Despite the opportunities presented by SCF programs, the proportion of companies that actually implement them in Asia Pacific and globally, has been relatively small until quite recently. How can treasurers leverage this untapped opportunity to help their companies achieve a sustainable competitive advantage and further optimize working capital efficiency? What are the key strategies of companies with the world's most successful SCF programs?

**Evolution of Supply Chain Financing Programs in Asia Pacific**

Previously seen as a financing strategy for small and medium-sized enterprises (SMEs) or as a stopgap technique for companies during troubled times, SCF has developed significantly post the global financial crisis in late 2008.

Today, an increasing number of large multinational companies (MNCs), especially those with strong credit ratings, are starting to leverage SCF programs to help unlock liquidity and increase the resilience of their financial supply chain. This is in part driven by liquidity constraints created by Basel III as companies are concerned that their smaller, lower-rated suppliers will find it difficult to raise capital in the future, which brings potential risk to their supply chain.

At the same time, MNCs are also seeking ways to fund working capital optimally to leverage high-growth emerging markets in Asia. This includes the challenge of accelerating their cash flow cycle to reduce the need for working capital, recognizing that an increase in their days payable outstanding (DPO) will have a negative impact on their suppliers’ days sales outstanding (DSO), further compounding supply chain risk. SCF programs provide an effective solution, enabling companies to extend and standardize their payment terms while positively impacting suppliers’ DSO.

There is also an increasing trend for highly-rated suppliers (some with a higher credit rating than their customer) to join SCF programs. While these sophisticated suppliers may be able to source financing at an equivalent or even better rate than their customers, the ability to discount receivables on a non-recourse basis via SCF programs significantly reduces their concentration risks, enabling them to further grow their customer base.

With the banking industry’s move towards more conservative credit models and more stringent banking regulations, the adoption of SCF programs is likely to increase further as companies continue to seek ways to optimize liquidity and fund investments.
New Strategies for Developing a Successful SCF Program

So how can companies implement an SCF program with the maximum chance of success? From Citi’s vantage point of working with leading companies to drive many of the world’s most successful SCF programs, we have identified three key strategies that these companies typically adopt. These can vary or be used in combination based on the companies’ working capital, efficiency and supply chain objectives.

Strategy 1: Benchmark working capital metrics
Companies can learn a lot by investigating the working capital metrics of their suppliers and customers. And with publicly available information, it’s easier for treasurers to gain a high-level view of their supply chain eco-system in order to quantify the tangible benefits of their SCF program. Bloomberg and Capital IQ are two of many data sources that provide subscribers with detailed financial information.

At Citi, we typically work with clients to analyze a number of key working capital metrics. Some questions to consider include:

- What are the days sales outstanding (DSO) of your suppliers
- What are your company’s terms compared to your suppliers’ average DSO
- Are your terms more or less favorable than your competitors
- What are the days payable outstanding (DPO) of your customers
- Are your terms shorter or longer than their payment terms with you
- Do your competitors also sell to these customers? If so, are you selling on the best terms

Answers to these questions are important for several reasons – most critically, if your company’s payment terms are shorter than your suppliers’ DPO, and/or your sales terms are longer than your customer’s DSO, you may be financing your competitors! This assumes your supply chain has an overlay with your competitors, which we have found to be the case across many industries.

An exercise in benchmarking working capital metrics can be highly effective to help treasurers assess business competitiveness, efficiency and the extent that their working capital goals can be realized. Figure 1 provides an example of a benchmarking exercise for 10 companies in the technology industry, using publicly available data from Bloomberg. We were able to put together a snapshot of the overall DPO for these companies, which helped a leading technology conglomerate to assess their position in the competitive landscape and provided guidance for the direction of their working capital goals.

#### Figure 1. Benchmark working capital metrics
The DPO for ABC Company is below average for the industry. There is an opportunity to extend the DPO and generate working capital benefits. ABC Company could be subsidizing its competitors which avail longer payment terms from the supplier funding a supply chain program, companies have a new avenue to enhance yields on trapped cash and benefit from their cash reserves.

In this structure, suppliers join the program at attractive rates, and when discounting is requested, the company funds the request, effectively benefiting from an early pay discount. Such solutions are, of course, bespoke, but they are increasingly in vogue because of their win-win nature.

Strategy 2: Create self-funded structures to enhance yields
Many companies operating in Asia have trapped cash that cannot be easily moved across borders due to regulatory, tax or business process constraints. Or they have huge cash reserves which can become a cost burden. Further, the returns on this cash can often be very low. By self-funding a supply chain program, companies have a new avenue to enhance yields on trapped cash and benefit from their cash reserves.

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Strategy 3: Leverage currency funding costs
Although multiple currencies in Asia coupled with increasing intra-region trade presents unique foreign exchange, regulatory and liquidity challenges for MNCs, the heterogeneity of the region can also offer opportunities. For example, cross-border financing can be more attractive than in-country borrowing. At the moment, US dollar financing in China can be more expensive than it is in Hong Kong or Singapore. To capture this opportunity, companies need to pair up with an experienced banking partner who understands the regulatory environment and can help structure a solution that is optimal to the parties involved and compliant to...
local regulatory guidelines. Knowledge of these markets and the opportunities that exist enable the delivery of more competitive financing rates. This can be leveraged to either improve terms or reduce costs for companies, and more cost-effective financing for their suppliers. Importantly, it also deepens the buyer-supplier relationship.

**Why are Some Programs More Successful than Others?**

The single most important factor to the success of SCF programs is engagement, especially across multiple corporate functions. While SCF initiatives are generally led by the treasury function or directed by the CFO to improve working capital, other corporate divisions will be involved as an SCF program gets implemented.

Procurement, accounts payable and information systems, each with their own priorities, directives and resources constraints also need to get on board. Strong collaboration between these distinct functions is required for a program to be successful.

To achieve organizational buy-in for your SCF program, a best practices approach is to show both company-wide and division specific benefits to all involved. Specific examples include better terms and reduced Cost of Goods Sold (COGS) for procurement, reduction in supplier account maintenance for accounts payable, and streamlined system-to-system integration for information systems.

From Citi’s experience, the best SCF programs are often viewed as an ongoing, evolving journey within a company and not as an isolated product or solution. A team comprised of individuals with the right leadership and project management skills needs to be assembled to advocate the benefits of an SCF program internally, and facilitate cross-functional collaboration so that each department looks beyond its individual responsibilities and is accountable for the program’s wider objectives.

**The single most important factor to the success of SCF programs is engagement, especially across multiple corporate functions.**

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**Figure 2. Self-funded supplier financing**

- Company and supplier sign procurement contract with commercial discount under earlier payment terms
- Company sends earlier payment discount information to Citi for platform setup
- Company approves supplier’s invoice and electronically instructs Citi to pay supplier on a future date
- Supplier notified by Citi of a payment from the Company, scheduled for a future due date (e.g. day 60)
- Supplier may choose earlier payment to liquidate their account receivables and cash out at favorable cost of commercial discount
- Citi remits funds to supplier, typically same day instructions for next day settlement
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CTA4164 May 2013