How supply chain finance helps SMEs optimize cash flow and grow?

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What is Supply Chain Finance (SCF)?

In a supply chain, buyers and suppliers have competing financial interests. The buyer wants to pay as late as possible whilst the supplier wants to be paid as early as possible. This method places the financial burden on other parties, complicating efforts to establish trust and foster long-term business relationships. Conventional financing approaches worsen the problem, resulting in inefficiencies and financial pressure. Such a conflict is addressed by a form of finance "SCF" which provides a range of financing and risk mitigation solutions to optimize working capital and liquidity in domestic and international supply chains.

Why is supply chain finance critical for SMEs?

It is critical because it addresses their key financial and operational challenges:

Improved Cash Flow: SCF bridges the gap between payment cycles, enabling SMEs to access working capital tied up in receivables or inventories.

Access to Affordable Financing: Leveraging the creditworthiness of large buyers in the supply chain, SMEs can secure financing at lower interest rates compared to traditional loans.

Operational Stability: SCF reduces financial stress, allowing SMEs to focus on production, meeting demand, and fulfilling orders without delays.

Enhanced Competitiveness: By improving liquidity, SCF enables SMEs to scale operations, invest in technology, and participate in larger deals with confidence.

Risk Mitigation: SCF reduces the risk of defaults and bad debts by shifting credit risk to financial institutions or through invoice factoring.

Strengthened Supply Chain Relationships: Timely payments facilitated by SCF foster trust and collaboration between SMEs and their larger corporate partners, ensuring a resilient supply chain.

Disruptive potential of supply chain finance?

Traditionally, supply chain finance has been inaccessible to smaller suppliers, as bank-led programs are designed to prioritize participants with strong credit ratings. The disruptive potential of supply chain finance lies in its ability to connect smaller suppliers to credit based on the buyer's creditworthiness rather than their own. This innovation enables non-investment grade and tail-end suppliers to access larger pools of capital. By unlocking credit for these suppliers, supply chain finance shifts the competitive landscape, allowing smaller players to scale operations, gain better visibility into payment cycles, and secure working capital efficiently.

A key example of this disruption is the $300 million facility pilot launched by the International Finance Corporation (IFC) and Citi under IFC's Global Supply Chain Finance Program (GSCF). This initiative aims to provide essential supply chain financing to suppliers and buyers in emerging markets, addressing liquidity constraints and enhancing market resilience during global economic uncertainties.

Fintech innovations in the field of supply chain finance?

The primary innovations in SCF are happening in the fintech space across the following dimensions:

Origination: Unique customer acquisition channels reduce competition and enable lenders to offer non-competitive rates with low customer acquisition costs and high margins.

Underwriting: Advanced credit assessment using transactional data lowers capital costs and creates competitive barriers for new entrants.

Capital Sourcing: Access to alternative, cheaper capital allows lenders to offer lower rates or higher margins, benefiting both the company and customers.

Collections & Servicing: Efficient repayment mechanisms, like embedded finance, minimize defaults and enable lending to riskier customers while maintaining profitability.

Case studies of such innovations in the major emerging economies?

The following examples showcase how fintech innovations are reshaping SCF in emerging economies, providing SMEs with vital tools to optimize cash flow, reduce financial friction, and drive sustainable growth.

China:

MY bank's Digital SCF Platform - MYbank, an internet-based bank in China, has developed a digital SCF platform to support SMEs. By leveraging digital technologies, MYbank offers decentralized and comprehensive coverage of supply chain links, enhancing the sustainability of SCF. Between 2018 and 2022, this initiative led to a significant increase in financing availability for SMEs, enabling them to expand operations and improve financial stability.

E-commerce-Centred SCF Models:

E-commerce platforms have integrated SCF solutions to support SMEs within their ecosystems. JD.com, a leading Chinese e-commerce company, has developed an SCF business model that leverages its digital infrastructure to provide efficient financing options to SMEs. This approach has enhanced SMEs' competitiveness and operational efficiency.

Saudi Arabia:

In Saudi Arabia, SMEs have focused on building supply chain resilience through agility, flexibility, and robustness. A study involving 255 SME managers revealed that enhancing these aspects positively impacted production and market performance. This approach has been crucial in navigating uncertainties and improving overall business performance in the region.

Brazil:

SKY Brasil's Fintech Initiative: Grupo Werthein, SKY Brazil's parent company, launched "SKX", a fintech initiative backed by a $161Mn investment. Targeting small businesses within SKY Brazil's supply chain, SKX offers payment services like credit and debit cards, with plans to roll out credit and microcredit options. This program aims to support around 1,500 small partners, including salespeople, call centres, and technicians.

Clara's Growth in Brazil: Clara, a Latin American fintech, has expanded its presence in Brazil by appointing a new finance director to manage its rapidly growing operations. Clara offers corporate credit cards, invoice management, and cross-border payment solutions, serving clients like Burger King and Toyota. With over $484Mn reals in total payment volumes, Clara's solutions have been widely adopted by Brazilian SMEs.

Mexico:

Clara's SCF Solutions: Clara's success extends to Mexico, where its SCF offerings, such as corporate credit cards and invoice management, have positively impacted SMEs. Its rapid growth and strong client base highlight its effectiveness in improving cash flow management and operational efficiency for Mexican businesses.

India:

Peer-to-Peer (P2P) Lending:

P2P lending platforms connect SMEs directly with individual lenders, bypassing traditional financial institutions. In India, P2P fintechs such as "Faircent" offer necessary infrastructure for such lending, providing SMEs with alternative financing options.

Buy Now Pay Later (BNPL) Services:

BNPL services offer short-term financing solutions that allow SMEs to make purchases and pay at a future date, usually interest-free. This model has gained traction in India, addressing high consumer credit demand and low credit card penetration.

Amazon Pay Later and Capital Float: Amazon India has collaborated with Capital Float to offer the Amazon Pay Later service. This BNPL option allows customers to purchase products on Amazon and defer payments, enhancing shopping flexibility. Capital Float provides the necessary financing infrastructure for this service.

Flipkart Pay Later: Flipkart, a leading Indian e-commerce platform, offers its own BNPL service called Flipkart Pay Later. This service enables customers to make purchases and pay for them later, simplifying the shopping experience

Thus, New supply chain finance technologies provide significant benefits for banks, buyers, and suppliers. They help banks improve and streamline their SCF services, allow buyers to better manage liquidity and strengthen partnerships, and enable suppliers to quickly access financing with ease.