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Improve Cash Flows and Drive Sharper Decision Making with Cognitive Accounts Receivable (AR) Analytics

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Increase visibility and predictability into accounts receivable function by leveraging automation and cognitive, machine learning-based analytics.

In an environment of increasing economic uncertainty, it has become imperative for businesses today to focus on agility and continuous innovation. As a result, finance executives have begun to rethink their conventional approach to orchestrating the overall Order-To-Cash (O2C) process. They are now looking to leverage disruptive analytics solutions based on Big Data and Machine Learning technologies to gain better visibility and predictability around the O2C process. Such solutions can also help identify automation opportunities across the O2C value chain, enabling enterprises to achieve the desired business outcomes at speed and scale.

While the O2C process is closely linked to the Finance & Accounting (F&A) function, the respective teams are under huge pressure to deliver more value, and contribute toward improving working capital management. The following are some of the key focus areas for F&A executives:

- Reducing overall costs of AR Function and maximizing cashflow.

- Decreasing working capital tied up in accounts receivable (AR), measured by Days Sales Outstanding (DSO).

- Generating deeper insight on customer payment behavior through pattern analysis.

- Identifying process-related gaps and optimization opportunities; for example, reducing invoice rejections and reprocessing.

- Enhancing predictive capabilities to anticipate write-offs, for minimized delinquencies, through constant focus on recoveries.

- Increasing emphasis on the "Power of Machine Learning" to build risk-scoring model and prioritize collections.

However, there are many challenges. Finance professionals across enterprises worldwide attribute the hurdles in orchestrating effective F&A processes to the following factors:

- Increase in collections volume with same or reduced staff

- Rise in DSO and past due accounts receivable

- Difficulty in prioritizing collection activity

- Increase in dispute-related invoices

- Inability to score customers/poor view of ongoing credit risk

- Difficulty obtaining risk data for emerging markets

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Furthermore, for several companies, DSO is usually running higher than the industry average, or organizations are not sure about the relevant benchmarking against best practices. Very few companies have fully automated their entire order-to-cash process, with most still using traditional methods for prioritizing collections and not adopting statistical, machine learning models for prioritization.

There is clearly a pressing requirement for automating order-to-cash processes, in order to boost cash flows and make the AR function more efficient and agile. The starting point for any such process transformation to be successful is the organization's ability to achieve end-to-end operational visibility, and perform root-cause analysis. With the advancement of technologies and access to more data, there are plenty of possibilities for improving the AR function and cash flows for the organization.

Broadly, there are three essential solution blocks for designing and implementing an effective AR solution and extracting significant business value:

Visibility

about Account Receivable Process to guide business decisions.

Improving financial and operational visibility provides the necessary transparency and insights into cash flows, real-time view of cash balances and customer credit balances, as well as overall receivables processes and working capital management. Often, organizations consider effective accounts receivable (AR) process management and strong analytics in isolation. They might use an enterprise-class reporting system that delivers standard aging reports, but decision makers still lack the requisite visibility for uncovering process-related gaps and gaining a vantage point for accurate trend analysis. In the absence of real-time, accurate AR metrics at an enterprise level, organizations struggle to transition from a reactive process management setup to one

oriented toward proactive decision making. Process owners find it time-consuming to gain insights into key performance indictors associated with different processes. Consequently, stakeholders are unable to take timely course corrective measures and fully optimize AR processes.

Monthly scoring of the AR portfolio can help companies find valuable clarity around portfolio risks, and target, on a priority basis, companies with the least propensity to pay. While most companies look at DSO and past due AR data, only a few employ more insightful KPI tracking methods, such as the collections effectiveness index, or root-cause analysis for reduction in dispute volume.

Predictability and Risk-Based Collection

about the process outcome and associated risks.

The ability to foresee the likelihood of late payments prior to the due date of the invoice, with the capacity to identify the root cause can enable organizations to plan operations more effectively. The emergence of risk-based collections has heralded the emergence of lesser known, yet more effective, statistical credit scoring models for predicting AR delays. These models are designed to ascertain the inherent risk of a customer, including the probability that the customer will become seriously delinquent, ask for a write-off, or file for bankruptcy at some point in the future–usually within six months from the scoring date. Statistical models "quantify risks" by stating the odds of delinquency, helping

AR departments evaluate and quantify risks from a dollar perspective.

From this standpoint, access to historical data is vital for building a successful statistical model that can accurately predict risks. AR departments often utilize internal data including information concerning the payment history of individual customers. Scoring models that deploy real data derived from existing customer payment behavior patterns have a proven track record of outperforming judgmental and generic credit scoring models. Moreover, for reliable predictive analytics, statistical models have always proven to be superior to their judgmental counterparts. When analyzing the same set of customer data in the same period, statistical scoring models predict delinquency with higher accuracy.

Moreover, enterprise finance and accounting teams can now harness a risk-based strategy for institutionalizing a proactive approach toward collections. Adopting statistical risk scoring allows firms to analyze their customer base and re-prioritize collections accordingly. While traditional reports provide a summary of current collections, a risk-driven scoring methodology facilitates risk assessment based on current and historical invoices. This generates a realistic risk profile of the customer, determining the probability of late payments or delinquency.

In addition, in order to accurately assess the return on investment generated by stretching payment terms, enterprises have to carefully evaluate several parameters. Subsequently, they apply the concept of risk-based collections by factoring in various aspects including the

customer's ability to pay, credit rating, agency data, relative industry, and geographic location. Other relevant determinants in this regard include invoice value, age of balance, remaining credit limit, capacity to employ alternative payment methods, historical payment behavior and potential commercial risks.

However, for truly establishing the most effective utilization of a specific receivable, companies have to determine the probability of payment, as well as layout a robust classification system. By designating customers' different categories such as the probability of loss or late payment, firms can segregate their receivables and determine the optimum approach. For example, an enterprise categorizes its receivables under different customer clusters–those likely to make timely payments, the ones expected to default and those that will drive larger losses. Classifying clients in such a manner can allow the company to implement tailor-made solutions for each of these categories, and thereby ensure high liquidity at minimal costs.

Performing collection risk-based statistical scoring should, therefore, be an integral part of the collections practice. It should always constitute a core component of the cash flow forecasting process; be it in driving and predicting free cash flows, mitigating bad debt, or even reducing counterparty risks around suppliers.

Automation

to boost productivity gain and drive efficiency.

Lack of automated processes results in increased past-due receivables, creating a pressing need for automation and augmented operational efficiency in collections. Moreover, even as a spike in manufacturing and orders triggers a natural influx in collections activity, there is often little appetite for boosting staffing. In addition, the correlation between adding staff and improved results is often intangible.

Automating the account receivables processes can help organizations realize significant efficiency and productivity gains, in terms of growing collections and reducing DSOs. Minimizing manual interventions across the O2C life cycle can also enhance supplier and dealer relationships. Proper routing of disputed issues, through streamlined workflows, would also reduce the overall dispute cycle time.

Automation can pave the way for increased productivity and effective management of collections, by helping prioritize various underlying activities, and allocating resources prudently to the highest risk accounts. Beside minimizing manual dependency, automation improves productivity while reducing the drain on resources on the organization. There are several areas of application for efficient use of automation, including chasing disputed invoices, prioritizing collections, identifying and mitigating risks, and setting and sending reminders including reporting and organizing call queues and managing disputes.

As companies face growing pressure to manage more responsibilities including rising invoice volumes, with less infrastructure and resources, there is an increased demand for automation and machine learning-based holistic A/R solution.

Accounts Receivable is a key function in the O2C process, directly impacting the top line and bottom line performance of an organization. If the sales teams responsible are not enabled to manage the collections process, it can lead to delayed payments or losses due to write-offs. Furthermore, persistent follow-ups can negatively impact customer relationships.

The secret weapon

REDaxis (Reduce DSO exponentially through automation, insights and statistical modeling), LTI's powerful persona-based analytics suite, has been built to optimize accounts receivable (AR) operations through actionable insights and

enhanced user experience, thus enabling execution from the point of identified action.

During the course of the collections process, our suite helps improve relationships between sales teams and customers, thus delivering exponential savings to our clients.

Its salient features include:

- Intelligent business signals through predictive algorithms to detect DSO patterns, potential write-offs and false discount claims.

- Ready KPI library and data model mapped across the AR Function value chain.

- Context or role-based (CFO, AR operations executive, Sales Manager, etc.) analytics insights with advanced visualization.

- Drill down capabilities at a granular level through intuitive dashboards/reports.

- Ready-to-deploy, cloud-based solution with a scalable architecture that caters to business growth and users from multiple geographies.

- Powered by LTI Mosaic, solutions developed for ERP customers, specializing in streamlined data sourcing and simplification of data development with connectors to all major ERPs.

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Business Outcome

Improved visibility
in customer payment behavior

Boosted
cash flows

Lowered probability
of customer delinquency
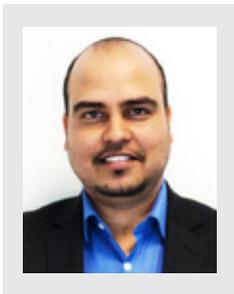
Augmented
collection efficiency

Reduced DSO
by significant margins

Enhanced access
to real-time information on pending collections

Click here to know more about the REDaxis Suite

About the Author

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Rakesh Sancheti is Vice President & European Business head for Cognitive & Analytics Practice for LTI. He is a technology evangelist, with 12+ years of consulting and delivery experience in helping customers drive cognitive-led digital transformations. He is a thought leader and passionate about possibilities presented with converging technologies like IIoT, Automation, Big Data, Analytics and AI for Businesses & societies. He has worked with clients across the globe to deliver solutions across Digital portfolios with a specialization in the Data to Insight value chain - Data Integration, Data Management, Business Intelligence, Big Data, Data Science and Machine Learning.

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