New Strategies for Financial Supply Chain Optimization

Rethinking Financial Practices with Your Suppliers to Maximize Bottom Line Performance

November 2006
Executive Summary

In today’s globalized world, the competition is no longer among the individual companies but among their whole supply chains. The opportunity at hand is to make your whole supply chain more competitive with the introduction of more advanced supply chain finance (SCF) practices.

Driven by the pressing need to lower the cost of goods sold, companies have embarked on sourcing from emerging markets and have been able to achieve significant benefits when the strategy was executed correctly, including 10%-35% savings on the cost of goods purchased. However, most companies are still leaving money on the table because they fail to take into account the SCF opportunity when undertaking low-cost country sourcing (LCCS). Applying SCF innovations can bring the next wave of cost savings into the corporate LCCS program, helping a buying organization optimize its working capital, reduce product unit costs by taking advantage of arbitrage opportunities due to the higher cost of capital in emerging markets, as well as reduce supply base risk by enabling faster and more predictable payments to emerging market suppliers.

Key Business Value Findings

Companies that have focused on evaluating and revising their funding and payment strategies as part of their emerging market sourcing programs (or as part of their selling strategy if they are an emerging market supplier) are achieving numerous benefits. Best in Class companies have notably better performance across key metrics, such as a 10-day advantage in their cash conversion cycle compared to Laggards and longer Days Payable Outstanding. The Best in Class outperform their peers with the help of more diversified SCF techniques and are much more likely to have a cross-functional team of purchasing, supply chain, and finance professionals managing their SCF programs.

Innovations Releasing Trapped Value in the Financial Supply Chain

The most frequently used SCF practices in LCCS are traditional methods of extending payment terms and early payment discount programs. Less than a third of study participants use one or more innovative methods of optimizing funding and payment schedules. Based on the survey data for those sourcing from emerging markets, there is significant value trapped in the current SCF process. For instance, Best in Class buyers report achieving, on average, 15-day extensions of Days Payable Outstanding. Releasing this value can bring savings for both buyers and suppliers, including extending payment terms and lowering the cost of procured goods for buyers, enabling access to cheaper trade financing, improving cash flow visibility and predictability for suppliers, and creating an overall less costly supply chain for both partners. For many companies this is a multi-million dollar opportunity.
Table of Contents

Executive Summary ........................................................................................................ i
Key Business Value Findings ....................................................................................... i
Innovations Releasing Trapped Value in the Financial Supply Chain ................... i

Chapter One: Issue at Hand ....................................................................................... 1
Supply Chain Finance in Emerging Market Sourcing ............................................. 1
LCCS Alone Is No Longer Enough ........................................................................ 1
Supply Chain Finance Challenges ......................................................................... 2
Will Your Company Miss the SCF Opportunity? ................................................. 3
The Expanding SCF Landscape ............................................................................. 4

Chapter Two: Key Business Value Findings ......................................................... 6
Benefits of Revising SCF Practices ........................................................................ 6
Best in Class Performers ....................................................................................... 6
Organizational Strategies for Supply Chain Finance ........................................... 7
Finance’s Involvement ....................................................................................... 8
Understanding Your Suppliers is Key for a Successful Relationship ............. 9

Chapter Three: Implications & Analysis ............................................................... 11
New Savings Opportunities with SCF ................................................................. 11
Improved Payment Automation and Visibility to Extend DPOs .................... 11
Reducing the Cost of Goods Sold: Early Payment Discount Programs ........ 14
Access to Alternative Receivables Financing for Suppliers ......................... 14
Third-Party Inventory Financing ........................................................................ 14
Most Common Supply Chain Finance Practices ............................................ 14
The Impact of Supply Chain Finance Technology ............................................ 15
Defining Your Supply Chain Finance Maturity Level ...................................... 17

Chapter Four: Recommendations for Action ..................................................... 19
1. Adopt a Cross-Functional Organizational Approach ................................ 19
2. Improve Supply Chain Finance Practices ................................................... 20
3. Choose the Right SCF Technology ............................................................. 20

Author Profile ....................................................................................................... 22
Featured Underwriters .......................................................................................... 23
Sponsor Directory ................................................................................................ 25

Appendix A: Research Methodology ................................................................. 26
Table of Contents

Appendix B: Related Aberdeen Research & Tools ............................................. 27
Figures

Figure 1. Top SCF Challenges for Buyers and Suppliers ........................................ 3
Figure 2. Buyers that Have Cross-Functional Teams to Manage SCF for LCCS .................................................................................. 8
Figure 3. Finance Organization’s Involvement with LCCS Programs ...................... 8
Figure 4. What Attributes of Your Emerging Market Supplier Do You Know? ................................................................................. 9
Figure 5. Current Automation of the Procure-to-Pay Process .............................. 15
Figure 6. Planned Technology Adoption over the Next 18 Months ...................... 16
Figure 7. Planned SCF Technology Spend Over the Next 18 Months ................. 16

Tables

Table 1. Average Cash Conversion Cycle for LCCS Buyers ............................ 6
Table 2. Average Days Payable Outstanding (DPOs) with Suppliers in Asia .......... 7
Table 3. The Magnitude of SCF Opportunities for Buyers Sourcing from Asia ....... 12
Table 4. Most Common Supply Chain Finance Practices .............................. 14
Table 5: Competitive Framework in Supply Chain Finance ............................ 17
Chapter One: Issue at Hand

Key Takeaways

- Enterprises seeking the next wave of sourcing cost improvements need to focus on improving supply chain finance practices; these practices create a lower cost and more reliable supply base.
- The lack of best practice knowledge around supply chain finance and poor visibility into physical supply chain events are the top barriers to leveraging supply chain finance opportunities.
- Supply Chain Finance solution providers can play a unique role in optimizing financial supply chains by improving transaction management and injecting the much-needed liquidity into the supply chains of cash-strapped companies.

Supply Chain Finance in Emerging Market Sourcing

As new markets emerge and supply chains become more globalized, sourcing materials from countries with lower labor and raw material costs is becoming increasingly widespread. Today, it is no longer a question of whether a business should consider Low-Cost Country Sourcing (LCCS) but rather a matter of knowing how to successfully launch, execute, or alter LCCS strategies to maximize a company’s benefits and minimize risks.

Aberdeen Group undertook a study of 143 companies to assess their challenges and opportunities in supply chain finance (SCF) when sourcing globally. Companies participating in this study included buyers in the United States and Europe and suppliers located in low-cost countries.

The low-cost countries (also referred to as emerging markets) from which the study participants source span Eastern/Southern/Southeastern Asia, Africa, Middle East, and Eastern Europe. In these countries, labor and raw material costs are generally lower than in the buyer’s country, but the cost of capital and access to capital is much more constrained. This creates multi-million dollar opportunities for applying SCF innovations to release value trapped by these financial imbalances. (See savings calculations in Table 3 in Chapter 3.)

LCCS Alone Is No Longer Enough

Driven by the pressing need to lower the cost of goods sold, companies have embarked on LCCS strategies and have been able to achieve significant benefits when the policy was executed correctly. According to prior Aberdeen research, successful enterprises have been able to save from 10% to 35% of total costs on goods purchased from emerging markets. However, most companies are

“Payment terms, visibility into supply chain, quality, and lead times that drive high on-hand inventory levels in the U.S. are the top issues with our key emerging market suppliers”

— A mid-size North American consumer goods company
still leaving significant money on the table because they fail to take into account the supply chain finance opportunity when sourcing from low-cost countries.

Applying supply chain finance innovations can bring the next wave of cost savings into corporate LCCS programs. These savings are predicated on increased efficiencies from merging the physical supply chain information with the financial supply chain. Physical supply chain data includes the status of good’s movement, the up-to-date information on goods location, and insight into potential delays. Financial supply chain data provides visibility of the status of purchase orders/invoice approvals/payment status/potential discrepancies, information on the size and deadlines for trade discounts, and the movement of funds/credit in the supply chain. Supply chain finance helps a buyer:

- Optimize its working capital
- Reduce product unit costs by taking advantage of arbitrage opportunities due to the higher cost of capital in emerging markets (e.g., offering suppliers access to capital at a lower rate in return for a lower cost of goods sold).
- Extend days payables outstanding (DPOs)
- Reduce supply base risk by enabling faster and more predictable payments to emerging market suppliers.

Understanding the cost of capital and access to capital of LCCS suppliers can help an organization construct payment and funding options to further reduce unit costs while setting itself up to be viewed as a preferred buyer. For many companies, however, SCF is not an integrated part of their LCCS strategy, resulting in higher end-to-end costs, increased working capital tied up in inventory, a riskier supply base, and higher administrative costs. On the supplier’s side, the cash flow challenges, lack of order-to-pay process automation and difficulty in accessing capital are significant hurdles to business continuity and development.

For instance, low-cost country suppliers report factoring orders to gain quicker access to the cash needed to fund raw material and work-in-process inventory. Many receive only 80-85 cents on the dollar value of their purchase order. This lost value will come back embedded in the unit costs for buyers. Emerging SCF innovations can help leverage the better financial access of many North American and EU buyers to reduce the suppliers’ cost of accessing money early.

**Supply Chain Finance Challenges**

Both buyers and suppliers report two shared top challenges — the lack of knowledge of SCF best practices and poor visibility into the movement of goods. Buyers also admit that it is hard for them to understand the true cost of capital in their financing and payment arrangements with LCCS suppliers. Suppliers rank the lack of automation of their order-to-invoice-to-payment activities among their top 3 challenges. This reflects the gap in automation between the predominantly U.S. and European Union buyers and their emerging market suppliers, which makes the supplier’s job even more difficult.
Figure 1. Top SCF Challenges for Buyers and Suppliers

- Suppliers: Lack of sufficient automation in the order-to-invoice-to-payment process
- Buyers: Difficult to estimate the true cost of capital in our relationship with LCCS suppliers
- Buyers and Suppliers: Poor visibility into physical supply chain events (movement, location of goods)
- Buyers and Suppliers: Lack of knowledge of supply chain finance best practices to lower end-to-end supply chain costs

Source: Aberdeen Group, November 2006

- “Internal resistance to change and the lack of strategic perspective pose a tough challenge for our relationship with emerging market suppliers,” says a logistics manager at a large European company.
- “Coordination between the payment process and the quality of goods is our top challenge,” says a mid-size North American pharmaceutical manufacturer.
- “Our emerging market suppliers are challenged in creating additional capital to finance expansions,” says the vice president of procurement at a large North American chemical manufacturer.

Will Your Company Miss the SCF Opportunity?

Aberdeen’s September 2006 Supply Chain Finance Benchmark Report introduced the problem of the disconnect between the strategies of buyers and suppliers in how they develop SCF practices. For example, persistent attempts to squeeze suppliers and extend payment terms without offering them anything in return can lead to a riskier supply base, with suppliers experiencing cash flow problems and thus not able to 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.

Few companies have taken advantage of the innovative practices in SCF – the September SCF report revealed that only 13% of companies are currently using SCF techniques to lower the cost of capital and cost of goods sold in their supply chain. These early adopters are proving that a company can revise its financing and payment terms without bringing noticeable disruptions to its own organization, while at the same time releasing the trapped value in the order-to-pay cycle and realizing increased savings on goods procured from emerging markets.
The Expanding SCF Landscape

Eighty percent of buyers in the study named Asia¹ as their top LCCS region (including East Asia, Southeast Asia, or Southern Asia). However, the landscape of LCCS is dynamic and these companies are already looking for the next emerging market.

New countries are becoming more attractive for strategic sourcing and some of the older lower-cost markets are experiencing rising costs. The top 3 new countries from which study participants plan to begin sourcing in the next 2 years are: India — 50%; China — 31%; Vietnam — 28%. India is catching up with China as a source of goods and materials, in addition to the many business and professional services already sourced from there. Vietnam has strongly come up as the #3 country of interest.

The dynamic nature of the LCCS landscape underscores the necessity of understanding the underlying SCF principles that should be factored into an LCCS strategy. Will your company compete just by searching for new places from which to source? Or will it build a strategic competitive advantage by being the most efficient partner for LCCS suppliers?

To build a cost- and risk-advantaged supply chain and keep it profitable in the long run, a company must consider the key challenges and opportunities in SCF for LCCS and choose the most appropriate SCF practice along with carefully selecting the enabling technology platform that will provide the critical level of visibility into the physical and financial supply chains.

---

¹This includes East Asia (China, Hong Kong, Taiwan, etc) – 58%, Southeastern Asia (Indonesia, Malaysia, Philippines, Singapore, Thailand, Vietnam, etc.) – 8%, and Southern Asia (Bangladesh, India, Pakistan, etc) – 14%).
### The Role of a Supply Chain Finance Solution Provider

An SCF solution provider plays an intermediary role between buyers and suppliers in a supply chain, streamlining transaction processing, improving visibility into financial supply chain actions, and providing a path to external sources of funding.

**Key functions in an SCF solution include:**

- Provides visibility into financial supply chain events — e.g., P.O./invoice/payment status, discounts available.
- Enables access to capital — e.g., early payment discount using a buyer’s own funds, factoring or reverse factoring by a financial institution, inventory financing from a third party, etc. Third-party SCF providers often offer funding to a buyer's suppliers at a lower rate than suppliers can obtain on their own.
- Enables electronic transaction settlement — including invoice reconciliation, payment, acquiring funds (accessing credit), selling receivables/payables, etc.

**Additional functions may include:**

- Provides visibility into the physical supply chain events (e.g. goods movement/current location)
- Supports letters of credit or open account automation
- Provides SCF consulting services
- Supplier on-boarding/ supplier network management
- Insurance services
- Other services (e.g., background check of supplier viability)
Chapter Two:
Key Business Value Findings

Key Takeaways

- Key benefits achieved by companies active in SCF: lower cost of procured goods for buyers, improved DPOs/DSOs, more predictable cash flows for suppliers.
- Best in Class companies have notably better performance across key metrics, such as a 10-day advantage in cash conversion cycle and improved DPOs.
- Fully 59% of Best-in-Class buyers have cross-functional teams in place to evaluate and manage SCF opportunities for LCCS, versus 26% of their peers.

Benefits of Revising SCF Practices

Companies are achieving numerous benefits from evaluating and revising their funding and payment strategies as part of their emerging market sourcing programs (or as part of their selling strategy if they are an emerging market supplier). Buyers have been able to lower the cost of procured goods, extend DPOs, improve supplier relationships and reduce supplier risk. On the flip side, suppliers have achieved more predictable cash flows and lower DSOs, as well as have been able to lower production costs and better support their customers’ business growth.

Best in Class Performers

Best in Class buyers in this study are defined as those companies that have achieved improvements over the past 18 months in both of the following categories:

- Days payables outstanding with low-cost country suppliers
- Total landed cost on items sourced from low-cost countries

Companies whose performance in either of the above categories has deteriorated are classified as Laggards, and those whose performance has not changed or improved only in one of the categories are classified as Industry Average.

The Best in Class not only show better performance on the payables side but also have been able to reduce the total landed cost of goods procured from lower-cost countries – they achieve this by better negotiating with the LCCS partners and employing more diverse SCF methods instead of asking for extended terms without offering their suppliers anything in return. In addition, they have better cash conversion cycles (Table 1).

Table 1. Average Cash Conversion Cycle for LCCS Buyers

<table>
<thead>
<tr>
<th></th>
<th>Best in Class</th>
<th>Average</th>
<th>Laggard</th>
</tr>
</thead>
<tbody>
<tr>
<td>29 days</td>
<td>31 days</td>
<td>39 days</td>
<td></td>
</tr>
</tbody>
</table>

Source: Aberdeen Group, November 2006
Fully 80% of buyers named Asia as their top LCCS region (including East Asia, Southeast Asia, or Southern Asia). The average payment terms statistic for this region is presented in Table 2.

### Table 2. Average Days Payable Outstanding (DPOs) with Suppliers in Asia

<table>
<thead>
<tr>
<th></th>
<th>Best in Class</th>
<th>All Others</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>54 days</strong></td>
<td><strong>39 days</strong></td>
<td></td>
</tr>
</tbody>
</table>

Source: Aberdeen Group, November 2006

**Case Study: AB Electrolux’s Best in Class Strategy**

AB Electrolux is a large consumer durables manufacturer headquartered in Europe. The company sources from emerging markets such as China, Eastern Europe, and Mexico.

“Many buyers do not reflect on the cost of financing for their suppliers, which is a natural component of the cost of goods sold in any supply chain,” says Christer Soderstrom, manager of supplier and customer finance for AB Electrolux. “What we have been doing to strengthen our supplier relationships ─ while simultaneously reducing the cost of procured goods ─ is break down the total supplier costs, including the cost of financing, and agree on certain increase of credit days or price reductions in return for providing financing through a bank we cooperate with.”

“We have had the approach of continuously evaluating and improving our supplier relationships for a long time. A recent addition to this approach was to also consider financial costs in our discussions with the suppliers. Initially, our purchasing organization requested a supplier finance program for Asia/China, in response to which our Group Treasury negotiated and provided the tool for supplier financing.

“We have been discussing the structure of this program with our suppliers and adjusting it to achieve better performance. The savings amount varies depending on the specific arrangement we have with a particular supplier. **Overall, the program has helped both us and our suppliers reduce supply chain costs and better understand each other.**”

**Organizational Strategies for Supply Chain Finance**

The Best in Class outperform their peers with the help of more diversified SCF techniques tailored to their company needs and are much more likely to have a cross-functional team managing SCF programs for LCCS. Establishing a cross-functional team comprised of purchasing, supply chain, and finance professionals is one of the key success factors for the Best in Class (Figure 2).
Setting up a cross-functional team that evaluates specific SCF techniques and their potential to lower the cost of capital, total landed cost, and reduce supply base risk ensures that the departmental performance metrics and goals are aligned with the overall company strategy and compliment each other. The interdepartmental misunderstandings and often contradictory goals between purchasing and treasury executives need to be eliminated if a company wants to be strategic in its choice of SCF practices for LCCS.

**Finance’s Involvement**

Finance needs to evaluate not only the traditional DPOs but the total landed cost of procured goods that includes financing costs in the supply chain. Working together with procurement and supply chain counterparts, treasurers and CFOs must find ways to collaborate with suppliers in a way that optimizes the financial supply chain for both.

Best in Class companies are much more likely to have finance’s involvement in developing LCCS strategies.
Without a cross-functional approach to SCF strategies, especially in LCCS programs, the success of the LCCS initiative is much less likely.

**Understanding Your Suppliers is Key for a Successful Relationship**

The disconnect between the desired goals and the planned actions of buyers and their suppliers can be the biggest obstacle to improving the financing and payment practices in a supply chain. Our research shows that there is not enough communication between the two parties on such key issue as the impact of their trade and payment arrangements on the short- and long-term liquidity and working capital management for the supplier. Figure 4 illustrates the lack of communication regarding supplier issues:

**Figure 4. What Attributes of Your Emerging Market Supplier Do You Know?**

- Your supplier’s payment terms with its suppliers: 45%
- The difference between your cost of capital and that of your suppliers in your primary low-cost country region: 40%
- Cost of capital for your supplier: 40%
- Ease of access to capital for the supplier: 22%
- % of your orders/invoices your suppliers are factoring: 20%
- Your supplier’s cost of factoring: 18%
- Rate at which supplier obtains trade financing: 13%

Source: Aberdeen Group, November 2006

Figure 4 proves how many buyers are unaware of the vital activity indicators of their emerging market suppliers. Less than half commonly know about their suppliers’ cost of capital and how it compares to their own, as well as about the cash flow challenges their supplier may be going through if the buyer payment terms are in discordance with the payment terms it has with its own suppliers.

The questions about how much it costs suppliers to manage trade finance underlying their relationship with the buyer – such as the cost of factoring receivables from a particular buyer or the rate at which other funding is available – remain largely unattended. This means that not enough companies are investigating the potential savings opportunities from tighter collaboration on SCF issues.

“Buyer-supplier collaborative issues sometimes go at a cost, as the company must ‘move’ at the same technological pace with the buyer despite the inadequacies in automating most of the operational systems.”

– Mid-size supplier (Middle East/Africa region)
Best in Class companies are moving ahead of the curve in their practices by proactively reaching out to their suppliers. This is made easier by their use of cross-functional teams that can better communicate the value of new SCF arrangements to their supply chain partners.

<table>
<thead>
<tr>
<th>Challenges Emerging Market Suppliers Face with Their Financial Processes</th>
</tr>
</thead>
<tbody>
<tr>
<td>⇒ “Unknown...that's the problem”</td>
</tr>
<tr>
<td>― Large North American aerospace manufacturer</td>
</tr>
<tr>
<td>⇒ “Cash flow management is always an issue. Generally they will 'back to back' our LC to get funding for the components required to build our order”</td>
</tr>
<tr>
<td>― Mid-size Australian retailer</td>
</tr>
<tr>
<td>⇒ “Cost of capital in low-cost countries is variable. It is difficult for suppliers to project capital requirements and costs, so expansions are usually delayed”</td>
</tr>
<tr>
<td>― Mid-size North American wholesaler</td>
</tr>
<tr>
<td>⇒ “Lack of third-party financing”</td>
</tr>
<tr>
<td>― North American chemical manufacturer</td>
</tr>
<tr>
<td>⇒ “Obtaining financing for their projects is cumbersome and cost almost prohibitive to construct in a cheaper way”</td>
</tr>
<tr>
<td>― European insurance company</td>
</tr>
<tr>
<td>⇒ “Timely availability of money in order to finance raw materials in time”</td>
</tr>
<tr>
<td>― Mid-size North American consumer packaged goods company</td>
</tr>
<tr>
<td>⇒ “Getting liability insurance”</td>
</tr>
<tr>
<td>― Large North American consumer durables company</td>
</tr>
<tr>
<td>⇒ “Capital availability”</td>
</tr>
<tr>
<td>― Large North American industrial equipment manufacturer</td>
</tr>
</tbody>
</table>
Chapter Three: Implications & Analysis

Key Takeaways
- Payment terms extension and early payment discount program are the most widespread SCF practices.
- Fully 4.71 percentage points is the average difference between the buyer’s cost of capital and that of its suppliers in East/South/Southeastern Asia.
- Large companies are almost four times more likely to be planning to spend over $500,000 in SCF technology over the next 18 months.

New Savings Opportunities with SCF

As fully 80% of the buyers in the study currently source materials from Asian suppliers, this group has been chosen to illustrate the potential savings opportunities from improving SCF practices.

Table 3 outlines the tremendous magnitude of value trapped in the supply chain for buyers sourcing from East, Southeast, and South Asian regions (see next page).

Financial challenges of emerging market suppliers impact their ability to buy raw materials, keep sufficient work-in-process inventory to fulfill orders on time, meet high quality standards, support rush orders, or keep pace with a buyer’s business growth.

Buyers that want to move to the next maturity level in SCF and LCCS can achieve better performance with the following opportunities:

Improved Payment Automation and Visibility to Extend DPOs

Helping your emerging market suppliers gain better visibility into their payment stream enables them to improve cash flow forecasting. This is a great way to bring suppliers value in return for negotiating better payment terms for your company.

This approach includes better communication between your Accounts Payable department and the supplier as well as an effort on your part to make payments more regularly. Adopting a new SCF technology platform can be a powerful way to provide joint visibility and automation to the purchase order-to-payment process.

Common Characteristics of Emerging Market Suppliers
- Average cost of short-term capital, annualized % (for suppliers in the survey): **17.5%**
- Cost of factoring LCs/confirmed purchase orders – **15-20%** of the factored amount
- Limited ability to expand/open lines of credit to support business growth or raw material orders for large orders
### Table 3. The Magnitude of SCF Opportunities for Buyers Sourcing from Asia

| Buyer-Side Performance Metric | Savings Opportunity | Sample Calculation: A hypothetical large U.S. buyer sourcing $500 million from China annually (estimated $41.7 million monthly). Average cost of short-term financing (30-day unsecured loan) is 1.5% for the buyer. |
|------------------------------|---------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------###
### Sample Calculation: A hypothetical large U.S. buyer sourcing $500 million from China annually (estimated $41.7 million monthly). Average cost of short-term financing (30-day loan) is 1.5% for the buyer.

| Buyer-Side Performance Metric | Savings Opportunity | Current survey benchmark data (only buyers sourcing from Asia): Average difference between the buyer’s annualized cost of capital and that of its suppliers in the primary emerging market = **4.71** percentage points

On average, participating buyers have reported DPOs of 46 days with their Asian suppliers. For such a supplier, the ability to obtain financing during this period at a rate close to the buyer’s rate (e.g. if they participate in reverse factoring), could translate to noticeable savings. In our example, the maximum savings is shown below (‘4.71’ refers to the annualized cost of capital difference, 46 days = 12.6% a year):

\[
\text{Savings} = \text{Average difference between the buyer’s annualized cost of capital and that of its suppliers} \times \text{12.6\%} \times \text{Amount Borrowed}
\]

\[
= 4.71\% \times 12.6\% \times $41.7 \text{ million}
\]

\[
= $247,473 \text{ (monthly savings)}
\]

\[
\text{Annualized Savings} = $2,969,676
\]

| Inventory carrying cost | Third-party in-transit/inventory financing | Assumption 1. The buyer chooses to finance inventory for 30 days with a regular inventory loan (no title transfer). Suppose, considering the credit rating of the company and the kind of goods in inventory, the cost of this loan is 1.2%.

\[
\text{Savings} = (\text{Rate of unsecured 30-day financing} – \text{rate at which inventory financing is obtained}) \times \text{Amount Borrowed}
\]

\[
= (1.5\% - 1.2\%) \times $41.7 \text{ million} = $125,100 \text{ (monthly savings)}
\]

\[
\text{Annualized Savings} = $1,501,200
\]

\[
\text{Note: A different type of inventory financing is the technique when the title of goods in inventory is passed over to the 3rd party that provides financing. The cost of such financing is usually higher but a company should consider that this cost includes the embedded risks incurred by the 3rd party financier, such as the uninsured credit risk, and other risks accompanying the title transfer.}
\]

Source: AberdeenGroup, November 2006
**Reducing the Cost of Goods Sold: Early Payment Discount Programs**

The cost of goods sold can be reduced through an effective negotiation process that outlines the additional value a supplier can receive in return for accepting a discount on its orders. An early payment discount program is one way for a buyer to reduce the invoice value, especially applicable when an enterprise has excess cash on hand. Having visibility into the financial supply chain allows a buyer to be notified of available discounts and take due advantage of them.

**Access to Alternative Receivables Financing for Suppliers**

Another way to negotiate a lower cost of goods sold with emerging market suppliers is by offering them participation in an SCF arrangement whereby a supplier that has a high cost of capital and constricted access to trade financing can leverage the better credit rating of its buyer to obtain pre- or post-export financing at a lower rate. Taking advantage of this arbitrage opportunity can ease supplier’s cash flow problems and ensure that the buyer has a less risky, more reliable, and less costly supply base.

**Third-Party Inventory Financing**

Goods sourced from an emerging market supplier often have extended transit times, especially if goods are moved by ocean. Consider potential savings from financing this stage of your supply chain via a third-party finance provider.

**Most Common Supply Chain Finance Practices**

To gain a competitive advantage, early adopters are adopting new SCF techniques and are upgrading their underlying processes and technologies. However, the majority of firms still employ traditional practices in financing and payment. Table 4 showcases the most common SCF processes for buyers and suppliers:

<table>
<thead>
<tr>
<th>Table 4. Most Common Supply Chain Finance Practices</th>
</tr>
</thead>
<tbody>
<tr>
<td>Buyers</td>
</tr>
<tr>
<td>Program to extend payment terms</td>
</tr>
<tr>
<td>Early payment discount program offered by your company</td>
</tr>
<tr>
<td>Buyer-financed raw materials for LCCS suppliers</td>
</tr>
<tr>
<td>Buyer-financed work-in-progress for LCCS suppliers</td>
</tr>
<tr>
<td>3rd party financing of vendor-managed inventory</td>
</tr>
</tbody>
</table>

Source: Aberdeen Group, November 2006
The Impact of Supply Chain Finance Technology

Realizing the value trapped in the financial supply chain is difficult without gaining an adequate level of visibility into the physical supply chain events first, followed by improved visibility into payment and invoice status. Different companies have achieved varying levels of automation of the procure-to-pay process, which is influenced by such factors as company size, geographical organization, industry of operation, as well as the business model.

- “Large corporations still have a lot more to gain from automating their financial supply chains, improving and extending their use of standards and the reach of technology,” says Nigel Woodward, director of worldwide financial services at Intel. “The enabling technology in this field needs to be continuously developed, including infrastructure and domain-specific capabilities such as messaging, treasury and payments; as well as the extension of the compute envelope and process automation to mobile devices.”

Figures 5 and 6 show the current level of procure-to-pay process automation and the planned technology adoption trends over the next 18 months.

Figure 5. Current Automation of the Procure-to-Pay Process

- P.O.-to-invoice-to-payment process automation 48%
- Accounts payable/Accounts receivable automation 46%
- None, all processes are manual or spreadsheet-based 27%
- Automated early payment discounting 18%
- 'Pay me now' discounting (dynamic discounting) 6%
- Collaborative online invoice dispute resolution 5%

% of buyers and suppliers

Source: Aberdeen Group, November 2006
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. The most efficient technology strategies have led to markedly better visibility into the physical and financial supply chains (as reported by about one-fifth of buyers and about one-tenth of suppliers). The study participants were also asked about the specific plans for SCF technology investment over the next 18 months. Figure 7 depicts the specific U.S. dollar ranges of planned technology investment over the next 18 months for companies above and below US$1 billion in revenue.
Case Study: Mitsui’s Best in Class Strategy

The large Japanese trading group, Mitsui & Co. Ltd, adopted a third-party transaction management platform for some of its business in 2002 and has been rewarded with significant cost savings and improved efficiency in all trade-related processes. “We needed a web-based solution that would allow us to electronically exchange documents both within our company and with our trade partners, thus reducing the amount of paper involved in the process,” says Shinya Imai, general manager of the trade function business department.

First Trial
Mitsui decided that the first trial of the new solution would be in the textiles group. Said Imai: “In the textiles and apparel trading business, we handle frequent shipments, which are paid for with letters of credit (LCs), and these generate floods of paper documents that have to be distributed manually within our offices and those of our suppliers and customers. On the import side, there are frequent amendments of L/s, a serious issue, which slows the payments cycle. Our systems have been in urgent need of rationalization. We also decided to trial the platform for the export of synthetic resin to Korea.”

Implementation Results
Cost savings were immediate, reports Imai: “On the import side, we had two US$50,000 shipments a week from Hong Kong to Japan and the direct cost of payment using the new platform assured transaction per consignment was $150 on average. Using the new technology platform, with its automatic online compliance engine as an alternative to LCs, we reduced the direct costs by 50%, and the indirect costs, mainly labor, by 51%. The overall cost saving compared with LC operation was about 50%. For our export business, the direct cost reductions are about 30% and the labor costs are reduced by 68%, so the overall cost reduction is also about 50%.

“Using this new transaction management platform has allowed us to significantly cut down the amount of paper that is shuffled, and to achieve an unprecedented level of speed, accuracy and full transparency for our trade processes,” says Imai. “Credit management has improved too: the new platform’s electronic documents, financial system and the guaranteed payments make credit more manageable.”

Defining Your Supply Chain Finance Maturity Level

To gauge your company’s SCF maturity, use Table 5 to assess your practices across five categories: strategy, organization, knowledge, technology, and financing.

<table>
<thead>
<tr>
<th>SCF Strategy</th>
<th>Laggards</th>
<th>Industry Average</th>
<th>Best in Class</th>
</tr>
</thead>
<tbody>
<tr>
<td>SCF Strategy</td>
<td>Investigating options for SCF</td>
<td>Have firm plans to enhance SCF practices</td>
<td>Actively using SCF techniques to reduce end-to-end supply chain costs</td>
</tr>
<tr>
<td></td>
<td>Laggards</td>
<td>Industry Average</td>
<td>Best in Class</td>
</tr>
<tr>
<td>----------------------</td>
<td>---------------------------------------------------------------------------</td>
<td>---------------------------------------------------------------------------------</td>
<td>------------------------------------------------------------------------------</td>
</tr>
<tr>
<td><strong>Organization</strong></td>
<td>No one in the company is specifically focused on SCF</td>
<td>SCF programs are led by the finance department</td>
<td>A cross-functional team is taking the leading role in SCF initiatives</td>
</tr>
<tr>
<td><strong>Knowledge</strong></td>
<td>No online view of payment process or in-process/in-transit order status</td>
<td>Differing views of cash flow and order status between buyer and seller</td>
<td>Collaborative order status and cash flow visibility for both buyer and seller</td>
</tr>
<tr>
<td><strong>Technology</strong></td>
<td>Manual-intensive payment processes</td>
<td>Use electronic invoice presentation and payment (EIPP) systems or other invoice or evaluated receipts automation systems</td>
<td>Use online platforms with automated discounting and invoice reconciliation capabilities; may use online payment platform with access to third-party financing</td>
</tr>
<tr>
<td><strong>Financing</strong></td>
<td>Rely on letters of credit and open accounts</td>
<td>Use own cash for early payment discounts</td>
<td>▪ Early payment programs include dynamic discounting</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>▪ May use third-party financing to leverage the strength of buyer’s credit and balance sheet to lower end-to-end costs</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>▪ Facilitate in-process and inventory financing in their supply chain</td>
</tr>
</tbody>
</table>

Source: AberdeenGroup, November 2006
Chapter Four: Recommendations for Action

Key Takeaways

• Institute a cross-functional team of finance, purchasing, and supply chain professionals to evaluate opportunities in SCF.
• Know 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.

If your company is searching for new ways to remain or become competitive in your market, SCF is a key area on which to focus next. Companies that have focused on improving SCF practices have been able to realize both hard and soft savings in finance, business process management, and financial transaction processing. For the Best in Class companies involved in this study, this has enabled a new wave of savings from their low-cost country sourcing programs.

If your company’s DPOs have not improved markedly in the past two years or if you have not seen a continued total landed cost improvement on goods sourced from emerging markets during that time, then your company should rethink its current SCF practices with low-cost country suppliers. The following Recommendations for Action should be considered.

Companies that have seen improvements can look to the “Best in Class Recommendations” for additional steps to take.

Recommendations for Action

1. Adopt a Cross-Functional Organizational Approach

Action: Set up a cross-functional SCF team with at least a part-time finance staff member involved.

Best in Class buyers are twice as likely as their peers to have implemented a cross-functional team of finance, purchasing, and supply chain professionals to evaluate SCF initiatives in emerging market sourcing. This factor is among the most important determinants of SCF success. A cross-departmental team will help your company make more optimal decisions that will result in lower unit costs and improved corporate financial metrics.
Best in Class Recommendation: Dedicate a full-time finance staff member to the cross-functional SCF team.

Increasing cross-departmental collaboration on SCF techniques and metrics will ensure that the company can capitalize on SCF innovations, better align with corporate goals, and reduce transactional costs.

2. Improve Supply Chain Finance Practices

Action: Work together with your preferred suppliers to determine ways to improve the financial supply chain between your companies. Clearly convey the magnitude of potential savings and ensure the supplier will also benefit from the new proposed practices.

Evaluate the cost structure for both your company and your preferred suppliers, including the pre- and post-export financing rates, any financial regulations by the local governments, as well as the working capital ratios at your company (e.g. does your company consistently have excess cash on hand or is it often cash-strapped?).

Assess the viability and feasibility of early payment discount programs, using your own cash or third-party financing, the impact of extending your DPOs, and the opportunities to reduce unit costs.

Work with your financial institutions or third-party SCF specialists to explore emerging opportunities in this space. Depending on particular demands of your company (including the accounting concerns you may have regarding debt vs. payables on your balance sheet or in-transit inventory accounting issues), your company may be better off partnering with either a bank- or non-bank financial institution, or a third-party technology solution provider that also acts as a source of financing (or enables bringing in your existing financial partner to use the platform).

Best in Class Recommendation: Work closely with your suppliers to maintain the current favorable terms while at the same time considering new ways to make your financial supply chain more competitive.

Optimize the financing schemes and management strategies for your inventory: Is a particular supplier capable of carrying out a vendor-managed inventory program? Is third-party financing needed for this process? Or would the end-to-end costs in your supply chain be lower if you obtained a low-rate inventory loan to purchase inventory sooner and free up cash your supplier needs to start the next production cycle? And if this is the case, could you negotiate a lower per-unit cost from your supplier in return?

Help your suppliers help you. As your business grows, monitor the progress of your suppliers and try to foresee any risks of supply chain disruptions. Shortage of capital is a prevailing problem for emerging market suppliers, so if you want them to keep up with your business development, consider offering them programs and tools to enhance their financial processes and gain better access to capital.

3. Choose the Right SCF Technology

Action: Automate the financial processes with your suppliers to gain a more up-to-date online view of the P.O./invoice/payment status and enable your financial insti-
tion partner to estimate the financial risk at all stages in the supply chain to pro-
vide trade financing at corresponding rates.

Without proper visibility into physical and financial supply chains, it is impossible to
estimate the level of risk at the key stages of the procure-to-pay process, which greatly
decreases the possibilities of accessing favorable third-party or partner financing or other
funding techniques.

Evaluate the benefits of on-boarding your core suppliers onto a shared technology plat-
form that enables a common view of the financial supply chain transactions. Buyers that
already have trade discounting programs in place or plan on introducing them soon,
should consider automating these programs to generate more savings for the company.
Additional benefits can be obtained by automating invoice dispute resolution, which im-
proves the quality of data transmitted into the accounting system and enhances compli-
ance.

**Best in Class Recommendation:** Work closely with your suppliers to extend auto-
mation of the physical and financial supply chain.

Onboard as many of your suppliers as possible to use the shared SCF technology plat-
form. A near-real-time consistent view of data throughout the supply chain is a crucial
component of achieving a win-win SCF program. In addition to the opportunities re-
viewed in the previous section, Best in Class companies can use their visibility into the
physical and financial supply chain to develop the most up-to-date SCF metrics and sup-
plier scorecards to track both their suppliers’ and their own performance.

Having automated the basic transactional processes, as well as added the automated dis-
pute resolution and chargeback processes, Best in Class buyers can get truly strategic in
building a system that can monitor their supply chain’s performance and detect/prevent
physical and financial disruptions at early stages.
Author Profile

Viktoriya Sadlovska
Research Analyst, Supply Chain Finance
Aberdeen Group, Inc.

Viktoriya Sadlovska focuses on various research topics in Financial Value Chain Management. She has extensive experience in researching, analyzing, and writing about numerous topics in economics, finance, and international trade. Sadlovska has worked on developing international economic ties of Odessa Region, Ukraine; she was responsible for international financial transactions and logistics of a small business firm in Ukraine; and in the U.S., she has worked for a non-profit organization focused on international economic development, taught various subjects in economics, and participated in grant-funded research that investigated the impact of border security on international trade. Sadlovska has recently obtained a Master’s Degree in Economics from the University of Maine.

Beth Enslow
Senior Vice President, Enterprise Research
Aberdeen Group, Inc.

Beth Enslow is senior vice president of enterprise research for Aberdeen Group. Enslow benchmarks and advises companies on how they can reshape their supply chain, global trade, and transportation processes and technology strategies to drive business value.

Prior to joining Aberdeen Group, Enslow was senior vice president of strategic development for Descartes Systems Group, a global supply chain software company. At Descartes, she led initiatives in such areas as RFID, wireless-enabled delivery, and inventory performance management. Before that, Enslow was research director at Gartner, Inc., where she ran its supply chain planning and logistics advisory practice on a global basis. She has worked for a number of other research and consulting organizations, including the Conference Board, a leading business think tank and economic forecasting organization. Enslow is also a lecturer on supply chain technology and supply chain finance at the Center for Supply Chain and Logistics Management at York University’s Schulich School of Business in Toronto.
Featured Underwriters

JPMorganChase

The Treasury Services business of JPMorgan Chase is a top-ranked, full-service provider of innovative payment, collection, liquidity and investment management, trade finance, commercial card and information solutions to corporations, financial services institutions, middle market companies, small businesses, governments and municipalities worldwide. With more than 50,000 clients and a presence in 36 countries, JPMorgan Chase Treasury Services is the world's largest provider of treasury management services.
Featured Underwriters

UPS offers businesses worldwide the opportunity to integrate supply chain financing and supply chain management. With an array of financial services designed to help your business participate fully in the growing global economy, UPS Capital can add its financial strength to your vision. The result is strong, profitable growth.

The addition of financial services to the other capabilities of UPS can provide resources for companies to enhance their competitive advantage by leveraging the supply chain - the flow of goods, information, and funds - through one single global service provider: UPS.
## Sponsor Directory

<table>
<thead>
<tr>
<th>JPMorgan Chase</th>
<th>UPS</th>
</tr>
</thead>
<tbody>
<tr>
<td>JPMorgan Chase Bank N.A.</td>
<td>UPS Capital</td>
</tr>
<tr>
<td>One Chase Manhattan Plaza 3rd Floor</td>
<td>35 Glenlake Parkway NE</td>
</tr>
<tr>
<td>New York, New York 10081</td>
<td>Atlanta, GA 30328</td>
</tr>
<tr>
<td>212-552-8635</td>
<td>1-800-637-0620</td>
</tr>
<tr>
<td><a href="http://www.jpmorganchase.com">www.jpmorganchase.com</a></td>
<td><a href="http://www.upscapital.com">www.upscapital.com</a></td>
</tr>
<tr>
<td><a href="mailto:edward.c.simpson@jpmchase.com">edward.c.simpson@jpmchase.com</a></td>
<td><a href="mailto:schmura@ups.com">schmura@ups.com</a></td>
</tr>
</tbody>
</table>
During November 2006, Aberdeen Group surveyed 143 companies involved in emerging market sourcing to estimate the savings opportunities from improving the supply chain finance practices. Considering the specific nature of low-cost country sourcing, this particular group of companies was chosen as the best focus group to illustrate the potential impact of supply chain finance techniques. The study examines how revised supply chain finance practices can help extend the financial benefit already realized from low-cost country sourcing.

The follow-up telephone interviews were conducted with certain study participants, as well as other enterprises with similar characteristics.

The demographics of the survey participants are the following:

- **Geography:** 52% of companies represented in the sample are headquartered in North America, 28% - in EMEA (Europe Middle East/Africa), 17% - in Asia/Pacific, and 2% in South/Central America.

- **Job title:** C-level (including CEO, CFO, COO, etc) - 6%, VP or Director - 31%, Manager - 30%, Other - 22%

- **Company size:** 20% of companies were classified as small businesses (less than $50 mln. In annual revenue), about one-third of respondents (36%) were mid-market ($50 - $999 mln. in annual revenue), and 44% were from large enterprises (over $1 bln. in annual revenue)

- **Industry:** The research sample included respondents from a variety of industries, with the following sectors most prominently represented: automotive, chemicals, consumer goods, high technology, industrial equipment manufacturing and retail.
Appendix B: Related Aberdeen Research & Tools

Related Aberdeen research that forms a companion or reference to this report includes:

- Sourcing from Low-Cost Countries? Supply Chain Financing and Technology Innovations May Help Extend LCCS Benefits (November 2006)
- Supply Chain Finance Benchmark Report (September 2006)
- Get Ahead with Supply Chain Finance: How to Leverage New Solutions for End-to-End Financial Improvement (July 2006)
- Turning Your CFO Into a Supply Chain Cheerleader (June 2006)
- New Paradigm Supply Chain Finance Offerings Compel CFO and Treasury Interest in the Supply Chain (April 2006)
- Rethinking China Sourcing: From Total Landed Cost to Total Delivered Profit (January 2006)
- The CFO’s Agenda for Global Trade (September 2005)

Information on these and any other Aberdeen publications can be found at www.Aberdeen.com.
New Strategies for Financial Supply Chain Optimization

Aberdeen Group, Inc.
260 Franklin Street
Boston, Massachusetts
02110-3112
USA

Telephone: 617 723 7890
Fax: 617 723 7897
www.aberdeen.com

© 2006 Aberdeen Group, Inc.
All rights reserved
November 2006

The information contained in this publication has been obtained from sources Aberdeen believes to be reliable, but is not guaranteed by Aberdeen. Aberdeen publications reflect the analyst’s judgment at the time and are subject to change without notice.

The trademarks and registered trademarks of the corporations mentioned in this publication are the property of their respective holders.

Founded in 1988, Aberdeen Group is the technology-driven research destination of choice for the global business executive. Aberdeen Group has over 100,000 research members in over 36 countries around the world that both participate in and direct the most comprehensive technology-driven value chain research in the market. Through its continued fact-based research, benchmarking, and actionable analysis, Aberdeen Group offers global business and technology executives a unique mix of actionable research, KPIs, tools, and services.
The following acts are strictly prohibited:

- Reproduction for Sale
- Transmittal via the Internet

Copyright © 2006 Aberdeen Group, Inc. Boston, Massachusetts

Terms and Conditions

Upon receipt of this electronic report, it is understood that the user will and must fully comply with the terms of purchase as stipulated in the Purchase Agreement signed by the user or by an authorized representative of the user’s organization. Aberdeen has granted this client permission to post this report on its Web site.

This publication is protected by United States copyright laws and international treaties. Unless otherwise noted in the Purchase Agreement, the entire contents of this publication are copyrighted by Aberdeen Group, Inc., and may not be reproduced, stored in another retrieval system, or transmitted in any form or by any means without prior written consent of the publisher. Unauthorized reproduction or distribution of this publication, or any portion of it, may result in severe civil and criminal penalties, and will be prosecuted to the maximum extent necessary to protect the rights of the publisher.

The trademarks and registered trademarks of the corporations mentioned in this publication are the property of their respective holders.

All information contained in this report is current as of publication date. Information contained in this publication has been obtained from sources Aberdeen believes to be reliable, but is not warranted by the publisher. Opinions reflect judgment at the time of publication and are subject to change without notice.

Usage Tips

Report viewing in this PDF format offers several benefits:

- **Table of Contents**: A dynamic Table of Contents (TOC) helps you navigate through the report. Simply select “Show Bookmarks” from the “Windows” menu, or click on the bookmark icon (fourth icon from the left on the standard toolbar) to access this feature. The TOC is both expandable and collapsible; simply click on the plus sign to the left of the chapter titles listed in the TOC. This feature enables you to change your view of the TOC, depending on whether you would rather see an overview of the report or focus on any given chapter in greater depth.

- **Scroll Bar**: Another online navigation feature can be accessed from the scroll bar to the right of your document window. By dragging the scroll bar, you can easily navigate through the entire document page by page. If you continue to press the mouse button while dragging the scroll bar, Acrobat Reader will list each page number as you scroll. This feature is helpful if you are searching for a specific page reference.

- **Text-Based Searching**: The PDF format also offers online text-based searching capabilities. This can be a great asset if you are searching for references to a specific type of technology or any other elements within the report.

- **Reader Guide**: To further explore the benefits of the PDF file format, please consult the Reader Guide available from the Help menu.