INSIGHTS FOR A SUCCESSFUL SUPPLY CHAIN FINANCE PROGRAM

Separating Fact vs Fiction

PR PrimeRevenue

In today's multinational supply chains, efficiency is top-of-mind for companies seeking ways to boost productivity and financial health. Global economic and supply chain disruptions are testing this governing principle in new ways – and many companies are concerned they're not doing enough. The efficiency gains achieved through decades of offshoring and outsourcing have been eroded by rising labor and shipping costs, and these challenges are exacerbated by the long-tail impact of an increasingly global and complex supply chain landscape.

There is a tremendous amount of working capital trapped in most supply chains. Unlocking this capital has the potential to increase cash flow, improve financial health and strengthen competitive advantage for all supply chain constituents. As a result, companies can free up funding for new efficiency focused innovation and process improvements.

For many businesses, supply chain finance has become integral to optimizing working capital. Having made the leap from niche to mainstream, supply chain finance helps companies around the world unlock significant amounts of cash flow each year. Despite these successes, there are many myths surrounding supply chain finance and how to leverage it to its fullest potential.

This white paper debunks some of the most common myths surrounding supply chain finance to help companies better understand the extraordinary potential a working capital improvement strategy can deliver to their businesses.

What is supply chain finance?

Supply chain finance is an effective tool to optimize working capital and reduce supply chain risk by allowing businesses to increase supplier payment terms while providing the option for their large and SME suppliers to get paid early.

MYTH 1:

Bank funding is committed in a supply chain finance program, which negatively impacts a company's balance sheet

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FACT:

Unlike a loan or revolving line of credit, bank funding within a supply chain finance program is uncommitted. It is not a loan or a tactic that impacts credit rating because companies aren't "borrowing" money. Instead, the funding is transactional and accounts payable are not reclassified as financial debt. In other words, it stays off the balance sheet.

That's great news for companies that want to improve working capital without affecting credit rating. For some, this is a great way to leverage existing banking relationships. However, bank-led supply chain finance programs have risks. Uncommitted funding means a financial institution can reduce funding, increase spreads or in the worst case, withdraw completely from a supply chain finance program at any time.

> Bank-led programs bring unwanted risk to supply chain finance. That's why many companies are implementing multi-funder programs instead.

Recent turbulence in certain markets and industries has impacted bank behavior – regardless of whether a company's creditworthiness has changed. Without the full participation of the financial institution leading the supply chain finance program, these companies have experienced higher costs and reduced credit limits.

To counter these challenges, many companies are turning to supply chain finance programs that aren't led by a single financial institution. Instead, they're implementing bank-agnostic, independent programs that provide companies the flexibility to easily switch between different funders or supplement with additional funders as needed. Through a multi-funder platform, these companies have greater access to liquidity and more control over how they operate their supply chain finance program. Further, companies can create new funding relationships outside of their relationship banks in addition to leveraging existing relationship banks.

MYTH 2:

Success depends on the number of suppliers participating in the program

FACT:

While it's true that most successful programs have a high volume of suppliers, what truly matters is whether suppliers are getting value from program participation.

In most cases, companies implement supply chain finance in conjunction with a terms extension initiative. Relationships are key in business – and slapping a supplier with a blanket term extension without providing a way to offset any potential negative impact is a great way to add strain to new and longstanding supplier relationships. Supply chain finance offers suppliers a tool to mitigate the cash flow disruption that can come from extended terms.

However, if a supplier doesn't get value from a supply chain finance program, it doesn't entice them to participate, and they will be less willing to accept a payment term extension.

> The bottom line is this: any business relationship must have mutual benefits. Most suppliers are already resistant to extended payment terms. It's even less attractive if they aren't receiving value elsewhere in the relationship.

That's why it's important to offer suppliers not only the opportunity to receive early payment, but also a platform that provides transparency and enhanced reporting capabilities.

PrimeRevenue's SurePay Platform provides increased visibility into invoice approval status and upcoming payment information. Suppliers can easily see which invoices have been approved for payment as well as what payment is coming and for how much. The SurePay Platform also automated tedious AR tasks such as remittance advice so suppliers can focus on other value-add tasks for the business.

MYTH 3:

The invoice discount rate is the most important factor in a supplier's decision to participate in a supply chain finance program

FACT:

Discount rate certainly influences a supplier's decision, but it's not the only consideration in the decision to join a program. Research shows the main consideration for a supplier is the financial value of on-demand liquidity compared to the cost of capital.

What really motivates a supplier to join a supply chain finance program? Many corporations believe the size of the discount rate deducted from the supplier's invoice balance is the primary consideration. Research indicates this isn't necessarily the case.

> The main factor for a supplier joining a supply chain finance program is the financial value of on-demand liquidity versus the cost of capital.

Sure, a lower interest rate than traditional financing is certainly enticing – however, flexibility to choose when to get paid in addition to certainty of payment date is arguably even more valuable.

Whether suppliers decide to take advantage of early payment or not, a supply chain finance program guarantees on-time payments. This is massive value-add considering nearly 50% of suppliers cite late payments as their most pressing payments challenge.

Another determination is related to materiality of sales with a customer. In other words, if a company introduces a program to a supplier, and that company is one of the supplier's biggest customers, then the supplier will be more motivated to join. Being paid early for a stream of large invoices means a higher volume of cash available on demand.

MYTH 4:

Multinational banks can fund all currencies and jurisdictions

FACT:

Just because a bank has a global presence doesn't mean they can serve all geographies. No one bank – no matter how global – has the processes and systems in place to serve all necessary currencies and jurisdictions.

This is an important factor to consider given the breadth of most global supply chains. If a company implements a supply chain finance program led by a single bank, and that bank can't serve key suppliers in certain parts of the world, the efficacy of the program is diminished.

Best-in-class supply chain finance programs, such as the ones implemented by Volvo, Co-op and Boston Scientific, are based on multi-funder platforms – rather than closed, bank-proprietary platforms.

These multi-funder platforms outperform bank-proprietary platforms in three areas:

Scalability. Technology provides the productivity and connectivity that allows a team that is lean or with limited resources to manage the requirements of a growing program. Adding new headcount or bank systems every time new suppliers are onboarded is simply not necessary when a single platform can provide that scalability in one bank-agnostic place.

Scope. Large corporations must be able to administer global supply chain finance programs. Multi-funder solutions support multiple jurisdictions, currencies and payment terms by being able to adapt the funding mix to the current needs of the program, wherever and whenever required.

Flexibility. Companies need the flexibility to work with multiple banks or use their own balance sheet (self-funding) without adding complexity to the operation or significant workload to the team. A bank-agnostic platform makes it as easy to connect to multiple funders as it is to connect to a single bank.

Finally, it's important to note the inherent benefit of "options" when working with a multi-funder platform. Global supply chains are uniquely susceptible to changes in the economic and geopolitical landscape. This is evidenced by the economic and supply chain crises of recent years. A supply chain finance program that's locked into a sole source (or highly limited source) of funders is held hostage to the funder's risk tolerance – which is constantly changing. For companies to deploy supply chain finance programs successfully, they need a promise of stability. More funders at the table delivers this in a way that no single financial institution can.

MYTH 5:

Bank syndication solves the problem of single-funder supply chain finance programs

FACT:

Contrary to popular belief, the limitations and challenges are largely the same. While there are multiple banks involved, they all participate through the lead bank and its proprietary platform. That means they adhere to a single set of rules and process/technology limitations.

In some single-funder supply chain finance programs, the lead bank will syndicate liquidity requirements to other banks. In these instances, the lead bank will invite other banks to join the program because it can't meet the funding requirements of a large supply chain.

This strategy has the same risks involved with a single-bank program. Not only is there little competition around best practices, innovation or pricing, the lead bank can shut down the program at any time.

A bank-agnostic supply chain finance platform allows participation from multiple independent banks and alternative funding sources. It ensures efficiency, competition and innovation across many program parameters whether it's currency, jurisdiction or pricing. This is why bank-independent platforms were the first to implement innovative features such as electronic supplier agreements and web-based supplier enablement tools. In fact, independent platforms are still the only solutions to offer electronic time drafts to suppliers.

Compare this to bank-syndicated programs. Due to lack of competition, funding spreads are typically higher, especially over the long term. The lead bank will often charge syndicate banks an additional 20 to 50 basis points or more to participate in the supply chain finance program. If a particular bank wants to be aggressive in pricing or offer a discount to a particular supplier, they can't because pricing is set by the lead bank. The company has no visibility into pricing as they do with a bank-independent platform and, given the lead bank's monopoly on funding rules, it has no incentive to reduce pricing as conditions warrant.

The bottom line is this – a bank-independent platform with multiple funders allows the supply chain finance program to take advantage of the best of each bank's capabilities.

In Summary

A well-executed supply chain finance program can be transformative for global supply chains. Freeing up large sums of working capital can improve virtually every aspect of the business – financial health, productivity, competitiveness, innovation and more. But, it's important to understand how supply chain finance programs work, what motivates suppliers to participate and the pitfalls that often hinder success.

There are many misconceptions that should be clarified before a company embarks on a new supply chain finance initiative, the most important of which are the limitations of a single-funder or bank-led program. Lead banks in these programs aren't motivated to provide competitive financing, and lack the technology focus to provide platforms that are scalable and easy to use. In many cases, they aren't capable of serving the variety of jurisdictions and currencies that comprise a truly global supply chain. These limitations undercut the success of a supply chain finance program before it can even get off the ground.

The solution to this problem is neutrality. Independent, bank-agnostic programs that draw on multiple funding sources from across the globe breed innovation and competition among funders. The platforms that power these programs are designed with the company and supplier in mind, not for and by the funder. They provide intelligent supplier targeting capabilities that maximize the value for both the company and the supplier – ultimately creating a program that delivers on its full potential.

About PrimeRevenue As a pioneer in global B2B payments, the PrimeRevenue SurePay Platform connects the entire supply chain by improving working capital and automating digital payments. Thousands of companies around the world leverage one streamlined platform to increase payment visibility, enhance control, and improve cash flow. PrimeRevenue is headquartered in Atlanta, with offices in London, Prague, Hong Kong, and Melbourne. For more information, visit **www.primerevenue.com**.

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