



## **Case Study: Efficient Cash Management Supports Growth**

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*Efficient cash management and trade finance, combined with aggressive vertical integration, meant that the Indonesian mobile phone company Selular was able to succeed despite the recession.*

2010 is looking good for Selular. The company has announced a predicted growth in profits of 20%, with expected sales growth of 38%. Such impressive figures have been made possible through the company's strong strategic initiative in the uneasy market of 2008 and 2009.

Indeed, these predictions are a long way from where the company found itself in the last quarter of 2008. Then, with the world in recession, we were presented with several challenges. Normally, the fourth quarter is our best performing of the year, with Christmas, Chinese New Year and Muslim holidays all falling during this period. Yet in 2008 this was not the case and our sales took a dive.

Problems also arose in Q4 in the form of currency fluctuations. In the space of a month, the exchange rate of US dollars to Indonesian rupiah fell by 30%, making US\$1 equivalent to 12,000 rupiah.

This drastic and rapid depreciation in foreign exchange (FX) rates was a blow to Selular, because we import in US dollars and sell in rupiah. Our prices are pegged to exchange rates, so when there is such fast change, sales inevitably fall. Indeed, sales dropped at the end of 2008 and - rather than restock in Q1 and Q2 of 2009 - we chose to run down our stock for as long as possible, clearing over three months worth of stock before reordering.

Yet with economists predicting a bleak outlook for 2009, we needed a plan to pull through the recession safely. As with any large business, there are fixed costs to maintain and, with 27 branches across Indonesia, one option was to close some down.

Selular has previously focused on the higher-end phones such as Blackberry. However, this misses around 70% of the Indonesian market, which uses phones costing under US\$100. Therefore it seemed sensible for us to examine the lower end. However, we decided upon a more positive path.

As we were already a distributor of Sony Ericsson, Motorola, Blackberry, Samsung, Nokia and HTC throughout Indonesia, a potential area of growth for us was the local market. The lower end of the Indonesian market is dominated by Nokia, and Nexian, which is a distinct local brand. Having previously worked with Nexian - and given that we were looking to expand in to the lower end of the market - we purchased a majority stake in the company. The acquisition of Nexian meant that we could vertically integrate into handset manufacturing without having to start a local brand from scratch. And as Nexian already made phones in China, it had built up expertise as a Chinese original device maker (ODM) buying phones and finding technical solutions with manufacturers and operators. We could not have achieved this on our own at such speed.

Despite the potentially difficult timing of the acquisition, Nexian and Selular sit well together. Selular has strong financing and credit facilities, and strong distribution and retail, which carry advantages for the

smaller Nexian. The fact that in the six months after the acquisition, Nexian sold 2.5 million handsets and achieved a turnover of US\$150m speaks volumes for the success of our strategy to grow our way out of the downturn. Telkomsel, a local service provider, now has 1.8 million subscribers using Nexian handsets, while XL Axiata has another million. As total phone sales volume in Indonesia is 1.8 million units, Nexian is crucial to our business.

The financing of the deal was executed through a working capital facility. This was arranged and executed by Falcon Trade Corporation, who offered a financing package based on their strong knowledge of the company. Our relationship with Falcon has been built up over several years, having evolved from a strong trade services-related partnership.

### ***Cash Management***

One challenge of the acquisition, however, was that it further complicated the structure of the business, making it vital for our cash management needs to be handled effectively. And with retail outlets nationwide selling own brand and other products, the efficient movement and handling of cash became more vital than ever.

For the past five years, Selular's cash management needs have been met by a basic enterprise resource planning (ERP) system, Microsoft Navision. It is connected live via a server in Jakarta, making it possible to see money coming in to all our outlets on a minute-by-minute basis.

For retail sales, cash is banked on the same day or the following morning. Each branch has a bank account, the contents of which are swept into a central account that can be accessed online.

As money coming in and going out can be seen on an up-to-the-minute basis, the weekly cash flow forecast can be predicted more accurately because of the centralised cash management system (CMS). Our forecasts are two months ahead and their accuracy has a major impact on our foreign currency as well as our working capital management needs.

As stated, we buy in US dollars and therefore need to purchase US dollars every day. The centralised system means that Selular can avoid overbuying. Also, the system prevents pockets of idle cash from being unused, meaning our level of borrowing has been significantly reduced. Indeed, Selular's overdraft has been reduced by around 20%.

We also have an internal system for working capital optimisation, driven by the weekly estimates and cash flow forecasts. We can show balance sheets and incomings on a screen on a daily basis. All branch numbers are consolidated onto one system, so that cash requirements are efficiently managed.

In order for our working capital to be optimised, we have also used trade financing facilities. For example, Sony Ericsson - of which Selular is a major distributor - can give us credit for 30 days, but this is only a partial benefit in a cash cycle that takes two to three months to complete. Falcon Trade is a major partner in providing for the shortfall with invoice discounting of up to 180 days. Falcon provides invoice financing in US dollars - and this plays a vital part of our cash management strategy. Meanwhile, we use local banks for rupiah financing. There is also a standby letter of credit (LC) facility that covers any credit risk to the vendor.

### ***Outlook for 2010***

The success of the Nexian acquisition has helped our recovery from the recession, allowing us to look forward with optimism. The Indonesian market has huge potential growth. Of the country's population of 250 million, only 120 million own a mobile phone, meaning over 50% of the population remains phoneless. If Selular can tackle this area of the market, the opportunity for growth is vast.

In this respect, Nexian will provide Selular with many more opportunities to penetrate the market in Indonesia. There are four million Nexian users in Indonesia and, by the end of 2010, the aim is to reach 10 million. To achieve this, Nexian must become a brand that is relevant to the local market, which we think is possible by following the local fashion for phone accessories.

Indonesians are particularly keen on phones with a 'QWERTY' keyboard for texting and email and our aim is to make Nexian fit in with this trend. Indonesians are also keen on using their phones for chatting and Facebook. The aim is to create a Nexian messenger - similar to Blackberry messenger - that will help to create a local community of Nexian users.

Applications (apps) for phones can also be used to win over the local market. As a rapidly expanding area of the global phone market, Indonesians are keen on buying apps for social entertainment and business uses. We see apps becoming as important as - if not more important than - phones themselves. One way for Nexian to take a slice of this is to give away apps specifically designed for the local market. And as part of our vertically-integrated business model, Selular is planning to acquire an apps company, which would help to drive local interest in apps whilst ensuring that it can take a share of the money to be made in this area. Offering local apps is perhaps the most effective way of achieving this.