

WHITEPAPER

Mid-Market and Small Companies Fuel Sustainable Growth with Supply Chain Finance

About the Authors



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Cheik has been a leader in value engineering for the past 20 years. He has worked extensively with CFOs and other executives to help them plan, execute and realize value from transformation initiatives. In this capacity, Cheik has worked with hundreds of organizations, both on the corporate and governmental sides, while at SAP, Oracle, Teradata and Kyriba. Digital transformation, especially for finance and supply chain management, is one of his specialties. Transforming finance, treasury, risk and working capital management into strategic liquidity performance management discipline is one of the areas in which he specializes. At Kyriba, he leads the global value engineering organization, whose charter is to collaborate with existing and prospective clients to understand, quantify and achieve business value from Active Liquidity Management (Active Treasury, Active Payments, Active Risk Management and Active Working Capital Management). Cheik holds a master's degree in economics, with a focus on economic development, and an MBA in finance.



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Shruti is a business value engineer at Kyriba, where she helps companies in understanding supply chain finance business value and building a case for change. She has been part of the fintech industry (Kyriba and Morgan Stanley) for over five years while working in different regions of India, France and the U.S. Shruti holds an MBA (strategy) from HEC Paris and a BTech from IIT-BHU, India.

Crucial Role of Small and Medium Size Enterprises (SMEs) for Global Economic Development

With Supply Chain issues creating shortages across the globe, it is more and more evident that SMEs impact economic development for a broad spectrum of countries.

Role of Small and Medium Businesses in Economy and Development

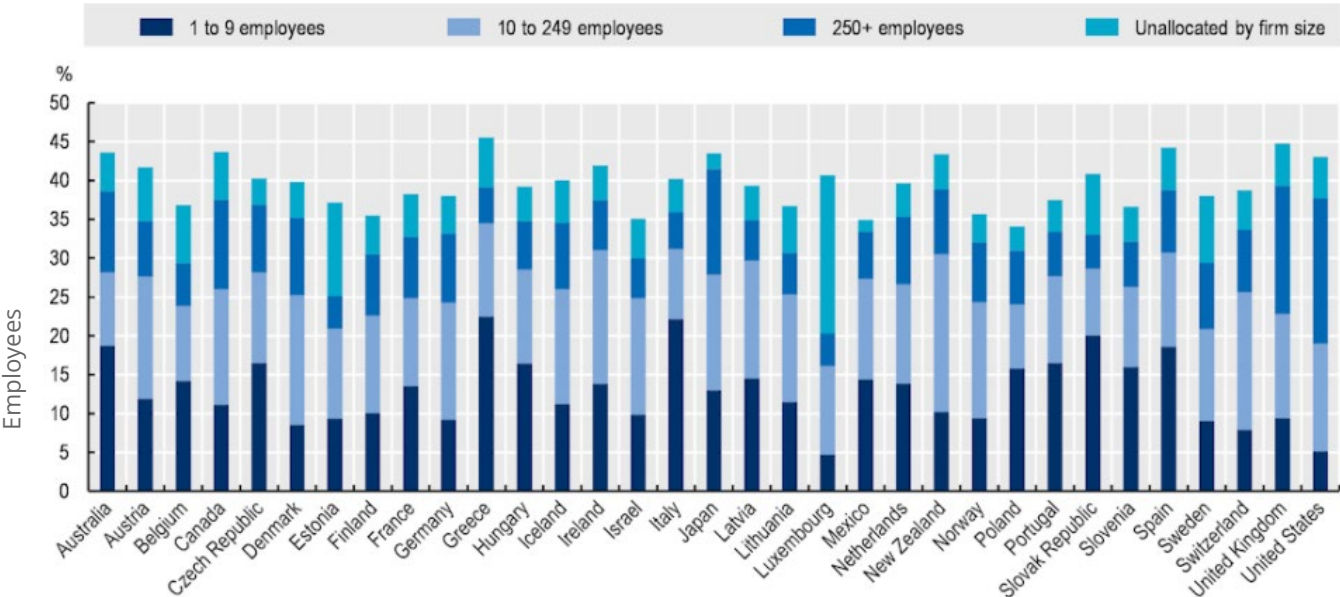
Small and medium enterprises (SMEs) are the backbone of economies and societies. They play a crucial role in a country's overall production and are core to sustainable socioeconomic development. All over the world, there is growing evidence of the significant impact of SMEs in both developed and developing countries.

Small and medium-sized businesses are important contributors to employment creation, value creation, poverty alleviation and income generation. They represent about 90 percent of registered businesses worldwide, contributing to more than 50 percent of employment globally (World Bank1). In Organization for Economic Cooperation and Development (OECD) member countries, SMEs are the predominant

form of enterprise, accounting for approximately 99 percent of all firms and about 70 percent of jobs on average, and are major contributors to value creation, generating between 50 percent and 60 percent of value added on average (Figure 1).

According to the World Trade Organization², which draws its finding from empirical studies and data sources, and the European Commission, the median GDP contribution of small and medium-sized businesses is 45 percent (55 percent in developed countries, 35 percent in developing countries). SMEs also feature prominently in the UN Sustainable Development Goals, which encourage the growth of these businesses in order to promote inclusive and sustainable growth, full and productive employment, and reputable work for all.

Figure 1: SMEs account for the bulk of employment in the most affected sectors



Source: OECD (2021) SME and Entrepreneurship Outlook (OECD, 2021 [7]) <https://doi.org/10.1787/888934249623>

“ There has been a clear and decisive global shift to trade on open account terms. This shift is led by larger corporations and well accepted by SMEs because of lower costs, less processing time and its enhanced attractiveness to buyers.”¹¹”

Support Needed for SMEs

Most SMEs, including new, innovative and fast-growing firms, remain heavily reliant on internal resources and traditional bank debt. According to a study by the World Trade Organization¹⁰, globally, more than half of the requests made by SMEs for trade finance are rejected, compared to only 7 percent for multinational companies. All of these facts signal the need to support SMEs with solutions beyond the traditional policies and stimulus support that governments and development banks have been providing. This call to action beyond traditional measures is even more essential in today's COVID-shaken world that is being forced to adapt to a “new normal.”

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Supply Chain Finance

Traditional bank-guaranteed trade finance solutions such as letters of credit and guarantees have been used extensively in the past. However, these solutions are criticized because of required tedious and cumbersome administrative processes as well as significant stress on balance sheets.

“ According to the ICC Global Survey, supply chain finance is one of the innovations most likely to change the trade finance industry.”¹²”



Supply Chain Finance

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One of the rising stars in the open account universe is payable supply chain finance, also known as reverse factoring. This solution helps to liberate capital tied in the working capital cycle of buyers and suppliers by enabling suppliers to be paid early while allowing the buyer to maintain, or extend, its payment terms.

A supplier usually has to invest upfront capital to purchase raw materials, manufactured goods and deliver goods to the buyer before receiving the payment at the negotiated payment timing. As we discovered earlier, the state of access and cost of this capital for SME suppliers is inequitable. A payable supply chain finance (SCF) solution helps suppliers gain access to capital – most likely at a much lower rate – without waiting for buyers to make payments on invoices.

An SCF program is established by a buyer for its suppliers with the help of financial institutions and SCF technology

providers. Depending on its own corporate objectives and payment terms benchmarked against market standards, the buyer optimizes its payment terms with suppliers. In order to prevent any negative impact of the new payment terms on its supplier, the buyer makes the approved invoices of the goods and services it purchased available for financing on the SCF platform. The suppliers are then able to “sell” approved invoices of the buyer to the financial institutions partnered by the buyer on the platform. This way, the supplier gets paid right away on the invoices they select on the SCF platform rather than waiting for payment terms to mature. When the invoice comes to its optimized full term, the buyer pays the full amount to the financial institution that now owns the invoice.

The invoices are financed at a discounted rate that is based on the credit risk of the buyer instead of that of the supplier. Generally, this discount rate is much cheaper than what a supplier could get on their own from banks, especially if the supplier is an SME or in a developing market. This is why, even with extended terms, suppliers are more likely to have lesser financing costs than they might have to incur with existing payments and their own credit profile. In addition to payment term optimization, buyers leverage SCF programs to achieve other objectives such as strengthening relationships, supporting suppliers and incentivizing suppliers to support sustainability.

Figure 5: Supply Chain Finance/Reverse Factoring Workflow

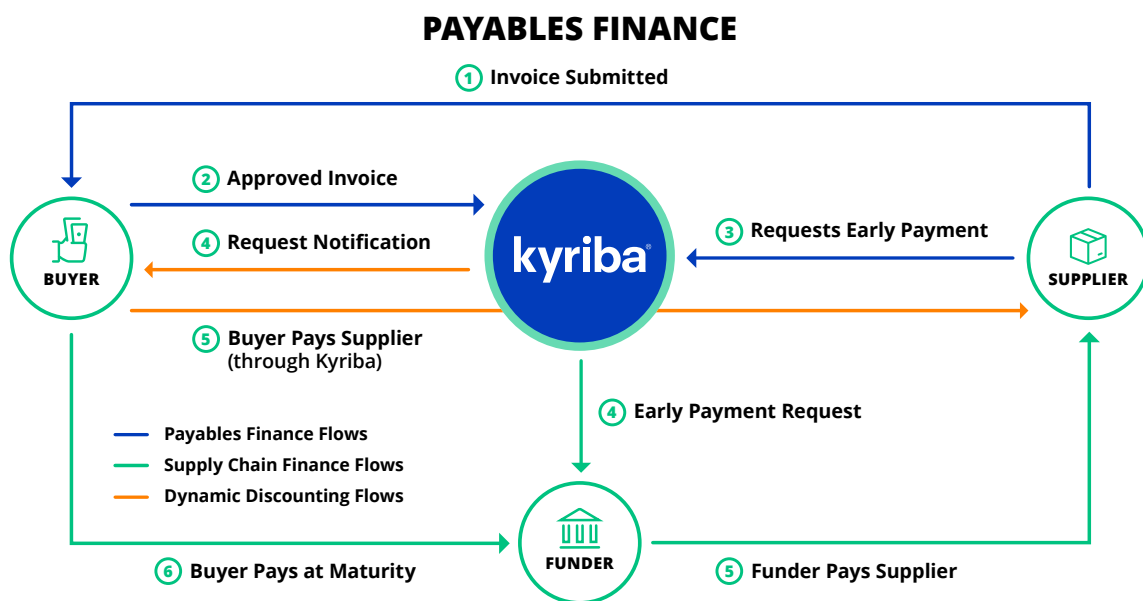





Table 1: Benefits of SCF Program for Buyers, Suppliers and Financial Institutions

 BENEFITS OF SCF PROGRAM FOR BUYERS	 BENEFITS OF SCF PROGRAM FOR SUPPLIERS	 BENEFITS OF SCF PROGRAM FOR FINANCIAL INSTITUTIONS
Increase free cash flow (increase DPO)	Increase free cash flow (decrease DSO) through early payment	Establish new revenue streams
Improve critical supplier relationships	Access to a new source of financing	Build new relationships with suppliers
Achieve “preferred buyer status”	Reduce financing costs (most relevant for SME suppliers with higher credit risk than the buyer)	Enhance relationship with buyer enterprises
Provide financial incentive for sustainability/responsible sourcing	Receive financial incentives for sustainability/responsible sourcing	Expand “green financing” portfolio
Enhance cash visibility/predictability	Enhance cash visibility/predictability	Enhance relationships with existing clients
Reduce accounts payable inquiries	Receive remittance information at no cost with reduced accounts receivable queries	
Reward bank relationships		



How Development Banks and Governments Can Leverage SCF for SME Growth

Supply chain finance has been stirring up significant attention globally as the innovative solution to facilitate access to credit and financing for SMEs. A study by the WTO on SMEs and Finance¹², stressed SCF as a pioneering approach for “bridging the huge financing gap for SMEs.”

A few key reasons for such endorsements are:

The Benefit from SCF Multiplier Effect:

SCF programs can provide financing to a vast number of SMEs through a handful of large corporations (Figure 6). This contrasts with other traditional methods such as granting loans, guarantees and traditional receivable factoring that require governments and banks to mobilize a large amount of resources to reach or process SMEs one by one. This method capitalizes on economies of scale that large corporations and supply chains can offer.

The Ability to Mitigate High SME Credit-Risk:

SCF provides financing to SMEs without injecting high credit risk into financial systems, since the programs carry a lower risk of larger buyer corporations' defaults. SCF programs present a "win" opportunity for funding entities too, not just for large buyers or SME suppliers (Table 1). Strengthening existing relationships with large corporate customers and penetrating the huge SME market without taking SME risks onto the books are big wins. This arrangement makes it easier to attract private financial institution funding instead of solely utilizing public funds. Even without private financial institutions, at the very least, it offers a self-sustaining financing model that development banks usually struggle with.

Offering a Lower Cost of Financing:

SCF is not just another, more-accessible source of financing for SMEs, but it is also much cheaper when compared to other available options that are based on their own credit profile such as direct loans, guarantees and traditional receivable factoring programs.

These characteristics make SCF programs powerful and efficient tools for development banks and governments to support SMEs – and thereby the overall economy – by alleviating the major barrier of a lack of finance and instead providing more agreeable finance.

The domino effect of this attractive alternative source of financing would help both public procurement entities to also attract more bids from SMEs, contribute toward local employment labor quotas and increase overall quality and bidders that could drive down the overall cost of tenders. Additionally, development banks can better fulfill their mission of empowering SMEs and create more employment, more wealth and more sustainable development.

In addition to the prominent financial benefits, the digital nature of SCF platforms provided by fintechs, such as Kyriba, offer multiple spill-over benefits. The digital setup provides much-needed visibility and auditing capabilities that development banks and governments often lack.

Figure 6: The SCF Multiplier Effect

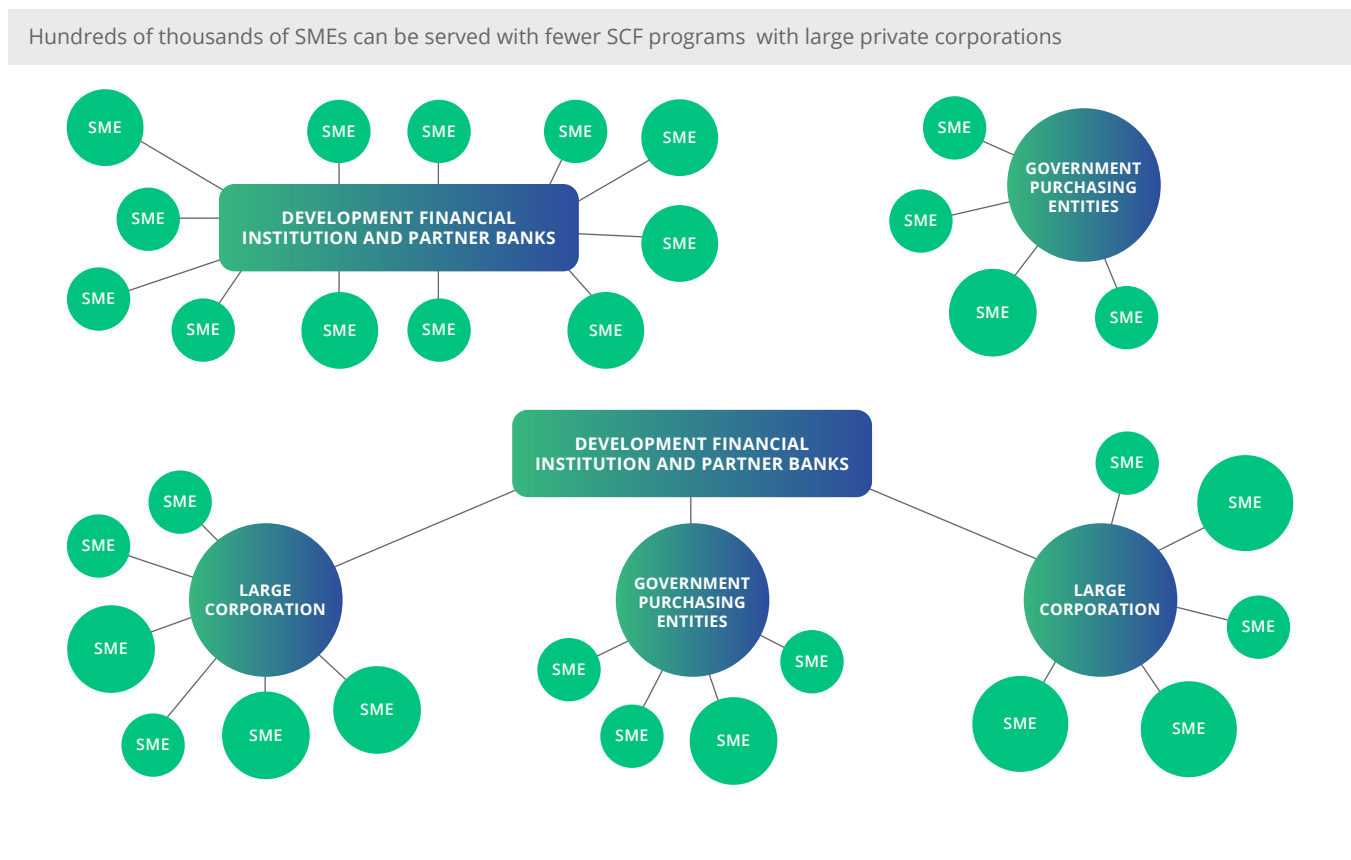


Table 2: How Supply Chain Finance programs help Development Banks and Governments

DEVELOPMENT BANKS	GOVERNMENTS
<ul style="list-style-type: none"> • Empower SMEs by providing an alternate lower cost of financing source • Inject transparency and traceability in the usage of funds • Support other sustainability objectives, such as countering climate change, by providing financial incentive to SMEs 	<ul style="list-style-type: none"> • Increase competition on public procurement contract bidding • Inject transparency and traceability in the usage of funds • Contribute toward local business/labor quotas • Increase the quality of the bidder pool • Supplement other initiatives, such as digitization, eco-sustainability and accelerating payments for SMEs

Exhibiting such capabilities can even put them on the front lines of securing funding from other international multilateral institutions such as the World Bank Group, IMF and IBRD.

From a wider strategic point of view, SCF programs should not be viewed as separate stand-alone projects. Governments can couple SCF programs with their other initiatives that have been or are going to be undertaken toward digitization and reduction of payment delays. More than 55 countries worldwide have or are considering e-invoicing mandates, including Germany, the Netherlands, India, Brazil, China, Greece, Indonesia, Italy and Romania.

Even though the major driving factor for increasing e-invoicing mandates is indirect tax compliance (VAT/ GST), digitizing the billing processes opens up new opportunities including benefiting from SCF programs on state-of-the-art digital platforms, such as that of Kyriba. Likewise, legislation to fight delayed payments practices has been on the rise. Delayed payments have become common practice in the private sector



and public procurement. These delays can hamper SMEs significantly by exacerbating their need to access finance. Strong negative impacts of such increasing delayed payments on SMEs’ financial health have made governments around the world pass various bills and policies such as the U.S. Prompt Payment Act (PPA), European Late Payment Directives and Section 15 of the MSME Development Act in India. In spite of some governments enacting these policies, SMEs’ struggles with late payments continue. SCF programs provide an alternative way to address this difficult conundrum of late payments. Unlike these measures, an SCF program does not impose the financial stress of short-payment terms on buying entities to provide faster payments to SME suppliers, and thus carries less resistance from them. This enables both players to thrive without getting into a cash flow tug-of-war that harms the overall economy.

This fascinating remedy hasn’t gone entirely unnoticed by the public sector. Many governments and development banks have tested this theory with phenomenal practical results.

The Netherlands

The Dutch Ministry for Economic Affairs supports and subsidizes “Betaalme.nu” (‘Pay Me Now’). It is a nonprofit initiative established in 2015 that has been joined by 63 large companies and institutions to draw timely payment manifestos for their suppliers leveraging SCF programs. It claims to help about 283,000 SMEs by affecting early payment of more than €2Bn worth of invoices.

The U.K.

The U.K. government also attempted to tap into SCF potential to boost the economy by convincing large corporations such as Boeing, Carillion, Dell, Rolls-Royce and Kingfisher to evaluate the implementation of SCF programs for their suppliers. While some organizations kept their promise and deployed successful SCF programs, such as Boeing and Siemens, others either exploited these programs in a wrongful manner or didn’t keep their promise of implementation.

Mexico

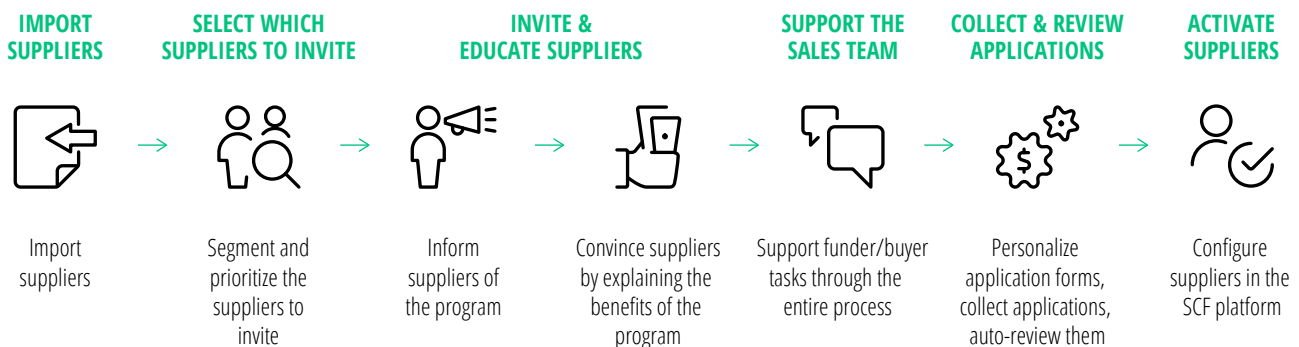
Nacional Financiera (NAFIN), a Mexican development bank, launched its own online reverse factoring (supply chain finance) program that has extended more than \$9 billion in financing and brokered more than 1.2 million transactions, 98 percent of which have come from SMEs, since its inception.



NAFIN has also created a similar online program for government purchases to not only improve access to finance for SMEs that are government suppliers but also to increase transparency and efficiency in payments made by government entities and enable greater participation by SMEs in public sector purchases. This program covered 268 government agencies in 2015 and provided financing to 6,647 government suppliers for a total of \$5.6 billion, accounting for about 42 percent of total financing provided through NAFIN’s online factoring transactions.

Figure 7: Kyriba Supplier Onboarding Suite

Management of the Entire Onboarding Cycle



World Bank Group/IFC-sponsored

As part of its Global Trade Supplier Finance initiative, the International Finance Corporation (IFC) has successfully launched SCF programs in 14 countries amounting to about \$3 billion to nearly 1,000 suppliers.

Kyriba works with governments and development banks around the world to establish financial channels, enable access to capital and instill active liquidity management through its solutions, including supply chain finance. The core solution is supplemented with a state-of-the-art supplier onboarding product suite (Figure 7) that streamlines the tedious process of onboarding thousands of suppliers, enabling outreach to SMEs, not just a handful of selective suppliers targeted by traditional supply chain finance programs.

Such advanced technology solutions put Kyriba at the forefront of being able to help governments and development banks in supporting small and medium-sized businesses for truly inclusive economic sustenance and growth.

As has already been well-documented and empirically demonstrated through extensive research and modeling, SMEs hold the key to sustainable economic growth. In good times, they fuel economic expansion, and in crises, they are disproportionately impacted. In fact, their survival rate decreases dramatically in periods of prolonged economic downturn, as we have been witnessing with the COVID-19 global pandemic. Given this duality of forces, as growth engines during expansions and facing decreased survival rates in recessions, finding innovative solutions to shoring up this segment in the economy is not only desirable, but also mandatory. One of these innovative solutions is supply chain finance. Supply chain finance, leveraging digital capabilities to seamlessly integrate buyers, sellers and funders, is a real opportunity to help SMEs improve their survival odds while establishing the foundation for a strong and accelerated recovery.



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About Kyriba Corp.

Kyriba empowers CFOs, Treasurers, and their IT counterparts to transform how they optimize financial technology solutions, de-risk ERP cloud migration, and activate liquidity as a dynamic, real-time vehicle for growth and value creation. With over 2,500 clients worldwide, including 25% of Fortune 500 and Eurostoxx 50 companies, Kyriba's pioneering Connectivity as a Service platform integrates internal applications for treasury, risk, payments and working capital with vital external sources such as banks, ERPs, trading platforms, and market data providers. Kyriba is a secure, scalable SaaS platform that leverages artificial intelligence, automates payments workflows, and enables thousands of multinational corporations and banks to maximize growth opportunities, protect against loss from fraud and financial risk, and reduce operational costs. Kyriba is headquartered in San Diego, with offices in Dubai, Frankfurt, London, Minsk, Paris, Shanghai, Singapore, Tokyo, Warsaw and other major locations. For more information, visit www.kyriba.com.