



Global Green Growth Institute

Ninth Meeting of the Management and Program Sub-Committee

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Increasing the level of GGGI's Working Capital

Background

1. GGGI began 2016 with total reserves of USD 33.8 million. This comprised USD 10 million of working capital and USD 23.8 million of retained surplus. During 2016 the institute recorded a net surplus for the year of USD 11 million resulting in total reserves of USD 44.8 million: comprising USD 10 million of working capital and USD 34.8 million of retained surplus. Members of the Council considered that the institute should not accumulate such large amounts of retained surplus. They instructed GGGI management to spend down the retained surplus to zero (targeting reserves of \$10m, equal to the approved level of working capital). Consequently a 2017/18 Work Program & Budget (WPB) was presented and approved which aimed at writing down the retained surplus over the biennial period 2017/18.
2. At the end of 2018 GGGI had total reserves of USD 17.4 million comprising working capital of USD 10 million and retained surplus of USD 7.4 million. The spend down of the retained surplus from USD 34.8 million to USD 7.4 million was achieved by recording operating deficits of USD 13.5 million in 2017 and USD 13.9 million in 2018.
3. During the biennial period 2017/18 GGGI spent heavily from its retained surplus to maintain operating capacity in its expanded network of country offices with the intention that by 2019/20 many of those country operations would become mainly self-sufficient. This would be achieved by largely funding country activities through earmarked funding. This strategy has proven generally successful as demonstrated by increasing annual expenditures which will be funded out of increased levels of earmarked funds.

Working Capital Days

4. Working capital days is a financial ratio used by many organizations operating in the not for profit sector. It is a measure of the amount of working capital expressed in days of expenditure. It is calculated by dividing the amount of working capital (in GGGI's case USD 10 million) by annual expenditures and multiplying by 365.
5. GGGI's total expenditures have increased from USD 41 million in 2016 to USD 44.1 million in 2017, USD 49.5 in 2018 to a budgeted USD 53.2 million in 2019. Working capital of USD 10 million equated to 89 days at the end of 2016, 83 days at the end of 2017 decreasing

to 74 days at the end of 2018 as total expenditures increased. This is projected to further decrease to 69 days at the end of 2019 as expenditures increase to a budgeted USD 53.2 million.

6. With GGGI's expenditures projected to continue to increase over the next number of years as more countries come on board and as earmarked funding increases it is appropriate that the council again consider what is the most appropriate level of working capital for GGGI.

Purpose of Working Capital

7. Generally, in not for profit organizations the purpose and the real need for working capital is as follows:
 - For cash flow purposes – by ensuring that cash/funds are available for financing of operational expenditures during the earlier part of the year particularly when funding from contributors is received later in the year.
 - For providing a degree of financial stability - this gives confidence (to staff, management, contributors, suppliers, etc.) that there will be some degree of continuity of operations should there be a loss of funding from one or more of its core contributors. Thus, if there is a permanent reduction in funding GGGI has the available funding to right size the organization in an orderly manner to fit the new funding reality.
 - Enables GGGI to meet temporary shortfall between anticipated income and the institute's expenses.
 - Give flexibility to respond to emergency situations appropriately, e.g. natural disasters, emergency evacuation from a country following political turmoil.

International Benchmark

8. While it is clear that working capital is required for an organization to finance its operations, there is no universal standard as to what the required level should be. Some considerations:
 - A commonly used working capital goal is 3-6 months of expenses i.e. 90 – 180 days of operating expenditures
 - Some international organizations like the CGIAR, an international agricultural research network comprised of 15 centers, have set their benchmark at the 75 -120 days of working capital with an average per center of 112 days.
 - Marie Stopes International, a family planning international NGO, has a working capital of 145 days.
 - The US benchmark for not for profit organizations is generally set at the 6 month or 180-day level.

Going concern assumption

9. The usual assumption is that the level of working capital is set on a “going concern” basis. If there is a real possibility of cessation of operations, then the level of working capital should correspond to the cost of an orderly closing of the institute, settling all liabilities.

Proposal

10. GGGI’s annual expenditures have been growing annually. Expenditures in 2018 were USD 49.5 million which is an increase of USD 5.4 million or 12.2 per cent over expenditures of USD 44.1 million in 2017. For 2019 budgeted expenditures are USD 53.2 million which is an increase of USD 3.7 million or 7.4 per cent. The annual rate of increase is declining but if we assume a rate of increase of 5 per cent per year then they would increase to USD 56 million in 2020; USD 58.6 million in 2021 and USD 61.6 million in 2022. Such a rate of increase does not seem unreasonable.
11. Assuming the standard International benchmark to be in the range of 75 – 120 days of working capital, GGGI management are proposing to increase the level of working capital from USD 10 million to USD 15 million. This would result in a working capital level of 103 days at the end of 2019 decreasing to 89 days in 2022 assuming that expenditures grow by 5 per cent annually from 2019 onwards.

Table 1: Proposed working capital & working capital days

	2018	2019	2020	2021	2022
Annual expenditures (US\$'M)	49.5	53.2	55.9	58.6	61.6
Working Capital (US\$'M)	10	15	15	15	15
Working capital days	74	103	98	93	89
Working capital days if working capital remains at USD 10 million	74	69	65	62	59

12. Total reserves at the beginning of 2019 were USD 17.4 million comprising USD 10 million of working capital and USD 7.4 million of retained surplus. The current operational budget of USD 53.2 million projects the further drawdown of USD 3.8 million from the retained surplus thus reducing them to USD 3.6 million at the end of 2019. Increasing the working capital to USD 15 million would require the transfer of USD 5 million from the retained surplus thus leaving it in a deficit of USD 1.4 million. Management propose to budget for an operating surplus in the period 2020-2022 to reduce the deficit of USD 1.4 million to zero.

Action Required

13. Members of the Management & Program Committee are asked to endorse the proposal to GGGI Council to increase the level of working capital from USD 10 million to USD 15 million.

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