choose to take earlier payment at a discount. General Mills has found this practice to be a “win-win” situation for both vendors and the company. It helps the company extend its terms without negatively affecting its valuable relationships with vendors, many of which are strategic relationships. The solution also provides vendors with more certainty in the timing and amount of payment. The practice has been so successful that the company is introducing it across its vendor base.

**Annual Working Capital Benchmarking**

As part of its continuous process improvement efforts, General Mills benchmarks its overall working capital performance against that of its peer set and the S&P 500 Food Group. It also reviews trends on an annual basis. Figure 16 on page 58 shows recent benchmarking results for key working capital metrics.

Ideally, the company likes to see at least a 50 basis point improvement in ROC from year to year. The results are used to develop working capital targets for the following year and to set process improvement action plans. Finance constructs the peer benchmarks based on publicly available data (e.g., financial and earnings statements, earnings calls, and investment presentations) and through relationships with benchmarking data suppliers such as APQC and the Corporate Executive Board.

**INFORMATION TECHNOLOGY STRATEGY AND APPLICATION**

*Our goal at General Mills is to hold zero domestic cash at the end of every day.*

— Craig Shafer, Assistant Treasurer

The treasury group at General Mills leverages technology to reduce workload, increase cash management efficiency, and provide cash management controls. The company has relied on SAP since the early 1990s for key treasury processes, including accounts payable, accounts receivable, and general ledger. In 2009, the company upgraded to the new treasury SAP modules for these processes. Using these modules, treasury reviews detailed current day cash positions and receives electronic bank statements five times daily. In addition, SAP automatically posts cash flows to the general ledger.
Ultimately, treasury’s goal is to hold zero domestic cash at the end of each day. Following the “the virtuous capital cycle” referenced in Figure 14, the group invests any excess cash in activities that drive additional growth, such as dividend payments, capital expenditures, and mergers and acquisitions activity.

RESULTS

*Keeping the focus on working capital has delivered us significant benefits.*

— Jerry Young, Vice President for Finance, Supply Chain

As a result of its focus on working capital management, General Mills has seen a steady decline in working capital as a percentage of sales—with one blip in 2008 due to commodity price volatility—over the last six years (Figure 17, page 59).
SUMMARY OF BEST PRACTICES
In summary, General Mills’ vice president of finance, supply chain, discussed the following best practices for improving working capital management and cash flow intelligence:

- a monthly working capital review,
- metrics to guide business decisions that encourage the effective use of working capital,
- accounts receivable effectiveness,
- accounts payable efficiency, and
- supply chain finance to help improve the company’s payables position.

Figure 17

Working Capital as a % of Sales
Case Study
Owens-Illinois Inc.

BACKGROUND
With 22,000 employees and more than 80 factories in 21 countries, Ohio-based Owens-Illinois Inc. manufactures glass containers for the food and beverage industries. The Fortune 500 organization reported $7.1 billion in revenue in 2009. With more than 70 percent of the organization’s business located outside of North America, it holds market leadership positions in each of the four regions it operates in: Asia-Pacific, Europe, Latin America, and North America.

Global expansion, market leadership, and a culture based on continuous improvement have contributed to the success of Owens-Illinois. The organization is actively seeking opportunities to not only expand production capabilities worldwide but also grow more stable and saturated markets through the introduction of new glass container concepts. The organization’s focus on continuous expansion and improvement is supported by four strategic priorities: strategic and profitable growth, marketing glass, innovation and technology, and operational excellence. Standardization, benchmarking and key metrics, and the implementation of Lean Six Sigma propel these strategic concerns.

VISION AND STRATEGY FOR IMPROVING WORKING CAPITAL MANAGEMENT

_Lean Six Sigma Kaizen events bring cross-functional team members into the room, and you end up with an appreciation of the end-to-end process._

─Joan Channell, global director, shared services

Ed White, CFO of Owens-Illinois, said the organization weathered the recession of 2008 and 2009 with relative ease thanks to its continuous process improvements, particularly in the realms of payables and receivables management. The organization was able to reduce inventories during the downturn and avoid extending payment terms at the expense of their suppliers. He said that Owens-Illinois had “record-low working capital at the end of 2009” in absolute value. Working capital was an important source of cash for the year. Owens-Illinois reduced its working capital as a percentage of sales from more than 19 percent in 2006 to 16 percent in 2009.
(Figure 18). This was achieved through process improvements, metrics, benchmarking, and creating a high-performance team and culture.

**Management of Working Capital as a % of Sales**

![Graph showing management of working capital as a percentage of sales over years 2009 to 2013.](image)

**Figure 18**

Owens-Illinois’ working capital components are shown in Figure 19. The organization aims to keep the capital committed to accounts receivables and accounts payable generally in balance as shown.

**2009 Working Capital Components**

![Pie chart showing working capital components in 2009.](image)

**Figure 19**
A Decade of Change

In 2000 Owens-Illinois began to standardize business processes and introduce metrics and benchmarking in North America. In 2007 it made a large effort to reduce waste and increase efficiency and quality in operations by implementing Lean Six Sigma. This implementation had an immediate impact on working capital by improving processes and enhancing cross-functional collaboration.

By 2005, with a strong corporate shared services team in place, the organization determined it needed a global shared service center outside of North America. Today, the global shared services group includes Europe, Australia, Latin America, and soon an office in China (Figure 20). Shared service centers have fostered cross-functional collaboration among accounts receivable, sales, accounts payable, and procurement through regular meetings, education and training opportunities, and Lean Six Sigma events.

<table>
<thead>
<tr>
<th>REGION</th>
<th>AR</th>
<th>AP</th>
<th>CASH</th>
<th>MASTER DATA</th>
<th>PAYROLL</th>
</tr>
</thead>
<tbody>
<tr>
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<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>NORTH AMERICA</td>
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<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
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<td>X</td>
<td>X</td>
<td></td>
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</tr>
<tr>
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<td>X</td>
<td>X</td>
<td>X</td>
<td></td>
</tr>
<tr>
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<td>TBD</td>
<td>TBD</td>
<td>TBD</td>
<td>TBD</td>
</tr>
</tbody>
</table>

Global Shared Services

Figure 20

The Road to Continuous Improvement

Lean Six Sigma was important in reducing waste and improving the performance of critical customer (internal and external) requirements at Owens-Illinois. A key component of the Lean Six Sigma process was the use of Kaizen events. Kaizen events allow a cross-functional team to map out a business process and improve it. These events also help to break down silos by allowing teams to understand the total process.

One example of the success of an internal Kaizen event focused on customer discount controls. Through Lean Six Sigma collaboration, the team was able to conduct a deep-dive analysis of the existing process to understand the root causes of
problems and identify opportunities to re-engineer and improve the process. Thanks to the efforts of this team, the organization was able to save $1 million.

**ANALYTICS AND MEASURES TO ENABLE BETTER WORKING CAPITAL MANAGEMENT**

*The most important part of measuring is that it enables everyone to understand the priorities.*

—Joan Channell, global director, shared services

For each process involved in working capital management, Owens-Illinois has key metrics to assess performance. Key performance indicators are kept simple and reported promptly. These measures are presented on a recurring basis (monthly and quarterly) to various departments to ensure working capital management is a pertinent subject for all employees.

For instance, on the seventh working day after a month closes, the general manager and sales staff receive an accounts receivable trends report (Figure 21, page 64). The one-page format allows for a quick view of accounts receivable activity. If underperformance is found for any of the measures listed, then owners can implement immediate and timely action to remedy the issues.

“The most important part of measuring is that it enables everyone to understand the priorities,” said Channell. Employees are more accountable for their goals and communicate the issues to management ahead of time, because they know they are being measured. The organization has moved to a single point of accountability model, where one staff member is assigned to each account and serves as the source for all details regarding activity on the account.
Improving Working Capital Management and Cash Flow Intelligence

KPI Reporting – Accounts Receivable

<table>
<thead>
<tr>
<th></th>
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<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Domestic Glass</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>DSO</td>
<td>10.2</td>
<td>15.3</td>
<td>16.2</td>
<td>16.4</td>
<td>16.3</td>
<td>16.9</td>
<td>18.0</td>
</tr>
<tr>
<td>BPDSO Best Possible DSO</td>
<td>9.8</td>
<td>15.8</td>
<td>15.2</td>
<td>16.4</td>
<td>16.7</td>
<td>16.3</td>
<td>17.6</td>
</tr>
<tr>
<td>ADD Average Days Deficient</td>
<td>0.5</td>
<td>(0.5)</td>
<td>1.0</td>
<td>0.1</td>
<td>(0.4)</td>
<td>0.5</td>
<td>0.4</td>
</tr>
<tr>
<td><strong>$MM</strong></td>
<td></td>
<td></td>
<td></td>
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<td></td>
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<tr>
<td>Sales</td>
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<td>123.7</td>
<td>142.2</td>
<td>142.1</td>
<td>153.9</td>
<td>157.1</td>
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<td>66.0</td>
<td>67.9</td>
<td>72.9</td>
<td>77.4</td>
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<td>93.3</td>
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<tr>
<td>Past Due Invoices &gt; 3 Days</td>
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<td>1.8</td>
<td>2.9</td>
<td>1.2</td>
<td>0.7</td>
<td>1.5</td>
<td>2.1</td>
</tr>
<tr>
<td>% Past Due Invoices &gt; 3 Days</td>
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<td>2.7%</td>
<td>4.2%</td>
<td>1.7%</td>
<td>0.9%</td>
<td>1.7%</td>
<td>2.2%</td>
</tr>
<tr>
<td>Customer Deductions</td>
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<td>0.8</td>
<td>1.2</td>
<td>0.8</td>
<td>1.0</td>
<td>1.3</td>
<td>1.5</td>
</tr>
<tr>
<td>% Customer Deductions</td>
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<td>1.2%</td>
<td>1.8%</td>
<td>1.1%</td>
<td>1.3%</td>
<td>1.6%</td>
<td>1.6%</td>
</tr>
</tbody>
</table>

**CUSTOMER**

<table>
<thead>
<tr>
<th>DBT (DAYS BEYOND TERMS)</th>
<th>TERMS</th>
<th>Brackets = Days Paid Early</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>1%10N30</td>
<td>3.6</td>
</tr>
<tr>
<td></td>
<td>N30</td>
<td>(5.2)</td>
</tr>
<tr>
<td></td>
<td>1%10N30</td>
<td>(2.0)</td>
</tr>
<tr>
<td></td>
<td>N30</td>
<td>0.4</td>
</tr>
<tr>
<td></td>
<td>N30</td>
<td>1.4</td>
</tr>
<tr>
<td></td>
<td>N30</td>
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</tr>
<tr>
<td></td>
<td>N30</td>
<td>0.7</td>
</tr>
<tr>
<td></td>
<td>1%10N30</td>
<td>(1.8)</td>
</tr>
<tr>
<td></td>
<td>N30</td>
<td>3.6</td>
</tr>
<tr>
<td></td>
<td>N30</td>
<td>0.7</td>
</tr>
</tbody>
</table>

*Trade Receivables Only

Figure 21

Average Days Deficient

DSO, or days sales outstanding, is oftentimes dictated by the business and markets. Owens-Illinois tends to focus more intently on average days deficient (ADD), which allows the organization to evaluate how much of its receivables are deficient at the end of each month. ADD is the difference between the DSO and best possible DSO, which is when all customers pay consistent with the contractual terms. From a finance perspective, it is an easy metric to understand; however, the challenge for the sales organization is to take ownership. Despite this challenge, the organization has made a lot of progress in this area and has successfully met its goal of keeping ADD to less than one day. Figure 22 on page 65 shows the steady decline in ADD from more than four days in 2006 to less than one day in 2010.
Accounts Receivable KPI – Average Days Deficient (ADD)

Figure 22

Past Due Invoices

To track the amount of past due invoices, Owens-Illinois created the percentage past due metric. Owens-Illinois aims for metrics that are fair to customers and have attainable goals. For example, Owens-Illinois realizes that, at times, invoice processing and payment by its customers can be hampered by delays in processing credits. For this reason, the organization initiates corrective actions only when three days have passed since the invoice due date. This three-day window accounts for the weekend, as well as delivery and shipping time. It measures credit analysts on the past due invoices greater than three days. Moreover, Channell said, the accounts receivable team communicates closely and regularly with sales managers to understand and intervene when a key customer’s payment patterns deteriorate.

Days Beyond Terms

The final component on the key performance indicator report for accounts receivable is the customer metric days beyond terms (DBT). This metric provides each general manager and their senior sales managers with insight into the top ten customers, their terms, and how they pay against those terms.
Days Payable Outstanding

During the recent recession, its days payable outstanding (DPO) was kept at an average of 60 days. As a rule, the organization tries work in a collaborative, win-win mode with its supply base. Several programs were rolled out to facilitate this. For instance, the procurement team implemented a procurement card program through which purchases are paid for with a credit card (P-card) or invoices are paid directly by JPMorgan Chase & Co. Owens-Illinois benefits from increased processing efficiencies and reduction in processing costs (fewer invoices to process). JP Morgan pays invoices to the supplier and bills Owens-Illinois, thereby increasing cash flow and providing a cash incentive paid as annual spend targets are achieved. This program accounts for only 3.5 percent of the organization’s total spend; however, the team continues to seek additional partners to join the program. With the right controls in place and a quick set-up process, Owens-Illinois trusts employees with P-card procurement privileges.

The organization also has found that suppliers appreciate predictability; they want to know when payments are scheduled to arrive. Accounts payable generates payments two times per month in all regions, thus providing suppliers with a payment schedule they can depend on.

Another program that has helped DPO is the implementation of the IBM Global Expense Reporting Solutions program. This program has given the organization the ability to manage travel and expenses globally using one process. Previously, the employee was set up for reimbursement direct to their account. Individuals submitted travel and expenses for reimbursement, and the employee was responsible for payment. IBM’s software allows Owens-Illinois to pay American Express directly upon receiving the travel and expense reports. The program has been successfully rolled out in North America and Europe, and a roll-out to Asia is expected later in 2010.

Additional Metrics

Additional metrics that are reviewed include procurement card percentage of spending, percentage of electronic payments, and lost discounts percentage.

Owens-Illinois has created innovative practices that have allowed it to significantly improve its ability to take negotiated discounts. When an invoice arrives from a vendor that offers discounts to Owens-Illinois, that invoice is fast-tracked for processing. Moreover, if there is a three-way-match failure (because, for instance, purchase order data disagrees with data shown on shipping documents or on an invoice), then the organization charges the amount of the lost discount back to the responsible operating unit. This level of accountability has resulted in a 91 percent salvage rate because the locations are motivated today to avoid charge backs.
The Accounts Payable Team

Globally, the accounts payable team processes more than 900,000 invoices annually. Accounts payable specialists are assigned to specific plant locations and are assigned a number of special projects to give them variety in their work. The accounts payable team tracks both individual and team metrics, and the individual metrics focus on the number of invoices processed per day. Although results vary by region, the organization desires to increase the processing speed for each processor. The team has also developed a vendor inquiry hotline.

Owens-Illinois has done a lot of work on matching exceptions. One of the larger initiatives underway is evaluated receipt settlement (ERS), which is a procedure for the automatic settlement of goods receipts. The major benefits of ERS include invoice variance prevention, the elimination of non-value-added work (e.g., tasks associated with reconciliation), and opportunity cost of capital savings. The organization believes that a two-way match is preferable to the three-way match approach because it does not require the use of paper invoices. Sixty percent of North American customer receipts are based on the ERS two-way match. The key to this is electronic data interchange (EDI), and that means the purchase order and receipt must be valid for payment. In North America, the organization still issues some paper checks but has a program in place to pay all vendors electronically. Currently, 70 percent of all payments worldwide are made electronically.

PERFORMANCE MANAGEMENT PRINCIPLES AND MEASURING PROCESS IMPROVEMENT

*Provide the team a robust process and visibility to performance metrics, and your job becomes celebrating the team successes.*

*Winning is fun for everyone.*

—Ed White, chief financial officer

In addition to a continued commitment to Lean Six Sigma, Owens-Illinois annually engages in benchmarking as part of its process improvement efforts. The finance executives at Owens-Illinois regularly invite third-party organizations to benchmark its processes in hopes of learning new and innovative techniques for working capital management. Owens-Illinois is committed to exploring new tools and techniques to facilitate better process controls and growth.

The organization employed a seven-step improvement plan to guide its global expansion since 2003, and White is its champion (Figure 23, page 68). The seven-step plan helps to define “what are we trying to accomplish and how are we going to get there,” he said.
Owens-Illinois Seven Step Improvement Plan

1. Ownership of the balance sheet value
2. Customer/Vendor relationships
3. Visibility of owners
4. Performance Metrics
5. Set easy goals for early success
6. Public recognition
7. Continuous process improvement

Figure 23

Ownership of the Balance Sheet Value
Owens-Illinois realized that some of its management team members, who were not finance professionals by training, did not fully understand the dynamics of working capital. For instance, one operating manager assumed that working capital could be optimized if he merely ordered factories under his control to invoice the customer for obsolete inventory at the end of a month. Soon thereafter, the finance team developed an easy-to-understand training curriculum to ensure that all employees in the organization understand this concept and how they affect working capital. The organization used a simple format to explain working capital (e.g., pie charts by region and the use of analogies to describe the details) and also tied it to financial incentives.

Customer/Vendor Relationships
Owens-Illinois understands and values its customer and vendor relationships. Its goal is to be good business partners to its internal and external customers.

Performance Metrics
Performance metrics are important to Owens-Illinois. When individual metrics are used, it is not meant to be used as a disciplinary tool but rather to hold each employee accountable for their goals. The emphasis on measurement helps the organization stay in control and correct issues.

Set Easy Goals
Owens-Illinois sets easy goals that are achievable, easy to understand, and relevant for the markets. Initially, the North American team was not able to review past invoices greater than three days, so they set a measure to review invoices based on a declining number of days. This allows the region to have early successes because the goal makes sense for their environment and it can affect the results.
Public Recognition

Owens-Illinois is proud of the culture it has created around recognizing its employees at each level in the organization. Ed White has been a big proponent for driving down how important recognition is; in his 30-year tenure at Owens-Illinois, he has made it a point to get to know as many employees as possible so they know they are a valued resource to the organization.

Continuous Process Improvement

Lean Six Sigma is a tool that Owens-Illinois has used to provide the framework to improve internal processes. This framework has enabled employees to continue to think about various ways to solve their problems with more than just a singular viewpoint. White said, “You should invite outsiders to provide in-depth evaluation of your processes and borrow their ideas shamelessly.”

Accounts Payable Recovery Plan

The organization has had four audits from 2003 to 2010 in North America. On the most recent AP recovery audit, the auditor reviewed 1.4 million invoices ($2 billion in annual payables volume) and looked for duplicate payments, reviewed vendor statements, and identified unused credits. The auditor found only 87 errors (5 σ), which is a remarkable score in Six Sigma terms. Owens-Illinois is currently planning third-party AP recovery audits for the other regions.

INFORMATION TECHNOLOGY STRATEGY AND APPLICATION

*We put a lot of emphasis on getting the data how we want it and when we want it.*

—Joan Channell, global director, shared services

Maximizing technology has played a large role in the initial success of working capital management at Owens-Illinois. The shared services team wants to be self-sufficient and not rely on the IT group. Therefore, useful training and the implementation of a global enterprise resource planning (ERP) system ensures immediate access to needed data. SAP allows the organization to accumulate information globally and provides a cross-functional view of a customer’s history with insight into their payment habits. Standardized ERP also eliminates the challenges that come with each region being on a disparate system; data is measured globally and consistently.

Owens-Illinois’ finance team also uses a report writing tool called Business Objects to generate information that helps credit and collections staff prioritize their
analyses and interventions when customer payment patterns signal trouble. The tool is independent of IT support, and the team is virtually self-sufficient in its use. The team is able to create simple straight-forward and prompt reports that can be refreshed in real time. The ability to have up-to-date data helps when teams interact with sales managers and with customers is invaluable, said Channell.

**SUMMARY OF BEST PRACTICES**

In summary, Owens-Illinois has employed the following best practices and lessons learned in order to improve working capital management and cash flow intelligence:

- Use incentives that will motivate employees to embrace and understand working capital management.
- Cross-functional collaboration and communication is important for process improvement efforts.
- Executive ownership and support coupled with a clear strategic direction are key to continuous improvement.
- Get information quickly, consistently, and globally through the use of real-time reporting.
- Employ tried and true improvement methodologies (i.e., Lean Six Sigma), and hold teams accountable for the results.
- Define working capital as accounts receivable plus inventory plus repair parts less accounts payable.
- Charge back lost discounts to individual plants to increase accountability.
- Implement a procurement card process.
- Keep frameworks and processes simple.
- Conduct bimonthly check generation, and employ rational payment terms.
- Use a two-way match in the evaluated receipt settlement (ERS) process, and implement disciplined purchase order and receiving processes.
- Build strong relationships with customers.
- Vendors serve as good internal and external business partners.
- Put the right people in the right jobs by creating interesting career paths for employees.
- Employee recognition is key to employee engagement.
Case Study
Zappos.com, Inc.

BACKGROUND

“We’ve aligned the entire organization around one mission: to provide the best customer service possible. Internally, we call this our ‘WOW philosophy.’”

—Company Web site

Zappos.com, Inc., was founded in 1999 by former chairman Nick Swinmurm following an unsuccessful trip to the mall to buy shoes. At the time of its founding, the prospects of an online shoe retailer were considered questionable, as naysayers believed that customers would not purchase shoes online without trying them on first. Zappos.com, however, not only survived but thrived. Today the organization is a leading online retailer of shoes (with over $1 billion in yearly gross sales and 2,000-plus employees in its family of companies), ahead of competitor J.C. Penney. Its success is primarily a result of its intense focus on customer service, including customer-friendly policies such as a 365-day return policy, free shipping outbound and for returns, and, in many cases, next business day delivery.

Zappos.com was acquired in November of 2009 by online retailing giant Amazon.com, Inc., and is currently a wholly owned but independently operated subsidiary that has diversified its online sales to include apparel, accessories, housewares, and beauty products.

Company leaders believe that corporate culture is paramount to the success of Zappos.com. The organization operates according to 10 established core values that support its corporate culture:

1. Deliver “WOW” through service.
2. Embrace and drive change.
3. Create fun and a little weirdness.
4. Be adventurous, creative, and open-minded.
5. Pursue growth and learning.
6. Build open and honest relationships with communication.
7. Build a positive team and family spirit.
8. Do more with less.
9. Be passionate and determined.

These 10 core values are part of daily life at Zappos.com. At the heart of the core values is customer service: Zappos.com considers and brands itself first and foremost as a customer service organization, not an online shoe retailer. To that end, the organization places strong emphasis on employee satisfaction and engagement and specifically budgets for fun events during working hours, heavily emphasizes training and development activities for all employees, and has established employee rewards and recognition programs that create a happy employee base. The company has found that happy employees, in turn, translate into high levels of customer service, and the organization’s business model and philosophy is geared entirely around delivering high levels of customer service.

VISION AND STRATEGY FOR IMPROVING WORKING CAPITAL MANAGEMENT

Roles and Responsibilities

The treasury team holds ultimate responsibility for working capital management at Zappos.com. The team is aided by the senior treasury manager, who oversees both treasury and accounts payable at the organization. This dual role provides him with a holistic view of the company’s cash flow position, including payables, check runs, and ACH runs.

The senior treasury manager, in turn, reports to the financial controller of the organization. Other key players in working capital management at Zappos.com include the financial planning and analysis (FP&A) team, the merchandising team, and an operational control committee that reviews key organizational performance metrics.

Strategic Importance of Working Capital Management

Zappos.com’s stated mission is “to provide the best customer service possible.” A key part of this mission involves stocking everything that is sold on the Zappos.com Web site at the fulfillment center in Kentucky, rather than drop-shipping goods, to enable control over the entire customer experience. All employees are educated about their individual role in and impact on working capital management, which follows the company’s growth and learning core value. Training and development enables the organization to communicate the strategic value of improved working capital management to both finance and non-finance employees.

Specifically, the organization has created a “Pipeline” team (named after its responsibility for developing the leadership pipeline) that is chartered with the creation of training courses for all employees in order to help them understand how
the organization operates. This includes two finance courses that cover the basics of financial statements and a Sarbanes-Oxley class.

Pipeline training courses also address how the various departments within the company contribute to the company’s mission and growth; for example, the four weeks of new-hire orientation that all employees undergo focus on training in the highest levels of customer service, helping employees create personal emotional connections with customers. The courses also explore, for example, how the merchandising department and buyers perform their functions. These courses demonstrate to Zappos.com employees the interrelationship of various departments and how individual employees’ actions and behaviors can have a direct impact on key business outcomes.

Cross-functional Collaboration Within Working Capital Management

Zappos.com ensures collaboration and calibration on working capital management through weekly cross-functional management meetings and monthly data triangulation meetings between treasury, FP&A, and accounting.

The operational control committee (composed of executives at the director level and above) convenes weekly to discuss and review key operational metrics. This committee maintains oversight of corporate performance metrics and measures and identifies improvement areas based on the metric review.

On the fourth week of each month, treasury, FP&A, and accounting meet to compare and triangulate their financial data (forecasted cash inflows and outflows vs. actual month to-date). FP&A prepares monthly reforecasts by meeting with the various department leaders and reviewing prior-month budget vs. actual, looking at prior-month sales and accounts payable timing and adjusting the remainder of plan year. This process enables the groups to determine what the final payment runs need to be to hit the monthly free cash flow goal, taking into consideration any sales upside or downside.

The senior treasury manager believes the meetings also provide a productive environment for airing operational glitches—for example, data entry errors that prevent successful completion of three-way matches between purchase orders, shipping receipts, and invoices. When a match cannot be completed immediately, the result is an exception item. Too many of these can undermine the integrity of the cash flow forecasts.
Improving Working Capital Management and Cash Flow Intelligence

ANALYTICS AND MEASURES TO ENABLE BETTER WORKING CAPITAL MANAGEMENT

“The relationship with our vendors is key at Zappos.com.”
—Meg McInnis, senior manager change management

Summary of Working Capital Key Performance Indicators
A summary of the working capital metrics tracked at Zappos.com is shown in Figure 24, and commentary on each follows. The metrics depicted in Figure 23 represent a small piece of what the operational control committee reviews weekly.

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Inventory turn</td>
<td>2.69</td>
<td>2.38</td>
<td>2.56</td>
<td>2.39</td>
<td>2.66</td>
<td>2.30</td>
</tr>
<tr>
<td>DIO</td>
<td>136</td>
<td>141</td>
<td>151</td>
<td>154</td>
<td>138</td>
<td>154</td>
</tr>
<tr>
<td>DSO</td>
<td>3</td>
<td>5</td>
<td>2</td>
<td>3</td>
<td>5</td>
<td>4</td>
</tr>
<tr>
<td>DPO</td>
<td>46</td>
<td>52</td>
<td>59</td>
<td>55</td>
<td>53</td>
<td>56</td>
</tr>
</tbody>
</table>

Figure 24

► Inventory turn: Considering that the company warehouses everything it sells online, this ratio helps monitor the health and aging of inventory at a high level and as a measure of year over year improvement. More in-depth product category and LPN (unit) aging is monitored closely by merchandising.

► Days of Inventory Out (DIO): Zappos.com has improved remarkably over the last year on this metric (in June 2009 DIO was 200-plus days), largely because of the success of its liquidation channel, 6pm.com. 6pm.com sells discounted and aged inventory, so its business model is very different from that of the Zappos.com Web site. For instance, 6pm.com charges customers for shipping and has a 30-day return policy. Prior to its acquisition by Amazon.com, the aging of inventory and DIO was a significant concern for Zappos.com because it was a net borrower and depended on a revolving line of credit that was
secured on the liquidation value of inventory as collateral. Since Zappos.com’s sales are cyclical, with most sales occurring in the fourth-quarter holiday season, the organization tended to have a shortage of cash during inventory ramp-up in the second and third quarters of every year, so it relied heavily on the revolving line of credit. Since the acquisition by Amazon.com, however, Zappos.com has become a net investor and DIO is not nearly as much of a concern today. The organization strives to maintain inventory at a healthy level and not let it age too much.

- **Days Sales Outstanding (DSO):** Zappos.com has a low DSO because most of its sales are paid by credit card and alternate methods like PayPal and Bill Me Later. The company focuses on charge-backs, with a team dedicated to maintaining or keeping track of charge-back volume. This team also monitors fraud statistics/fraud detection rates, and on a weekly basis provides the status of orders reviewed and of orders that were cancelled because they were deemed high-risk. Currently, the charge-back volume is below 0.2 percent of gross sales, compared with the industry average of approximately 0.5 percent.

- **Days of Payables Outstanding (DPO):** Zappos.com focuses on this metric much more than on DSO. The organization purchases everything it sells on the Web site in advance. Zappos.com has more than 1,000 trade vendors, with average terms of 60 days.

Zappos.com maintains weekly accounts payable metrics, including invoice count, paper versus EDI, weekly invoices parked/posted volumes, new vendor setups on the trade and non-trade side, and three-way match metrics.

An analysis of some of these metrics, such as aged unmatched goods receipts (GR), revealed to management a problem in the trade purchase to pay cycle, specifically due to pricing/quantity discrepancies and PO changes. This analysis was the genesis of the PEHZ improvement project discussed next. It was through the daily and weekly monitoring of these important metrics that the organization realized the need for improvement.

Figure 25 on page 76 summarizes some of the key AP metrics tracked by Zappos.com.


**Accounts Payable Metrics**

<table>
<thead>
<tr>
<th>Metric</th>
<th>Manual</th>
<th>EDI</th>
<th>Expense</th>
<th>Trade</th>
</tr>
</thead>
<tbody>
<tr>
<td># of Trade Invoices Entered</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td># of Expense Invoices Entered</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Unmatched Invoices</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>AP Head Count</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>New Vendors Added</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Vendors</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Purchase Orders Created</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Purchase Orders Changes</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Purchase Orders Changes</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Prior to Ship Date</td>
<td></td>
<td></td>
<td></td>
<td>Trade</td>
</tr>
<tr>
<td>After Ship/Prior to Cancel</td>
<td></td>
<td></td>
<td></td>
<td>Trade</td>
</tr>
<tr>
<td>After Cancel</td>
<td></td>
<td></td>
<td></td>
<td>Trade</td>
</tr>
<tr>
<td>Aged Unmatched and Unpaid Invoices</td>
<td></td>
<td></td>
<td></td>
<td>Trade</td>
</tr>
<tr>
<td>Units in FC Exception Area</td>
<td></td>
<td></td>
<td></td>
<td>Trade</td>
</tr>
<tr>
<td>Aged Unmatched GR</td>
<td></td>
<td></td>
<td></td>
<td>Trade</td>
</tr>
<tr>
<td>Inventory Shrink in Units</td>
<td></td>
<td></td>
<td></td>
<td>Trade</td>
</tr>
</tbody>
</table>

Figure 25

**Working Capital Performance Improvement: The PEHZ Project**

The working capital metrics described above are monitored on a weekly basis by the operational control committee. These weekly metric reviews alert finance employees about any potential working capital issues before they become serious problems.

Several years ago, the need to deal with a rising tide of exception items—in purchasing, receiving, or invoicing—came up at an operational review focused on the accounts payable area. The metrics review indicated a spike in the volume of three-way match discrepancies and failures—for example, vendors sending the wrong shoe styles or colors. These occurrences, of course, were gumming up the warehouse’s work flows and causing delays in the time it takes to make a product sellable on the Web site. They also were increasing the warehouse labor required to handle the exceptions, since the exceptions had to be diverted from the receiving dock onto an exception lane.

Upon further examination, the organization found that these exceptions were a driving factor in treasury’s inability to effectively forecast and manage cash flow. In effect, the company found itself in the quandary of having sufficient cash but still being unable to pay its vendors because it couldn’t perform the three-way match process from an accounts payable standpoint (due to a receiving or purchasing exception that blocked the three-way match). The PEHZ (Purchase Exception Handling at Zappos) project was created to get to the root cause of the problem.
The PEHZ project is a six-month-long project that began in early 2010 and will go live in the first quarter of 2011.

The high-level objectives of PEHZ are to:

- Implement an automated work flow to communicate and expedite the early resolution of purchasing, receiving, and invoicing exceptions. In the early days at Zappos.com, the resolution of purchase exceptions took place via e-mail between the fulfillment center in Kentucky and the merchandising department outside of Henderson, Nevada, which was not an effective way to communicate. Zappos.com believes that an automated work flow engine is critical in expediting the resolution of purchasing exceptions.

- Enhance buyer tools around the purchasing process. This enables buyers to make more educated decisions and have access to up-to-date information regarding their purchases.

- Introduce new EDI transactions to improve effective communication between the buyer and the vendor for the purchase-to-pay cycle. Zappos.com works with its vendors that are not yet on EDI to migrate them to EDI and offers them options for becoming compliant with the EDI program. Currently, the purchase order creation, advanced shipping notices (ASNs), and invoices are part of the trade EDI program. With the PEHZ effort, the PO acknowledgment and the PO change orders will also be included in the EDI program, which will further synchronize the Zappos.com systems with vendor systems, well before the goods are delivered to the company’s docks. Synchronizing the Zappos.com systems with the vendor systems is critical to resolve any kind of mismatch problems early on. In the past, the company didn’t realize it had a problem until the invoice was due, and in some cases when the invoice was past due. The new EDI transactions shift the negotiations and “sync-ups” between the vendor and Zappos.com up front, while the purchase is being created, which should help the company more effectively manage cash flow.

- Improve roles, access, and security controls for the vendor portal. This is a continuously-evolving objective with the goal of opening up systems where possible to allow vendors and sales representatives to view their sales volumes, accounts payable invoices, and exceptions data and become part of resolving their own exceptions. The ultimate goal is to get the product to the shelves, sell it as quickly as possible, and provide timely payments to the vendors. Vendor relationships are key for making this happen.
PEHZ is expected to reduce the quantity of purchasing and receiving exceptions by 75 percent. This benefit will be a result of improving processes and exception handling for PO confirmation by bringing in the additional EDI transactions noted above. For example, prior to PEHZ, Zappos.com had not been effectively reconciling ASNs against purchase orders. With PEHZ, ASNs will be brought into the EDI program to ensure that what the vendor plans to ship to the company dock is what the buyer intended. If not, the PO can be adjusted appropriately before the goods arrive at the dock. This is critical for the receiving departments in the Kentucky fulfillment center, because if there is alignment before the goods hit the dock, then receiving handles the incoming goods only once, and the product moves rapidly to the shelves, becoming sellable, and then on to the customer.

In addition, as part of PEHZ, the organization has established new processes for PO communication. Now, Zappos.com has the ability to automate the sending of POs and change orders through e-mail, EDI, and the vendor portal. There are many methods for generally communicating exceptions to the vendor: All vendors are included in exception reporting and work flow action items. This ensures that vendors are included earlier in the exception resolution process, rather than having the resolution fall primarily on the Zappos.com staff (Figure 26).

Trade EDI Landscape

PEHZ should improve the invoice reconciliation process by 85 percent, which significantly impacts the accounts payable process. Through improved communications and issue resolution around three-way match discrepancies via the automated work flow, and by implementing processes to address exceptions upstream, the number of unmatched goods receipts will be greatly reduced, which will allow invoices to be processed faster. The new processes will ensure that many
of the exceptions and reasons for non-matching will be resolved well before the accounts payable team becomes involved.

**PERFORMANCE MANAGEMENT PRINCIPLES AND MEASURING PROCESS IMPROVEMENT**

“Embrace and drive change, while building open and honest relationships with communication.”

—Zappos.com core values #2 and #6

**Change Management and Process Improvement**

Senior leaders at Zappos.com realize that in order for any significant organizational change to be successful—including changes on a more macro scale such as being acquired by Amazon.com or on a more functional scale such as implementing the PEHZ project to reduce exceptions and improve cash flow management and forecasting—they should follow foundational principles of change management. The organization, indeed, takes very seriously its commitment to successfully implementing change—it has recently established a full-time senior manager of change management position, and it applies core principles of change management to all key business change, finance-related or otherwise. In fact, the new senior manager of change management at Zappos.com was previously the senior manager of accounting operations, which helps to bring the principles of effective change management to the world of finance at Zappos.com.

The company’s change management department is housed inside of the project management department. This is primarily because Zappos.com as an online retailer, is a technology-based-company, with projects that are primarily technology-based. At any given time the organization has a number of projects in process.

To ensure effective change, Zappos.com adapted key principles of successful change management, which it attributes to McKinsey & Co. The critical success factors for successful change projects (and the common denominators among failures) are summarized in Figure 27 on page 80.
Common Denominators of Unsuccessful and Successful Projects

<table>
<thead>
<tr>
<th>Common Denominators of Unsuccessful Projects</th>
<th>Common Denominators of Successful Projects</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Lack of commitment and follow-through by senior executives</td>
<td>• Senior managers, middle managers, and frontline employees were all involved</td>
</tr>
<tr>
<td>• Defective project management skills among middle managers (pertaining to using senior managers as project managers)</td>
<td>• Everyone’s responsibilities were clear</td>
</tr>
<tr>
<td>• Lack of training and confusion among frontline employees</td>
<td>• Reasons for the project were understood and accepted throughout the organization</td>
</tr>
</tbody>
</table>

Figure 27

When implementing a change project such as PEHZ or SAP financials, Zappos.com first ensures that its senior executives have committed to follow through. The lack of such commitment is a primary reason that organizations experience unsuccessful projects.

Defective project management skills among middle managers also drive project failure. For example, instead of investing in a project management office or hiring full-time project managers, as Zappos.com has done, organizations whose projects have been unsuccessful would typically assign a senior manager to manage the project, on top of his or her full-time job.

Another primary reason for failed projects is the lack of training for and confusion among front-line employees. Zappos.com has found that training its employees on the new process is key. For example, the organization learned many lessons around training best practices when it switched to SAP financials. And, as described earlier, when the organization was implementing new systems as part of the PEHZ project, employee training and better vendor communication would have allayed some of the vendors’ unnecessary worry about slower-than-usual payments.

One of the most vital the common denominators behind successful project initiatives is involving senior managers, middle managers, and other relevant employees in the change at the beginning of the process, with clear responsibilities. For example, when Zappos.com hires and/or brings in subject matter experts to provide content expertise for a particular project, the organization educates them to ensure they understand their responsibilities and the duration of the project. The
organization trains and communicates with affected employees to ensure that the reasons for the project are understood and accepted throughout the organization. To this end, the senior manager of change management spends a large percentage of her time making presentations across departments on all types of projects and initiatives (finance, technology, etc.). Employees are commonly asked to rate the company post-change on its performance with regards to the critical success factors outlined in Figure 27, so that it continuously improves in its change efforts.

Organizational change management at Zappos.com endeavors to establish a successful process for implementing business process improvements, change management strategies, workforce training, and workplace communications, as well as to ensure that the corporate core values are part of each organizational change initiative. Dedicated solution analysts (which are similar to business or technical analysts at other organizations) are assigned to fully document the steps of existing processes prior to engaging in any significant project or change effort, recognizing that the organization is rapidly growing and, therefore, processes change quickly. The organization incorporates a number of change management strategies, such as project kickoff parties, focus groups, surveys, and fun videos, to engage employees early on in the change and secure their buy-in to the goals and objectives of the project. In addition, the organization strives to recognize any external stakeholders of the project, including vendors as well as freight carriers and customers, who are also often a big part of the success of a project.

Fundamentally, the senior manager of change management believes that employees need to understand what organizational or business goals will be achieved by the change in order for the change to be successful. To accomplish this, the change management department works with directors and senior managers to show staff members how the change will make their jobs easier, to help them understand and accept their roles in using the new system or process, and to push them to a higher level and expose them to new opportunities.

Ultimately, the objectives of the change management department at Zappos.com are to:

- build awareness of the need for change,
- create the desire to participate and support the change,
- transfer knowledge on how to change,
- develop the ability to implement required skills and behaviors, and
- provide reinforcement to sustain the change.

If employees are engaged early in the change process, and if relevant parties are continuously informed of the project status, then the success rate for the project will go up.
Measures and Techniques Used for Working Capital Management

Performance

Free cash flow is a very important measure to Zappos.com and is one of the key metrics tracked by parent Amazon.com. As discussed earlier, on a monthly basis, treasury, FP&A, and accounting triangulate data regarding free cash flow, and one of the metrics specifically tracked by FP&A is free cash flow per unit sold. FP&A establishes a financial plan at the beginning of the year, and then on a monthly basis monitors the progress toward cash flow goals and makes adjustments to the forecast based on daily sales receipts and cash outflow data. The treasury department prepares daily cash positioning snapshot reports every morning and disseminates them to senior executives across the company to make them aware of the status of operating cash and investments.

From a more macro standpoint, the organization has identified five key cross-functional business drivers that ensure organizational success and ultimately translate into optimal working capital levels. For example, one measure of the health of organizational culture is net promoter score, which ultimately impacts revenue. In addition, since the organization is an online retailer and site uptime is paramount, the organization also closely tracks site downtime. Other key business drivers include profit margins and pricing, merchandising stock-out rates, and shipping costs and operating expenses as a percentage of sales. These key business drivers are reviewed closely during the weekly operational control committee meetings.

Performance Management Principles

Zappos.com conducts monthly manager meetings (for executive, senior, and middle managers, and occasionally supervisors) to assess the financial performance of the company, review the forecast and performance to forecast, review sales plans, discuss any anticipated shortfalls, and review cross-departmental metrics. These meetings align all managers with the overall financial goals of the company and encourage managers to share the key themes and information with their teams in a meaningful way. In addition to a financial and sales discussion, the manager meetings announce promotions and recognition/rewards and discuss the Pipeline classes. Pipeline classes are offered to managers to help them communicate financial goals and metrics, and their alignment with organizational strategy, to their teams.

INFORMATION TECHNOLOGY STRATEGY AND APPLICATION

Successfully leveraging IT and automation is critical for an Internet business such as Zappos.com. One area in which the organization has focused in terms of automating working capital management was discussed in the section describing the PEHZ project. The organization implemented an Oracle work flow engine, combined with internally developed applications, that will allow communications among facilities, vendors, customers, employees, and staff members as the organization grows. This work flow capability facilitates effective management and resolution of work flow action items.
Before IT instigates a new technology project, solution analysts first document the process being improved. Providing IT project managers with all of the pertinent details about the process helps ensure that the project design will succeed.

Project success is also facilitated via weekly status meetings with all of the relevant stakeholders on any one project or initiative to ensure their feedback is heard and incorporated into the project.

LESSONS LEARNED

“Working capital is not just a responsibility of finance or treasury.”

—Lakshan Fernando, senior treasury manager

Below are some of the lessons learned shared by the virtual site visit hosts in their journey to improve working capital management and cash flow intelligence:

- It is important to make performance and system metrics part of the everyday process.
- Key performance metrics should be reviewed on a firm schedule, not only with executives who are interested in and driven by them, but also with frontline employees who directly impact them. Frontline employees may not understand all of the metrics, but if they are looking at them on a weekly basis, when they grow into leadership positions they will have a firm grasp on the operations of the business and will know the drivers behind the metrics and how to improve them.
- Ensuring the right project sponsor for the project is critical. Project sponsors need to be active (not just sponsors in name only) and need to provide credibility to the project.
- Cross-departmental collaboration is key. Working capital management is not just a responsibility of the finance department, and the more that finance shares information with other departments, the more the other departments realize that and take an active role in managing their piece of working capital. The key to success is ensuring that all employees understand their role in, and impact on, working capital management and how their specific function contributes to the health of the overall company.