PrimeRevenue

6 Ways Automotive Companies are Using Supply Chain Finance to Fund the Future

Overview

As transformation reshapes the automotive industry, its business leaders face a critical obstacle – liquidity. The scale and pace of this transformation is forcing automotive manufacturers, OEMs and suppliers to make massive and costly changes to their businesses. According to PwC's Global Innovation 1000 study, automotive companies made up six of the top 20 R&D spenders in 2017. That's a telling statistic given the fact that the list also includes names like Amazon, Microsoft and Apple (note: Volkswagen spent 21 percent more than Apple on R&D).

"How will we fund X strategic business initiative?" is a question that weighs heavily on even the largest, most profitable automotive companies and especially on suppliers that lack access to investment-grade funding.

For many businesses across the automotive supply chain, the answer is supply chain finance.

Unlike commercial-based lending, dynamic discounting or early payment programs, supply chain finance is a win-win for all parties involved. It doesn't negatively impact the balance sheet (for buyers or suppliers) and suppliers are paid the full amount due for invoices. Most importantly, the cash flow gains delivered are substantial enough to fund the kind of large-scale strategic business initiatives that often require billions of dollars in working capital.

What is Supply Chain Finance?

Supply chain finance improves cash flow by allowing companies (buyers) to optimize payment terms with their suppliers. At the same time, it provides suppliers a way to get paid early by a third-party – typically a financial institution. By increasing the time it takes to pay suppliers, buyers can free up cash that would otherwise be trapped within the supply chain. Likewise, by enabling suppliers to be paid early by another party, suppliers can accelerate their own cash flow.

Fueling Tomorrow's Success. From luxury car brands to niche suppliers, an increasing number of automotive companies are using supply chain finance to fund the changes and transformations that will power their future. These initiatives include:

1 Innovation investment

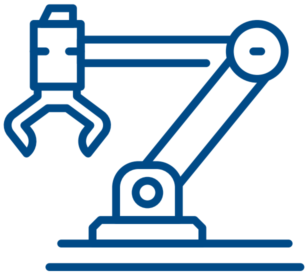
Autonomous driving, embedded digital services and EVs are just three areas driving significant investment across the automotive supply chain. Historically, companies have used their own balance sheet to pay for these large-scale innovation programs – whether by increasing debt, austere cost cutting and/or restructuring, or the sale of assets. Supply chain finance provides an attractive, off-balance sheet alternative to these measures.

Take one of the **world's largest truck manufacturers,** for example. The manufacturer's current growth strategy includes the introduction of new EV fleets across numerous markets as well as significant R&D into self-driving capabilities. To efficiently execute this growth strategy, the manufacturer realized it needed to better manage the amount of working capital tied up in its inventory. Through a supply chain finance program facilitated by PrimeRevenue, the company has accomplished just that – achieving total cash flow gains in excess of $700 million.

2 Fund M&A success

The race to innovate is driving up M&A activity across the automotive sector. According to an annual report by PwC, the value of M&A activity in the industry increased by 30 percent in 2017 to $53.2 billion. One particular area of growth is in the component supplier market where PwC reports deal volume increased by 70 percent in the same year. The trajectory shows no signs of slowing down as companies reconcile their growth and innovation strategies with an evolving automotive ecosystem.

Mann+Hummel, a maker of automotive filtration products, is an example of one company that's using supply chain finance as a way to help fund strategic acquisitions. Its rapidly growing supply chain finance program (powered by PrimeRevenue) has generated significant cash flow gains that have helped the company execute numerous acquisitions to expand its production capabilities and product portfolio.



3 Build out new infrastructure to support evolving production demands

The transformations happening across the automotive industry are making sweeping changes to production requirements for both OEMs and suppliers. Furthermore, the cost to produce vehicles is at an all-time high – as much as 20 percent higher than the previous generation. Whether through building out new production capabilities or acquiring them outright, like Mann+Hummel in the previous example, companies are using supply chain finance as a funding mechanism to meet changing production requirements.

ZM Silesia, a supplier to Michelin and a participant in Michelin's supply chain finance program, claims early payment on invoices has generated enough cash to grow and reinvest in new machinery, plants and equipment.

4 Invest in education to overcome labor shortage

In a recent survey, the National Association of Manufacturers reports that 64 percent of respondents cited attracting and retaining a quality workforce as one of their top challenges. In response, many automotive OEMs are taking matters into their own hands.

PrimeRevenue customer **Michelin North America**, located in the upstate South Carolina corridor, has partnered with local technical colleges to offer the Michelin Technical Scholars Program.

This program provides opportunities for select students to develop hands-on work experience with competitive pay while earning their degree in Mechatronics Engineering Technology.

These programs require substantial economic investment that, in the absence of off-balance sheet funding options, could negatively impact profits. Improved control over cash flow has enabled Michelin (and many others in the industry) to unlock large sums of working capital that can be used to solve complex business challenges, such as this one.

5 Increase financial agility

The current state of the automotive industry has underscored the need for greater agility. Transformation breeds innovation and opportunity, but it also creates chaos and instability. Having the financial agility to navigate those threats is vital. This is especially true for sub-investment grade suppliers and/or suppliers that want to access liquidity at lower funding costs.

Belgium-based **ALRO Group** is an example of the latter. The company provides surface treatment of plastic and metal automotive parts for many leading luxury car brands. During the global financial crisis, the company sought a cost-effective way to improve its cash position and turned to the supply chain finance program of one of its largest customers. By participating in the program, the company was able to receive near-immediate payment for invoices rather than wait 75+ days. Fast-forward to today (and the industry challenges that define today's business landscape), and ALRO Group continues to benefit from the cash flow improvements delivered by supply chain finance. In the last five years, the company has traded over $110 million in invoices and receives payment 104 days early on average.

6 Increasing enterprise value

Amid the changes happening across the industry, a more scrutinous eye is being applied to companies' profitability and value-creating potential. "How can we increase return on capital?" is one question financial executives must answer in the face of higher capital spending, and supply chain finance is one way for them to turn up the dial.

One global supplier's five-year growth plan included very specific goals in this area – including delivering **$1 billion+ in additional cash flow** and achieving a minimum of 15 percent return on capital. Within months of implementing a supply chain finance program with PrimeRevenue, the company had unlocked more than $100 million in cash flow.

Liquidity and Agility Through Supply Chain Finance

The price of transformation continues to be high for automotive companies, and it's one reason why industry leaders are embracing supply chain finance. By materially improving cash flow, supply chain finance can unlock large sums of working capital that can be used to fund mission-critical business initiatives.