Trends in
Supply Chain Finance

SupplierPay Meeting • 17 November 2014

David Gustin
Managing Director, Global Business Intelligence
Co-founder, Trade Financing Matters

Discussions Topics

- **Clarify Confusion** around Supply Chain Finance Nomenclature
- **Overview** of Early Pay Techniques
- **Critical Issues**
  - P2P Complexity: Direct vs Indirect Supplier Expenses
  - SupplierPay - Do Corporates want to be a Bank to their Suppliers?
  - Where are the Banks?
  - New Models disaggregating Banks and Factors for business credit
- **Key Questions** to Address

The vast majority of trade credit sits on companies balance sheets in the form of payables and receivables.

- Trade finance is a large, global and interconnected industry, encompassing nearly $8tn in notional credit*.
- Most of trade credit (~$7.5tn) is not intermediated directly and remains on corporate balance sheets (in the form of trade receivables).
- Banks are the main third party source of financing for corporate trade, but intermediate roughly $500bn of trade credit (12%).

**Note: $2tn in USA, an estimated 3 trillion Euros of accounts receivables outstanding in the EU, estimated $8tn globally*

Nomenclature and Definitions Matter

- The term **Supply Chain Finance** is not universally accepted nor well defined.

- **Self-Funded Early Pay**
  - Supplier gets paid earlier than the due date on the invoice and money comes from the balance sheet of the buyer (egs. static discounting, dynamic discounting)

- **Funded by Third Party (Factor, Bank, Non Bank, Pcard)**
  - What the market calls Supply Chain Finance – ie Taulia's TED program or PrimeRevenue's multi-bank model, or Orbian's capital markets model — is when the supplier is paid early but the money comes from someone other than the buyer.

- In addition, important to point out there are **five main triggers** that we see for supply chain finance that can involve taking information to trigger liquidity.

Early Pay Techniques

	Technique	Description
Buyer Focused	**Supply Chain Finance**	Supply chain finance is an uncommitted credit facility typically with near investment grade corporations that rely on approved invoices to fund receivables.
	Dynamic Discounting	Discounts are offered on all invoices approved, opening up the entire procurement spend, based on a sliding scale.
	Reverse Auctions	Buyer sets APR rates and submits approved invoices for suppliers to bid.
	Pcards	Small suppliers and low dollar invoices typically funded by a bank (eg. U.S. Bank, Citibank)
Seller Focused	**Seller Auctions**	An alternative to factoring where companies sell single invoices that are not credit enhanced on an exchange.
	Factoring	Factoring consists of several distinct services: receivables monitoring and collection, credit assessment, payment guarantees and financing. It is seller-focused as opposed to SCF and dynamic discounting that are buyer focused.

How Supply Chain Finance differs from Dynamic Discounting

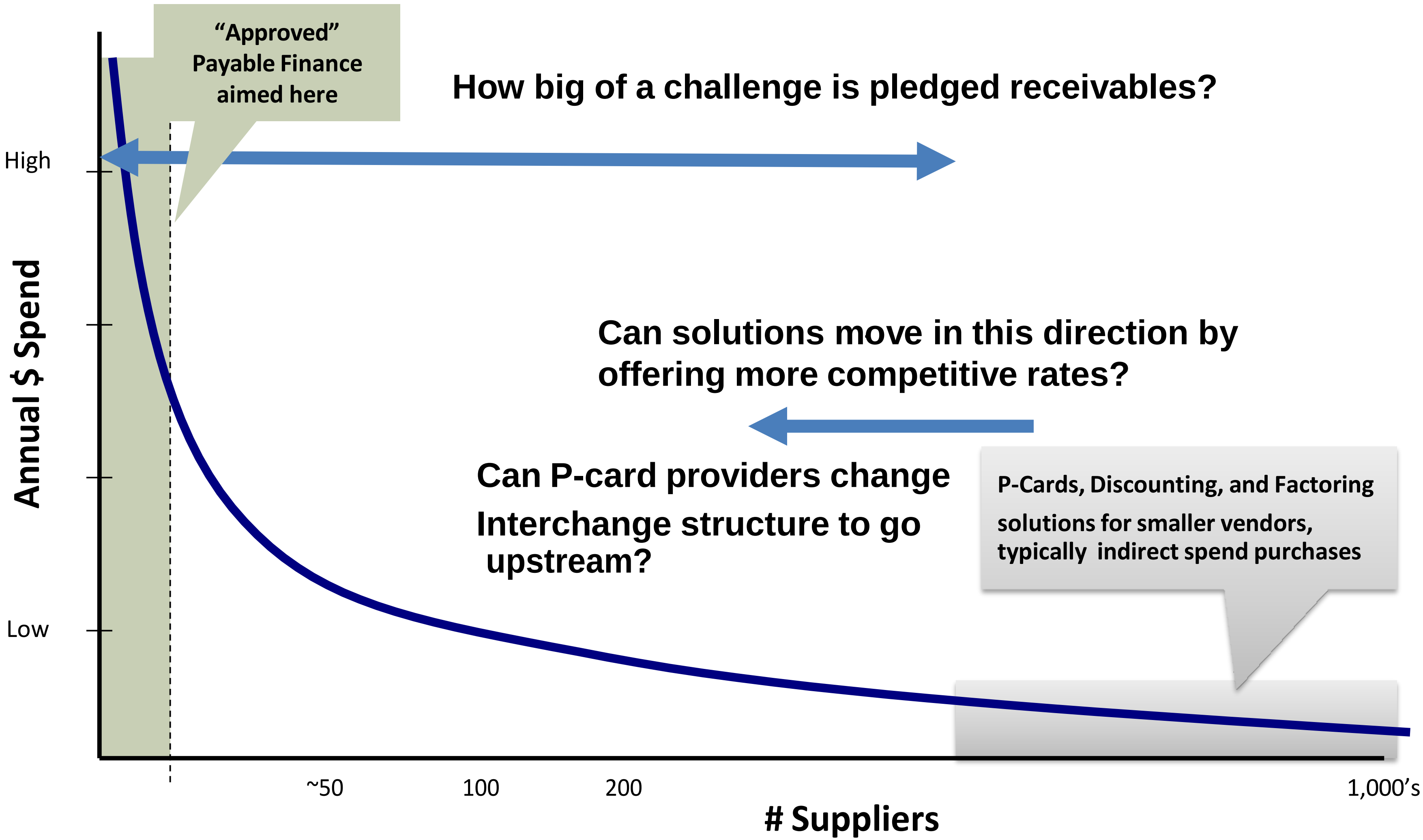
Supply Chain Finance

- Supply Chain Finance is a credit and cash management product, and focuses only on investment grade or near investment grade companies
- SCF programs typically have a ROI and that is tied to DPO extension.
- Funders typically "buy" receivables which makes it difficult to profitably implement bank funded SCF programs for SME buyers. (KYC, UCC filing costs, etc.)
- SCF program rates are based on Libor or Euribor plus a spread

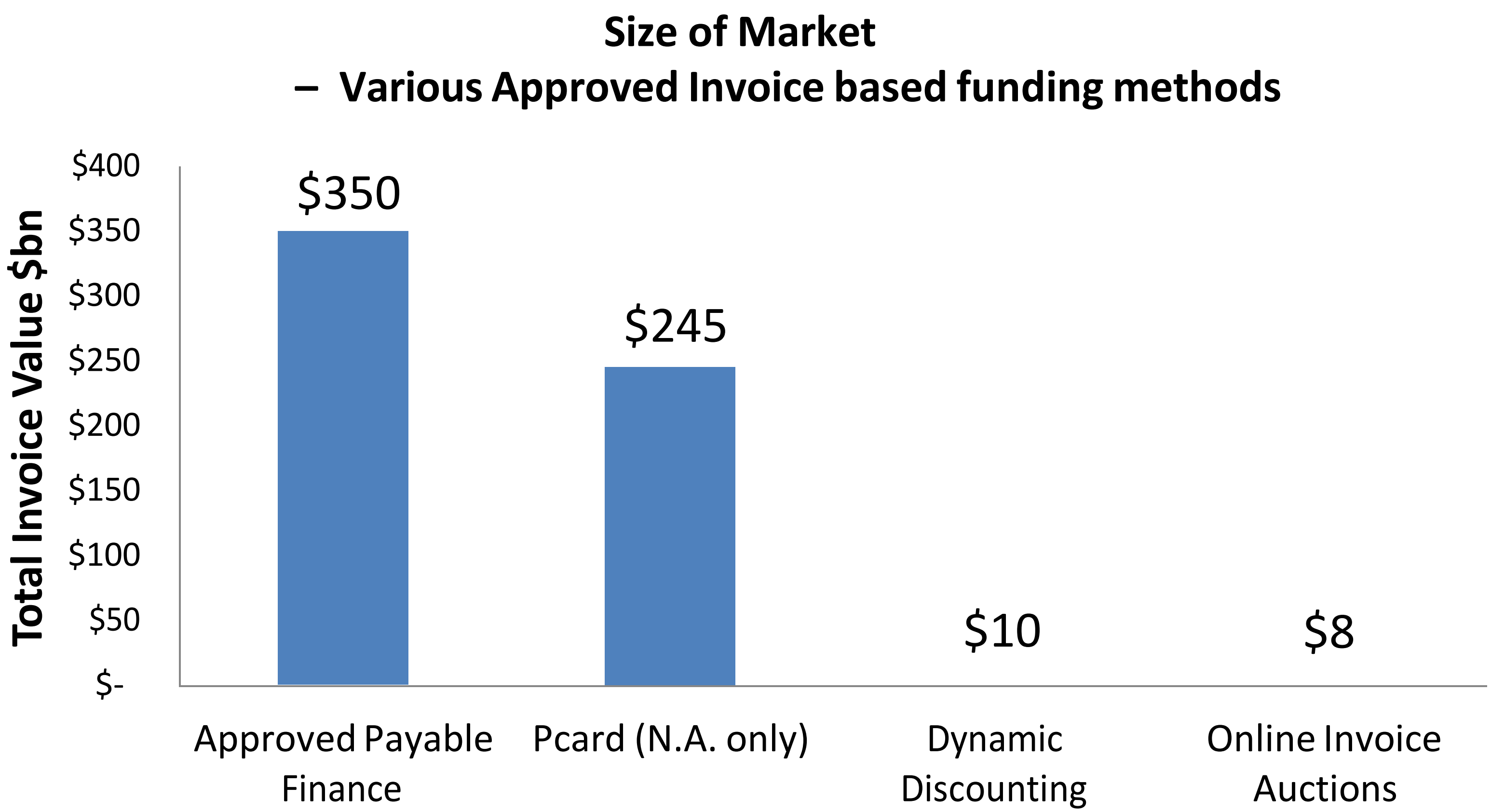
Dynamic Discounting

- Dynamic Discounting requires no bank line. Programs can be done by any corporate, investment grade, non rated, non investment grade, etc.
- Corporates tend to self-fund using their own surplus cash (although options are being developed to use third party non bank funds).
- Funding is based on based off Treasury hurdle rates and have APRs approaching 20%+
- Typically focused on the long tail of suppliers (smaller, more indirect spend)

Early Pay Finance Options Tend to Get Positioned Based on Relative Size of Suppliers



Relative Size – Select Early Pay Models



Source: GBI Analysis, RPMG 2012 Pcard study

Purchase-to-Pay Complexity

Percentage/share of spend in different categories

- Direct
- MRO/Catalog
- Specialized - Print, Telecom, Marketing, Logistics, IT, etc.)
- Services
  (simple + complex)
- Contingent Labor
- T&E
- Other indirect/catalog

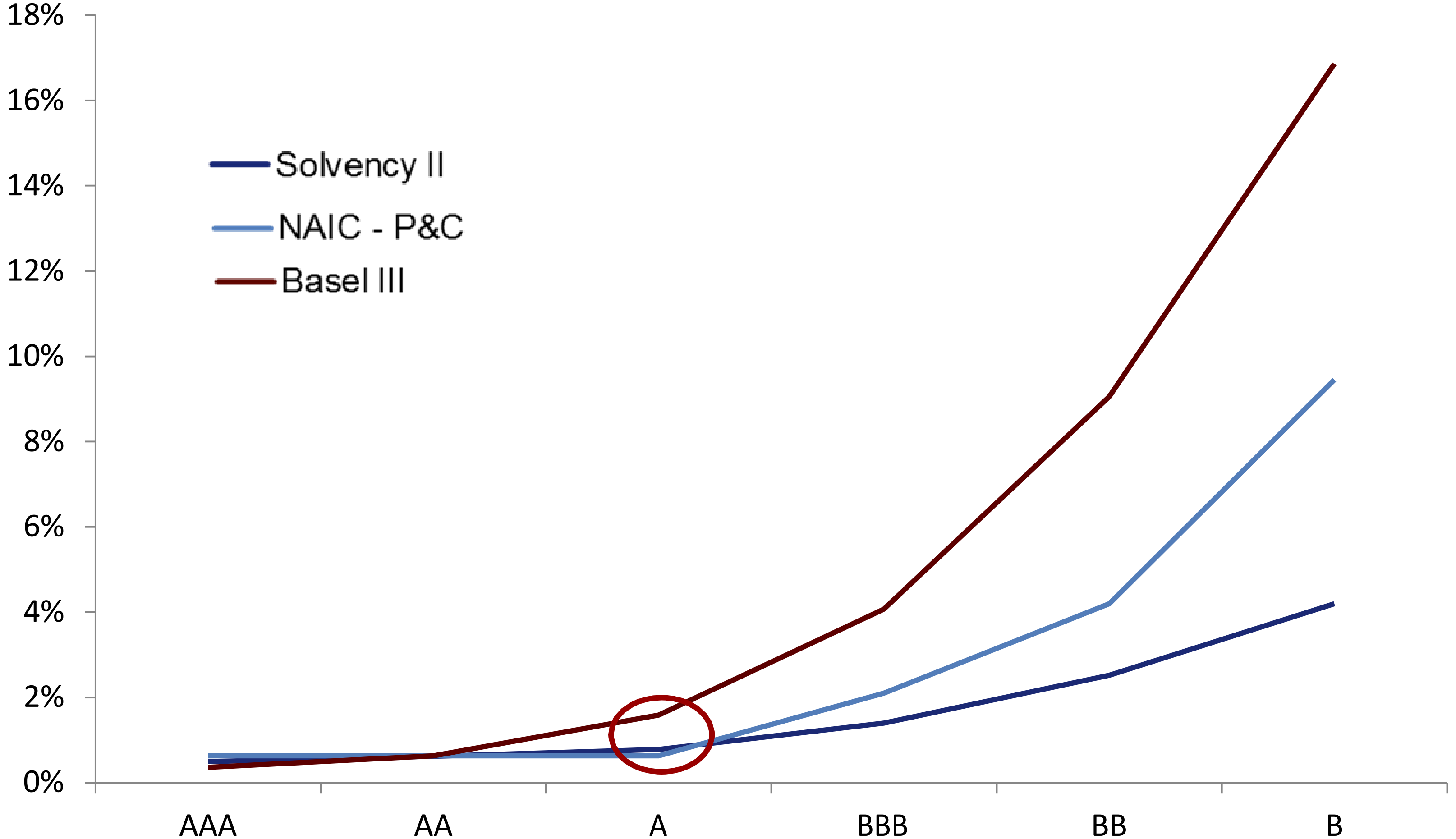
Do we want our Large Corporations to be Banks to their Suppliers?

- **Material effect on balance sheet**

- **What is the role of third parties to finance these early pay programs?**

- **Three drivers for Non Bank funding**
  - **Technology enabling (B2B, einvoicing, data warehouses, analytics, etc.)**
  - **Zero interest rate environment**
    = impact on Corporate Treasurers
    + Investors
  - **Vast regulation = unintended consequences + arbitrage opportunities**

Bank regulatory costs become less efficient than third party at less than investment grade, creating intermediation businesses.



Sample: Corporate Bonds
Source: Conning; Institution of International Finance

Diagram of Business Bank and Disintermediation

Business Banking	"Disrupters"
• Checking Account	
• Cash Management	
• Lending / Credit	
- Commercial Purchasing cards	MasterCard; basware
- Line of Credit (Letter of Credit)	
- Loans	
> Small Business Installment	Funding Circle – Better for business, better for investors, better all round
> Commercial Mortgage	
- Working Capital Loans	
> Asset Based Lending	FINACITY; GSCF Global Supply Chain Finance; DEMICA Intelligently Working Capital
> Factoring	TUNGSTEN Built on OB10; C2FO; taulia; GT NEXUS
> Invoice Discounting Line	TUNGSTEN Built on OB10; C2FO; taulia; GT NEXUS
> Distributor finance	AQ AmeriQuest Business Services; CorCentric work smarter
> Supply Chain Finance	PrimeRevenue OpenSCi; ORBIAN Trading on better terms

Factoring versus P2P Supplier Network Model

Factoring Model	P2P Model
• Relationship and Operation intensive • Seller-focused • Labor intensive • Factoring consists of several distinct services: receivables monitoring and collection, credit assessment, payment guarantees and financing. • Focused on small to mid market • Risk is highly concentrated in one sector – RETAIL (footwear, apparel, furniture, etc.) Essentially you have major Big Buy retail that are the obligors to these factoring companies.	• Approved invoice (Buyer focused) • Typically large global names as Obligor • Supplier onboarding facilitated by Buyer • Provides great efficiency play for Buyer (business rules, workflow, dispute resolution, etc.) and supplier (customer service, etc.) • APRs 20%+ • Cash acceleration 20+ days

Key Questions to Address

- **Spend Analytics** – how long is your tail and have you put existing programs in place for early pay?
- Do you have the **technology to manage Early Pay**? E-invoicing, eProcurement, ERP, etc. Most companies have ERP systems, but the goal is to get all invoices submitted electronically from suppliers in a no-touch/low-touch manner so that cash can be truly optimized.
- **Onboarding suppliers** is always a challenge, regardless of technique – can you commit resources?
- **Governance issues** – Finance vs. procurement misalignment and conflicting KPIs- increase DPO versus Healthy Supply chain- How will you navigate?
- Do you have the ability to **enforce** and **monitor the success** of programs?

Any Questions?

David Gustin
*President, **Global Business Intelligence***
*Co-Founder and Managing Director, **Trade Financing Matters***

dgustin@globalbanking.com
dgustin@tradefinancingmatters.com

www.globalbanking.com
www.spendmatters.com/tfmatters

phone: 001- 604-924-0851