Emerging Trends in Supply Chain Finance

By:

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ABSTRACT

In recent interviews with global traders about their supply chain finance programs, Global Business Intelligence discovered some important emerging trends. Because companies operate their supply chains on a global basis to compete, they are much more concerned about managing inventory and working capital. There are other forces driving opportunities in supply chain finance. To begin with, companies are rapidly increasing their planned direct imports and global procurements. This has major balance sheet implications, as many companies are accruing in-transit inventory at some point overseas. In addition, use of third parties to manufacture outside of the U.S. has exploded, while Internet-based technologies enable real-time exchange of information between trading partners about product and business data.

INTRODUCTION

Supply chain management (SCM) is the process of planning, implementing, and controlling the operations of the supply chain with the purpose to satisfy customer requirements as efficiently as possible. Supply chain management spans all movement and storage of raw materials, work-in-process inventory, and finished goods from point-of-origin to point-of-consumption. The term supply chain management was coined by consultant Keith Oliver, of strategy consulting firm Booz Allen Hamilton in 1982.

Supply Chain Management encompasses the planning and management of all activities involved in sourcing, procurement, conversion, and logistics management activities. Importantly, it also includes coordination and collaboration with channel partners, which can be suppliers, intermediaries, third-party service providers, and customers. In essence, Supply Chain Management integrates supply and demand management within and across companies.

ACTIVITES OR FUNCTIONS OF SUPPLY CHAIN MANAGEMENT

Supply chain management is a cross-functional approach to managing the movement of raw materials into an organization and the movement of finished goods out of the organization toward the end-consumer. As corporations strive to focus on core competencies and become more flexible, they have reduced their ownership of raw materials sources and distribution channels. These functions are increasingly being outsourced to other corporations that can perform the activities better or more cost effectively. The effect has been to increase the number of companies involved in satisfying consumer demand, while reducing management control of daily logistics operations. Less control and more supply chain partners led to the creation of supply chain management concepts. The purpose of supply chain management is to improve trust and collaboration among supply chain partners, thus improving inventory visibility and improving inventory velocity.

SUPPLY CHAIN ADVANTAGE SUITE

SUPPLY CHAIN FINANCE

"Supply Chain Finance" (SCF) is now taking on a distinct persona as a range of products that companies perceive they need, and indeed an area that banks are keen to develop to meet those needs. In another report from the Aberdeen Group, they note that, "The key benefits [of Supply Chain Finance] include the reduction of the cost of capital and more flexible cash flow for sellers, and easier access to credit and the ability to make more proactive use of accounts payable balances for buyers. By leveraging better visibility and control over supply chain transactions, SCF also enables cash and credit flexibility, including the ability for financing/factoring to be done at many more points in the supply chain – raw material, intermedia production, point of shipment, point of customs clearance, arrival at vendor-managed inventory hub, etc".This helps unlock the trapped value of goods throughout their lifecycle.

Supply Chain Finance (SCF) is the next wave of cost improvement for organizations. More than two-thirds of companies are investigating or putting in place Supply Chain Finance programs to improve financial metrics and lower end-to-end costs.

EMERGING TRENDS IN SUPPLY CHAIN FINANCE

In recent interviews with global traders about their supply chain finance programs, Global Business Intelligence discovered some important emerging trends. Because companies operate their supply chains on a global basis to compete, they are much more concerned about managing inventory and working capital. There are other forces driving opportunities in supply chain finance. To begin with, companies are rapidly increasing their planned direct imports and global procurements. This has major balance sheet implications, as many companies are accruing in-transit inventory at some point overseas. In addition, use of third parties to manufacture outside of the U.S. has exploded, while Internet-based technologies enable real-time exchange of information between trading partners about product and business data. We found the market is in the early stages of migrating to data triggered finance. These 6 triggers include:

Purchase Order Issue

While suppliers desire more offshore funds access, traditionally pre-shipment finance has been seen as a pure supplier responsibility and the local Asian bank domain. There are some banks that are playing in this space using buyer Master Purchase Orders for working capital facilities for key suppliers.
Work in Progress Payments

We found a small number of large (usually regional or global) banks with buyer support programs and Master Purchase Order contracts with medium to large Tier 1 and 2 suppliers who have performed well to contract over many years.

Vendor Managed Inventory (VMI)

Many high tech manufacturers in the 'made to order' business are using Vendor Managed Inventory programs. Lead Logistic Providers and major 3PLs are behind these programs and there will be a growing interest in trigger finance/payment when inventory is pulled from a warehouse.

Vendor-managed inventory (VMI) is one of the most widely discussed partnering initiatives for improving multi-firm supply chain efficiency. Also known as continuous replenishment or supplier-managed inventory, it was popularized in the late 1980s by Wal-Mart and Procter & Gamble. VMI became one of the key programs in the grocery industry's pursuit of "efficient consumer response" and the garment industry's "quick response." is Successful VMI initiatives have been trumpeted by other companies in the United States, including Campbell Soup and Johnson & Johnson, and by European firms such as Barilla, the pasta manufacturer.

Inventory in Transit Financing

There are a select few vendors that are going beyond the GT Nexus, Inttra and Tradebeam supply chain visibility models to enable international in transit inventory to be funded on a non-recourse basis to emerging market suppliers.

Proof of Delivery via Forwarder Cargo Receipt (FCR) and other documents

As more cargo is exported with electronic messages such as FCRs and advanced shipment notices, there will be more opportunities to develop liquidity off these messages. This trigger remains to be explored and developed.

Buyer approved Invoices

This is a post-shipment finance model that basically works like this: Bank provides overseas supplier early payments as financing from buyer accepted invoices. Buyer interfaces their AP or creditor ledgers to the Bank's working capital platform, which makes available to their suppliers approved payables that are both date and value certain.

The market is moving away from documentary based trade (Letters of Credit, etc.), making way for Open Account opportunities in supply chain trade finance structure. The time for your company to make the transition is now.

THE SUPPLY CHAIN FINANCE STRUCTURE

The process begins with the supplier sending an invoice to the buyer. The buyer approves the invoice and uploads it to the Supply Chain Finance (SCF) platform, thereby creating an irrevocable payment obligation. The supplier is now able to sell the invoice to the financier at an attractive rate, based on the buyer risk. The transaction is designed to be a “true sale” where the risk is transferred from the supplier to the financier. For example, in a supply chain with 75-day terms, it is possible for the supplier to receive payment on day 5, at a low SCF cost, while the buyer is able to pay the financier on day 75.

The success of a Supply Chain Finance solution hinges on the real-time visibility and integrity of invoice data, to enable all participants in the structure to track invoices, advance payments and settlements. If the process were not automated, the key efficiencies of lending against eligible invoices would be lost in the costs of manual processing.

IMPLEMENTATION PHASES FOR A SUPPLY CHAIN FINANCE SOLUTION

Most of the supply chain finance solution providers follow three phases for implementing the SCF solution, these are as follows:

Phase 1 – Feasibility

- Analyse the payables history of the buyer and their trading terms with individual suppliers
- Deliver an indication of the potential improvements and efficiencies in costs, payment terms and cash flow

Phase 2 – Implementation

- Design the optimum structure for the supply chain financing programme
- Work with suppliers to offer advice and training
- Test all aspects of the platform's performance rigorously prior to launch

Phase 3 – Processing

- Launch the programme
- Support the buyer and suppliers
- Add new suppliers and ensure their smooth integration into the ongoing programme

THE BENEFITS OF SUPPLY CHAIN FINANCE

Supply Chain Finance enables a company to leverage credit to maximize the efficiency of their working capital and enhance their relationships with their suppliers. The buyer can extend payment terms and the supplier receives advance payments discounted at rates considerably lower than their normal funding margins. The lender, in turn, gets the benefit of a margin higher than the risk profile commands.

Buyers benefit

- The potential for extended payment terms without burdening suppliers with high financing costs
- A reduced working capital requirement resulting from extended payment terms
- The buyer's relationships with their suppliers are enhanced

Suppliers benefit

- The opportunity to receive early payment of invoices
- A reduced working capital requirement resulting from reduced payables outstanding
- The ability to better predict payment flows
- An enhanced buyer relationship and any future growth with the buyer will require less capital

Lenders benefit

- Increased buyer financing with enhanced returns
- Automatic processing with efficient transparency and visibility of underlying payables
- The financier's relationship with their client is enhanced

CONCLUSION

In the new millennium, supply chain management has been a key focus of the manufacturing industry as it strives to introduce greater efficiencies into its processes and protect itself against margin pressure. In the last five years, globalised supply chains, which take advantage of sourcing from lower cost economies, have been the most universal initiative. Supply chain finance is a combination of technology solutions and services that links suppliers, buyers, financial institutions via service providers optimizing transparency, financing costs, availability, and delivery of cash on the occurrence of one or several supply chain events.

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Managing Supply Chain Demand Variability : The Bullwhip Effect

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