Developing Your Supply Chain Finance Strategy

It is the CFO's job to maximise the bottom line. This can be done in several ways, finding cost savings on goods purchased or optimise working capital and use effective cash management strategies.

Trying to find savings in the supply chain with persistent attempts to squeeze suppliers and extend payment terms without offering them anything in return can lead to an uncertain supply base. Suppliers that experience cash flow problems cannot effectively support rush orders or a buyer's business growth. This eventually leads to suppliers embedding the cost of extended payment terms into the cost of goods sold, so the buyer's perception of savings from the extended terms proves to be an illusion.

Organisations are continuously seeking new ideas and solutions for effective cash management but can overlook the opportunity of Supply Chain Finance (SCF).

An increasing number of companies have already implemented SCF and those companies have been able to realise both hard and soft savings in finance, business process management, and transaction processing costs.

Sourcing from global producers means that today's supply chains can be long, in addition, the development of direct sourcing has made supply chains more complex and created a need for integrated solutions. Companies operating across international markets must overcome challenges to make sure products and services reach their end consumers cost efficiently and timely and the SCF represents an opportunity to gain competitive advantage as well as reduce costs and improve supplier relationships.

There is an increasing awareness over the past few years, with technology driving the appetite for introducing or extending SCF solutions. Digitization of business processes and the emergence of new fintech platforms for payments have brought opportunities for all sizes of enterprises, in the past smaller and mid-sized enterprises might have thought SCF was too costly or too complex for them. To fully maximise the working capital potential of a SCF programme it should be part of an integrated Procure to Pay (P2P) strategy and approach.

Working capital optimisation is (still) the most important reason for implementing an SCF programme.

Most Common Supply Chain Finance Practices

Buyers	%	Suppliers	%
Program to extend payment terms	49%	Extended payment terms for our buyer	46%
Early payment discount program offered by your company	40%	Early payment discount program offered by the buyer	29%
Buyer-financed raw materials for LCCS suppliers	17%	Factoring of confirmed receivables/ letters of credit (LCs)	25%
Buyer-financed work-in-progress for LCCS suppliers	13%	Credit insurance to mitigate Buyer's inability to pay	21%
3rd party financing of vendor-managed inventory	10%	Inventory/ production loan from a financial institution	17%

Source: AberdeenGroup,

There are several fundamental benefits achieved by companies active in SCF: lower cost of procured goods for buyers, improved DPOs/DSOs and more predictable cash flows for suppliers.

Principal reasons for implementing an SCF programme:

- Working Capital optimisation
- Supplier liquidity needs
- Supplier relationship improvement
- Supply chain stability improvement
- Other
  Additional revenues, cost reductions
  Utilise cash surplus
  Optimise corporate finance (incl. asset financing)

Key Success Drivers for SCF Programmes

When preparing an organization for SCF there are several strategies which can maximise the benefits of such a programme. The opportunity can also lead to implementing more advanced practices to make your whole supply chain more competitive.

- Institute a cross-functional team of finance, purchasing, and supply chain professionals to evaluate opportunities in SCF.
- Learn and understand the key financial pain points of your suppliers: the cost at which they obtain trade financing, their payment terms with their own suppliers, the percentage of orders they factor, and what impact your payment terms have on their working capital strategies.
- Evaluate the opportunity cost of your current financial practices with suppliers and estimate the savings opportunity from using a different SCF arrangement or a new SCF technology.

Don't Underestimate the Impact of Supply Chain Finance Technology

Different companies have achieved varying levels of automation of the procure-to-pay process improvement, which is influenced by such factors as company size, geographical organization, the industry of operation, as well as the business model. Early adopters of SCF technologies have successfully managed to reduce the costs of processing orders and invoices, improve staff productivity or reduce/redeploy freed staff members.

Recommendations for Action

1. **Set up a cross-functional SCF team, with a full-time employee focused on the process.** This factor is among the most important determinants of SCF success. A cross-departmental team will help your company make better decisions that will result in lower unit costs and improved corporate financial metrics.
2. **Work with your preferred suppliers to determine ways to improve the financial supply chain.** Evaluate the cost structure for both your company and your preferred suppliers, including the working capital ratios at your company. The shortage of readily available capital is a problem for emerging market suppliers, so consider providing programs and tools which will

improve their financial processes and give them better access and cheaper capital.

3. **Choose the right SCF technology - Automate the financial processes with your suppliers.** Additional benefits can be obtained by automating invoice dispute resolution, which improves the quality of data transmitted into the accounting system and enhances compliance. Onboard as many suppliers as possible to use the shared SCF technology platform.

Conclusion

By carefully planning with and supporting its suppliers, a company can take advantage of SCF beyond just the financial metrics. Not only does SCF add value to a business by lowering working capital, reduction of the cash cycle, sharing the benefits of interest arbitrage, and the reduction of risks, but the collaboration with all departments in the company working together to integrate their processes brings other long-term benefits.

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