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Supply Chain Finance

Should we be excited or worried?

According to the World Supply Chain Finance Report, it was estimated that the volume of trade finance used in 2020 was $505 billion, up from €117 billion in 2015. While Europe and North America are still the largest markets for such finance, the Asian use of such funds has grown by 70% in the same period. Some estimate that the potential for trade finance is to grow to more than 10 times that market size. Anyone who has been associated with reverse factoring will tell you that 2020 saw an explosion of interest from large corporates but also a strong trend in new deals being done. These trends are continuing in 2021. So if you are a supply chain fintech or a merchant banker, these are exciting times. But there are things we should be careful about in this area. The collapse of Greensill is a lesson to use all that bad players can be very good at exposing the structure of an industry that relies on institutions following the spirit of the rules and not just the words. Trade finance is remarkably low risk versus other types of finance, but it is not risk free. The only good news is that the industry structure did work and caught up with Greensill without causing lasting damage. Another issue is disclosure by large corporates. How many companies are using supply chain finance to window dress their balance sheets? The worrying answer is that while we can guess who is involved, we have no idea how specific balance sheets are impacted. The final issue is that most of this growth in trade finance has been taken up by investment grade corporates and is largely unavailable to smaller companies. Some fintech players are trying to change this but it is a considerable challenge to get the technology right while aligning with the increasing demands of banking regulation. The one bright light on the horizon is that several players are attempting to develop inventory financing products. While inventory financing has been available for many years for traded commodities, it has not been available for other types of inventory. If these players get this right, it will prove to be a games changer in working capital management. The one thing that is for sure is change is on the way and that change will surface new opportunities and risks.

In This Issue

Insolvencies

Will 2021 be a record year?

A study by the credit insurer Atradius back in March estimated that the level of global insolvencies in 2020 declined by 14%. A lot of this had to do with the various government supports offered to businesses to stem the economic impact of the pandemic. Richer countries offered businesses cheap loans, wage supports, debt and tax deferments. In Australia, Singapore, France and Austria insolvencies plunged by more than 40% from the previous year. So it could be argued that many businesses that would have gone to the wall in a normal year still exists due to Covid-19 supports. In the same study, they also forecast that business insolvency will surge by 26% in 2021 as all these supports end. For Australia, Singapore, France and Austria insolvencies are expected to grow by more than 70%. If all this turns out to be true, then the financial rollercoaster that we have been on since early 2020 might be far from over and many businesses that thought themselves immune to the pandemic may be impacted by a second wave of financial disruption. This presents the possibility that many customers and suppliers will be gone by the end of this year and the consensus would suggest that smaller businesses will be more affected than larger businesses. This is because larger businesses have much better access to capital markets and have used their leverage to ensure that they have plenty of liquidity available in the event of another crisis. But this won't mean that larger firms are immune to disruption. Expect bad debt write-offs to increase and supply chain holes to appear as key suppliers drop out of existence. The good news is that much of this can be mitigated by good risk management. All this doom and gloom may not come to pass, but it is better to be prepared.

Payment Terms

Spend Category Comparison

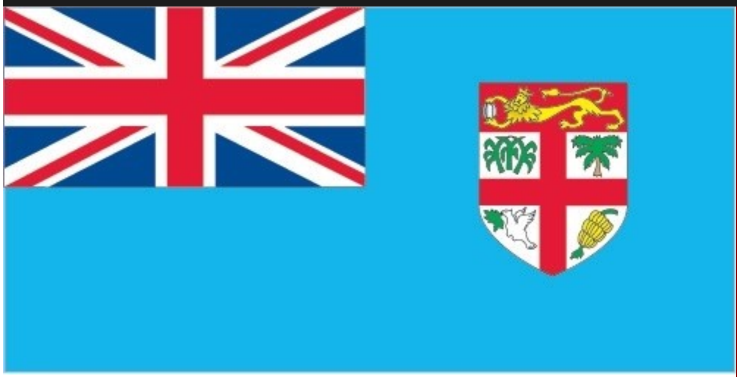
When we started TermsCheck, we thought that our clients would be most interested in comparing supplier level terms from our database. In the majority of cases, this has proved to be true. But many also wanted various industry comparisons. For example, one client in the chemical industry wanted to see how prevalent the use of settlement discount or skonto was in the DACH market (Germany, Austria and Switzerland). Another US client wanted to see the spread of payment terms available for automotive spares. So we have developed these industry analysis from the data that we have. A Brazilian client wanted payment term information for professional services. A French client wanted payment terms for transport companies in Germany, Italy, Poland, UK and South Africa. Yet another wanted to get payment term information for all 65 of their level 1 spend categories in the US. Luckily, this is made much easier since most of the data we collect also includes spend category information. So while we still fulfil many supplier and customer level data queries, the output from the database has evolved to satisfy these enquiries. It also shows that many in sales, procurement and finance continue to be frustrated by the inaccuracy and general nature of payment term benchmark. They are seeking simple and accurate information on the actual payment terms offered and accepted across the world. We are privileged that we can meet this demand as more people become aware of TermsCheck's capability. If you want more information, email us and we can explain further.

TERMSCHECK.COM

Factoring

Why does it remain popular for SMEs?

It is said that the first factoring transactions were conducted in Ancient Mesopotamia and it has remained a core banking activity to the modern day. Anyone who is involved with modern invoice factoring will tell you that it can be a tricky business to get right. It may seem simple to say that a bank or investor will fund a company's customer invoices for a fee, but there can be quite a detailed process to go through to make sure that the invoice is real, the funding is going to a legitimate source and managing the risk of the customer not paying the invoice. But it still remains a popular instrument with smaller businesses as a means of funding working capital when there is little or no access to the same type of funding available to large corporates. But it remains an awkward and expensive form of finance.



Fiji: Peace means Progress

Fiji has one of the most developed economies in the Pacific through its abundant forest, mineral, and fish resources. The main sources of foreign exchange are tourism, remittances from Fijians working abroad, bottled water exports, and sugar cane. Although natural resources are abundant including timber, fish, gold, copper, offshore oil, and hydropower, there is still a large subsistence sector. The tourist sector is dominated by visitors from Australia and New Zealand followed by Americans, Chinese, British Canadians, Japanese and Koreans. This is no wonder given all the wonderous beaches and opportunities for scuba diving in the coral reefs. The only real blot on the Fijian landscape has been politics. Ethnic tensions have been rife for many decades between the majority Melanesians who make up 54.3% of the population and Indo-Fijians who make up 38.1%. These tensions have resulted in political instability that has boiled over in to several coup d'état. The last coup was in 2006. Things have stabilised considerably since but the tensions persist. Growth these days depends very much on tourism where visitor number have doubled in the past two decades. But long term problems are low levels of investment and uncertainty over property rights. While covid has hit the economy in 2020/21, expect continued stability to be the bedrock of growth.

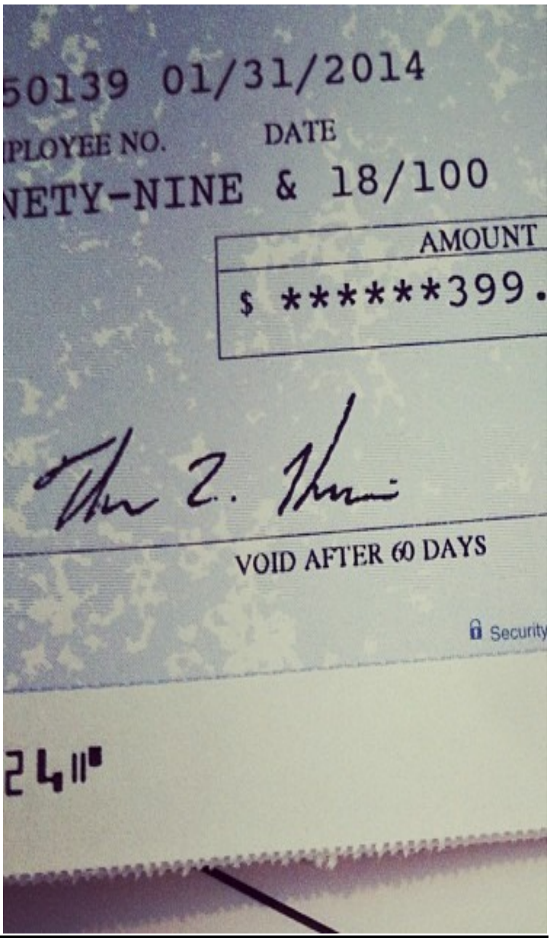
US-China Tariffs: Here to stay?

Given that the US and China are the world economic superpowers, it is not surprising that there are some frayed edges in the ongoing competition to be the most powerful countries on Earth. But the years since China opened up its economy have been a prosperous period for all where China has advanced by leaps and bounds and the rest of the world has found a huge source of well educated cheap labour that has benefited millions, if not billions. But in the last four years, things have become more tense. The Trump administration's approach seems to have been confrontational on the trade front. Almost every opportunity was taken to slap tariffs on Chinese imports in the name of "America First". So some expected that when the Biden team arrived everyone would calm down, have a quiet conversation and everything would go back to the way it was before. But that hasn't happened. At a recent summit in Alaska, the US and Chinese foreign ministers traded barbs in the most public fashion. History does tell us that tariff barriers can go up very fast but take decades to come down. So we should expect the current trade barriers to last.

Cheques

When will we finally say goodbye?

While the use of cheques across the world continues to decline there are still some stubborn outliers. One is the German supermarkets that cling to the cheque as a means of delaying payment to their suppliers. The big one are companies in the United States. While ACH payments continue to grow in America, the use of cheques continues to hold ground. Many American finance managers are convinced that extending float time by the use of checks is good for their business. Unfortunately, that is a complete myth. The theory assumes that if it takes time through postage and bank clearance to cash a cheque for the supplier, then the company issuing the cheque will have the cash in their bank for a longer period of time. In fact, this is not true. Treasury departments routinely hold large cash buffers on any given day since they do not know when the cheque will be presented or how long it will take to clear through the banking system. These payment accounts usually do not accrue any interest and will prevent treasurers doing something else with the cash that might have earned money in the short term. But US banks are complicit in this myth since many of them earn very good revenues by providing lockbox banking services and therefore have little incentive to get rid of cheques. Cheques and lockbox services are highly susceptible to fraud and are much more expensive than electronic alternatives such as ACH. So if you are still using cheques, save some money and reduce the risk by paying electronically.



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Informita

Website: www.informita.com

Twitter/Facebook: @informita

Email: brian.shanahan@informita.com
Phone: +351-911556662