Supply Chain Finance

Supply chain finance (SCF) solutions represent a combination of technology solutions and financial services that closely connect GVC anchors, suppliers, financial institutions and, frequently, technology service providers. They are designed to improve the effectiveness of financial supply chains by preventing detrimental cost shifting and by improving the visibility, availability, delivery and cost of cash for all GVC participants. They are focused on facilitating trade conducted on an open account basis, which now makes up 80 per cent of world trade.[17] A wide range of industries are well-suited for (and have started to adopt) SCF solutions, including: retailing, automotive, manufacturing, electronics, food and drink, pharmaceuticals, distribution, heavy equipment and technology.[18]

There is, at times, confusion with respect to the difference between trade finance and SCF. Trade finance corresponds to the provision of financing to suppliers to help them produce goods and to foreign buyers to help them purchase these goods. Trade-related supplier financing is often made through loans (e.g. bank line of credit backed by insured foreign accounts receivable) or via the sale of accounts receivable to a factoring company. Buyer financing is usually provided through direct loans made by a financial institution or export credit agency or by the supplier when selling on open account terms. Trade finance also includes the payment instruments commonly used in international trade transactions (e.g. letters of credit and documentary collections) to safeguard the interests of buyers (who want to ensure receipt of the right goods) and suppliers (who want to ensure they are paid). Finally, trade finance includes risk mitigation instruments such as trade credit insurance (that protects suppliers against the risk of non-payment by foreign buyers) and contract bonding (that protects foreign buyers against the risk that the supplier fails to perform its obligations under a commercial contract). As we will see, SCF constitutes an alternative means for suppliers and buyers to gain access to cash. Accordingly, SCF can be considered a sub-set of trade finance.

Supplier payment programs

The most frequently used SCF solution consists of supplier payment programs driven by GVC anchors. The concept behind supplier payment programs is relatively straightforward: the GVC anchor provides access to its lower cost of capital to its key suppliers, enabling them to get paid more quickly and to decrease their financing costs.

Using a shared technology platform, suppliers can request funding from a participating financial institution as soon as a pre-defined event takes place or at any other point in time prior to the scheduled settlement date (Figure 3). Under *pre-shipment* arrangements, suppliers can gain access to cash as soon as a purchase order is received from the GVC anchor. With *post-shipment* structures, the approval of the invoice by the

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became more global, web-based technologies improved and paper documents started being replaced by electronic documents, the development and distribution of SCF solutions accelerated.

[17] International Chamber of Commerce Banking Commission, "Rethinking Trade Finance 2009: An ICC Global Survey", March 2009, p. 9. Open account trade refers to a payment arrangement whereby suppliers ship goods to buyers and give them an agreed-upon period of time to pay (e.g. 30 days). Other payment methods used in international trade include cash in advance, letters of credit and documentary collections.

[18] Source: Demica, "Demand and Supply, Supply Chain Finance - A Second Report from Demica", May 2008, p. 4.