

## FinancialQuotient

# What is 'days payable outstanding'?

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### WHAT DOES IT MEAN?

Days payable outstanding (DPO) refers to the average number of days a company takes to pay its suppliers. It can be estimated by dividing the average account payables of the company, say, over a year, by its average daily purchases from suppliers. It can also be computed over a monthly or quarterly period.

### WHY IS IT IMPORTANT?

DPO is a reflection of how quickly the company needs to pay its bills

from the suppliers. An increase in DPO over time indicates that the company is taking more time to part with its cash to pay the suppliers. The longer the DPO, the longer the cash is kept within the company to generate more economic returns.

DPO is also a reflection of the company position vis-a-vis its suppliers and its own cash-flow situation. An increase in DPO over time may be an indication of an increase in the bargaining power over the suppliers.

However, it may also be an indication of a cash-tight situation within the company. In the latter case, the

company is delaying parting with its cash by stretching its payment periods with suppliers.

A decrease in DPO over time may indicate other situations with the company, such as a loss of bargaining power with suppliers or a rise in suppliers' concerns about the credit standing of the company. In both cases, suppliers are expected to demand faster payment of their bills to the company.

By examining how DPO changes over time, one can detect subtle changes in a company's credit standing and its supplier relationship.

### IF YOU WANT TO USE THE TERM, JUST SAY:

"As the company consolidates its order of raw materials to fewer suppliers, it is able to negotiate for a better and longer payment term with its suppliers and thereby manage to improve its days payable outstanding."

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