



Supply Chain Finance (V)

Supply Chain Finance Management of *Commercial Bank*

The Li & Fung Management Book Series

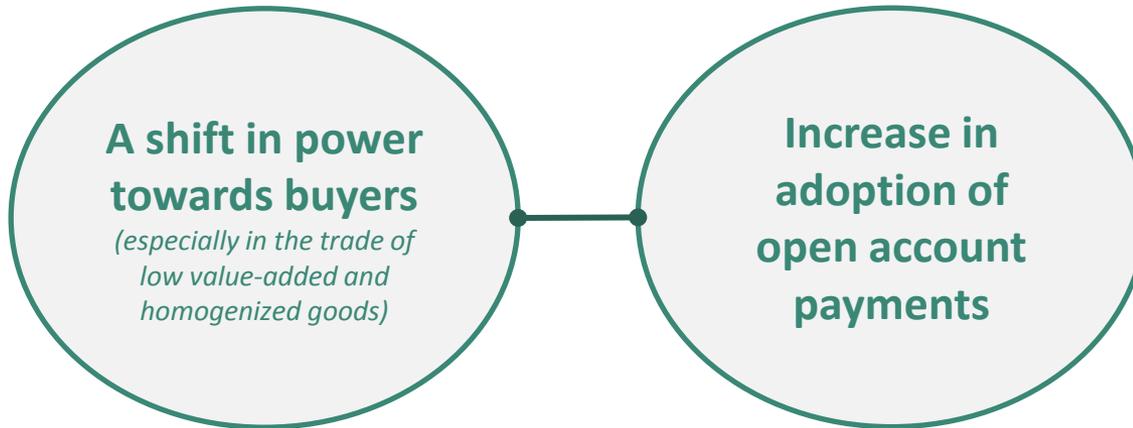
Winnie Lo, Howard Hung

Management Theories and Business Models

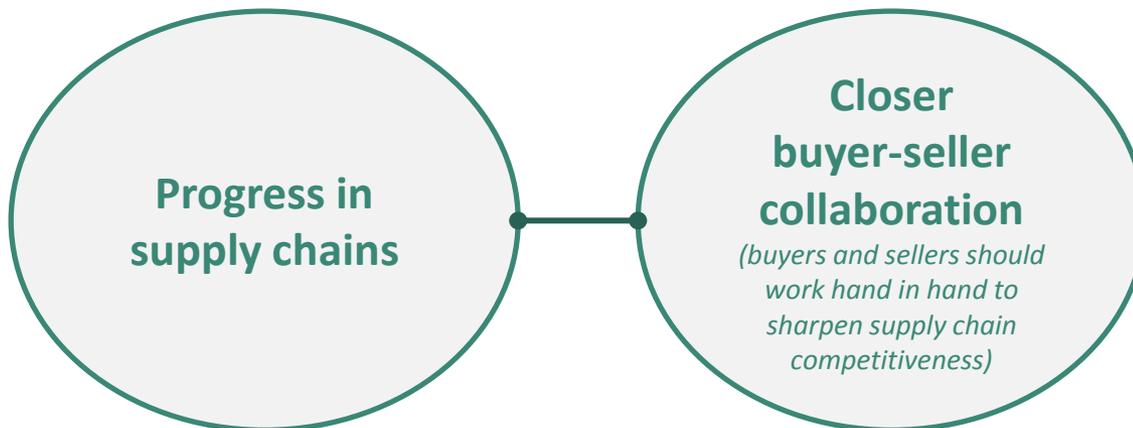
August 2016

Transformation of international trade

Trend 1

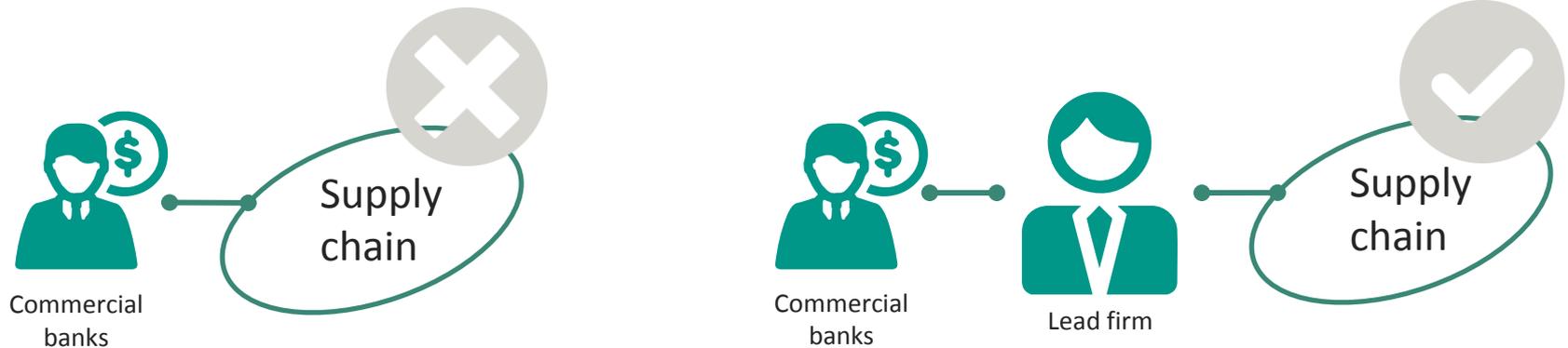


Trend 2



1. Previous financial products that address only a particular supply chain process could no longer satisfy market demand.
2. An increasing number of international commercial banks are developing “end-to-end” financial solutions covering the entire supply chain.

Commercial banks & supply chain



- Commercial banks do not participate directly in actual supply chain operations
- The shortcut for commercial banks in supply chain finance is to identify the lead firms in supply chains, and gain more in-depth information about supply chain transactions through cooperation with the lead firms.
- Lead firms serve as the anchor customers in the entire supply chain flow; commercial banks provide supply chain finance solutions based on the credit rating of lead firms, as well as the future cash flows generated from actual supply chain transactions.

Trade finance vs. supply chain finance

Commercial banks' supply chain finance shares a number of similarities with their trade financing

1. It integrates commercial banks' asset-based services and intermediary services.

Asset-based services

- Accounts receivable financing
- Factoring
- Accounts receivable pool factoring
- Negotiable instruments pool financing
- Advance payment discount
- Inventory financing
- Warehouse receipt financing
- Export credit insurance financing
- Prepayment financing
- Financing by pledging the rights of future goods

Intermediary services

- Accounts receivable collection
- Credit reference
- Financial management consulting
- Cash management
- Settlement
- Loan guarantee
- Remittance
- Currency exchange

2. Supply chain finance emphasizes the actual transactions between supply chain upstream and downstream players, instead of merely looking at the financial statuses of individual players.

3. Financing is mainly based on inventory, accounts receivable and prepayment.

Trade finance vs. supply chain finance

Some differences between commercial banks' supply chain finance model and trade finance model



Trade finance model

<ul style="list-style-type: none"> • Letter of Credit 	The most common settlement method	<ul style="list-style-type: none"> • Open account
<ul style="list-style-type: none"> • Loose in risk control 	Risk control level	<ul style="list-style-type: none"> • More stringent risk control <i>This model takes into account the stability of cooperation between upstream & downstream players</i>
<ul style="list-style-type: none"> • Generally led by commercial banks <i>Commercial banks need to evaluate each deal</i> 	Role of commercial bank	<ul style="list-style-type: none"> • Commercial banks offer collaborate with logistics and insurance companies to provide services
<ul style="list-style-type: none"> • Single trade process 	Coverage	<ul style="list-style-type: none"> • 'End-to-end' financial solutions covering the production, supply & sales processes
<ul style="list-style-type: none"> • Partial information about the supply chain operations 	Information	<ul style="list-style-type: none"> • Obtain comprehensive information about the supply chain processes



Supply chain finance model

Commercial banks & supply chain finance

- Supply chain finance helps ease the financial pressure on small- and medium-sized enterprises (SMEs) posed by credit rationing
 - Factors such as industry, company size, fixed assets, financial indicators and guarantee method are no longer the emphases in credit evaluation of the debtors' (mostly SMEs)
 - Instead, commercial banks evaluate the continuity of trade transactions and the credit ratings of lead firms
 - Commercial banks focus on the overall financial health of the supply chain
 - The loans must be self-liquidating in nature and debtors must not use the funds for other purposes

- SME is granted better credit ratings in general, compared with getting funds via traditional credit evaluation methods



Commercial banks protect their respective interests through the establishment of operational control and repayment guarantee measures



Commercial banks & supply chain finance

Chinese commercial banks that have actively launched supply chain finance services include:



2 dimensions of supply chain finance innovation of commercial banks



1

Cross-industry penetration and data integration

- Refers to the capabilities of commercial banks:
 - To integrate the database of logistics companies, debtors, upstream, downstream enterprises and the customs
 - To reduce information asymmetry and the problem of credit rationing



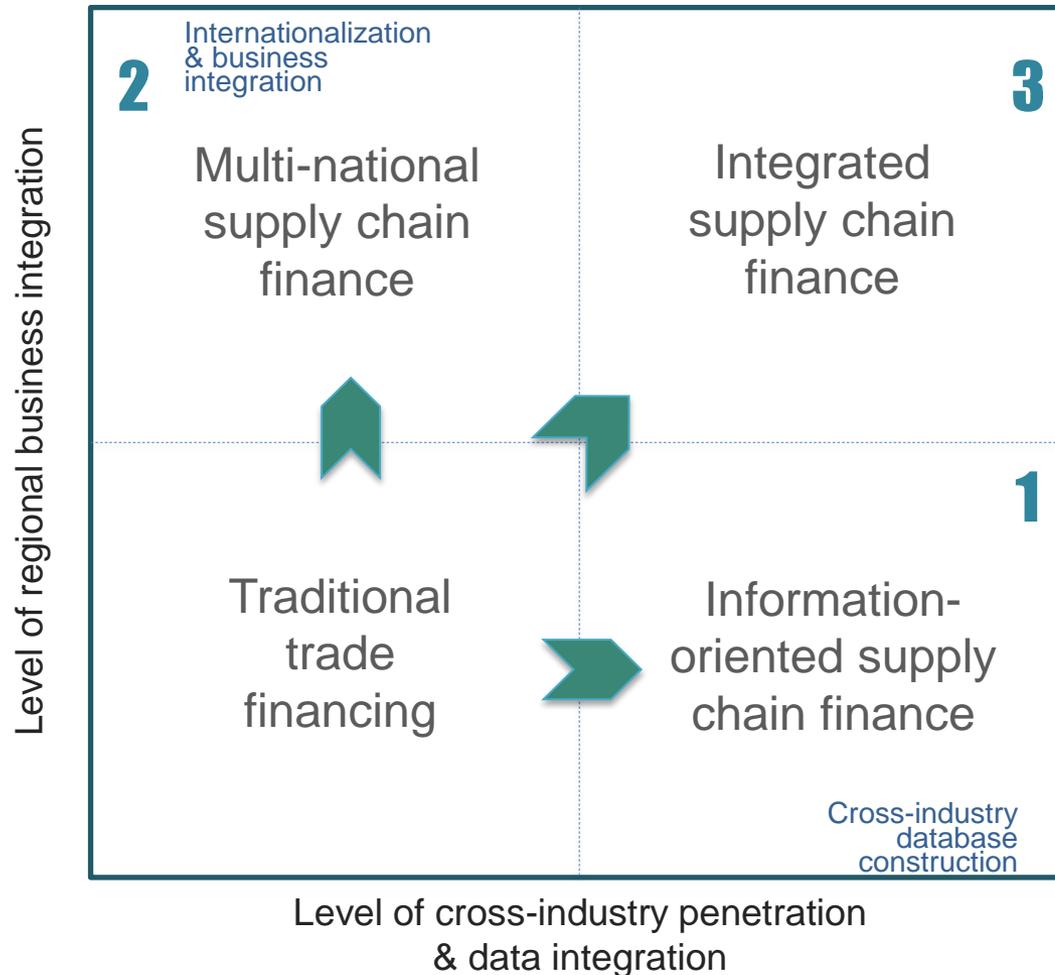
2

Regional business integration

- Refers to the capabilities of commercial banks:
 - To lower the transaction cost of customers by providing integrated regional service
 - To achieve economies of scale and economies of scope through regional integration

3 supply chain finance models of commercial banks

- based on the 2 dimensions



3 supply chain finance models of commercial banks

1 Information-oriented supply chain finance

2 Multi-national supply chain finance

3 Integrated supply chain finance

Service models

- Relatively basic
- Solutions provided through the provision of cross-industry data

- A high degree of business integration
- Not provide with much information of transactional processes

- Offer both multi-national business support and in-depth information of transactional processes

Risk control mechanisms

- Access to customers' operational data
- Able to control risk through customer screening and information control

- Guarantees repayment through income generated by a/c receivable, inventory, L/C, etc.

- Incorporate risk control measures of the other 2 models

Capabilities required

- Have to possess strong ability to connect with customers' information system

- Have to possess strong internationalization and business integration capabilities
- Able to break down organization silos within the company

- Have to possess a combination of capabilities of the other 2 models
- Need to work closely with customers for a tailor-made solution

Ping An Bank



- Ping An Bank is the first joint-stock commercial bank listed in China
- Headquartered in Shenzhen
- It has 528 banking outlets under 38 branches throughout the nation, a representative office in Hong Kong and over 2,000 overseas banks, by the end of 2013
- Total assets of the bank amounted to ¥ 1.89 trillion, its deposit balance and loan balance (including discounted bills) totaled ¥ 1,217.2 billion and ¥ 847.3 billion in 2013, respectively
- Ping An Bank achieved a net profit of RMB 15.2 billion in 2013

Ping An Bank's online supply chain finance service platform

(Ping An SCF platform)

- Its information system is the backbone of its information-oriented supply chain finance service.
- The bank has launched an online supply chain finance service platform to connect its stakeholders, such as customers, 3PLs, B2B platform providers, the Customs, the State Administration of Taxation, and State Administration of Foreign Exchange.
- Currently, the service platform has over 2,000 users, of which, more than 100 users are lead firms in supply chains.

5 edges of Ping An Bank's online supply chain finance service



Ping An SCF platform connects to the information systems of lead firms, their upstream and downstream partners, as well as logistics companies, and so forth, to enable efficient data exchange, allow customer authentication and submit electronic data.



Ping An Bank works closely with financial software developers to design financial management software that caters to the needs of SMEs in supply chains and to achieve seamless connection between enterprises and itself.

Financial software
developers



Ping An SCF platform operates an “end-to-end” service model; services include supplier financing, prepayment financing for downstream distributors, inventory financing, consumer loans, etc.



Ping An SCF platform is able to connect seamlessly with customers from a wide range of industries.



Ping An SCF platform uses a standard system of commodity codes that can easily identify different types of goods. Ping An also collaborates with leading logistics companies in China as an industry standard setter by incorporating the latter into its system.

Citibank

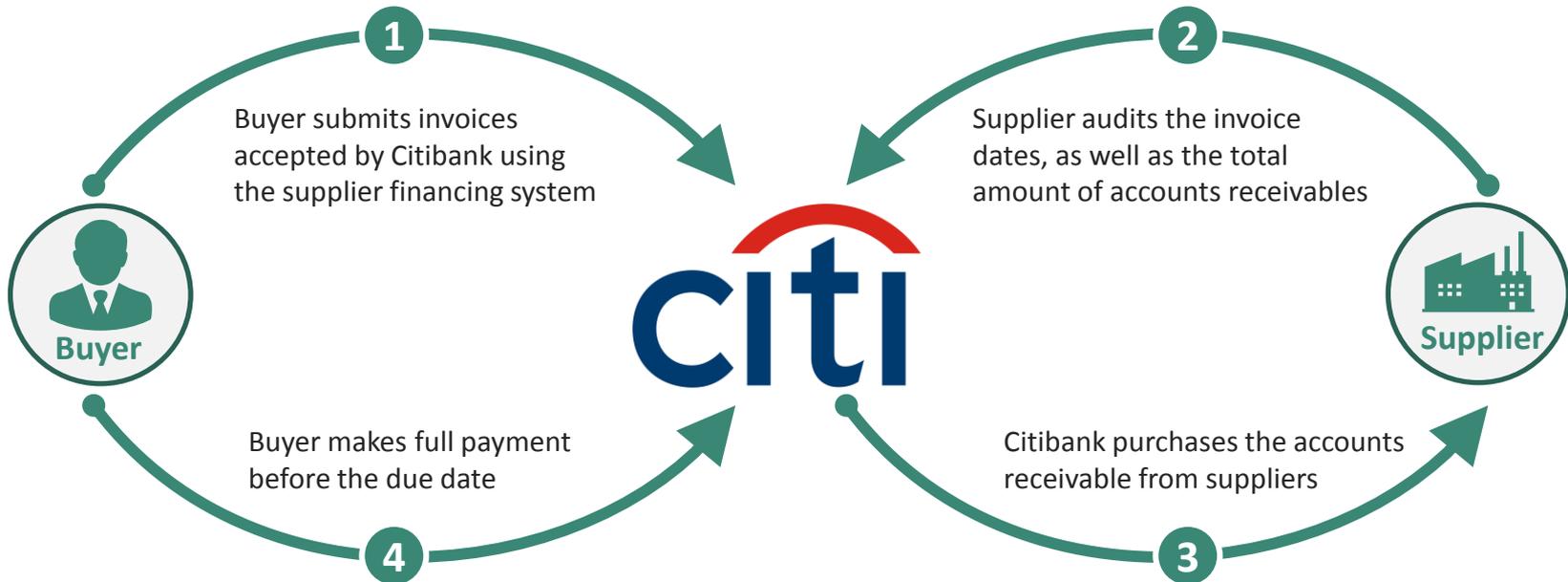


- Founded in 1812
- Citibank has branch locations in around 150 countries and regions
- Citibank is a leading multi-national supply chain finance service provider

Citibank's supplier financing system

- Citibank has found that traditional customer-supplier relationships can no longer guarantee supply chain stability in turbulent economic times
- Many of Citibank's clients concern about the stability of upstream suppliers
- Indeed, effective interactions between upstream and downstream supply chain players can boost supply chain performance
- The higher the buyers' participation in supplier activities and decisions, the better the supply chain performance
- The most challenging problem facing the upstream suppliers of Citibank's clients is the huge working capital tie-up, owing to long accounts receivable collection period. Thus, Citibank establishes a "supplier financing system"

Citibank's supplier financing system



- The supplier financing system of Citibank helps the clients ease the financial pressure of their suppliers
- The ultimate goal of the system is to optimize overall supply chain operations and enhance supply chain flexibility

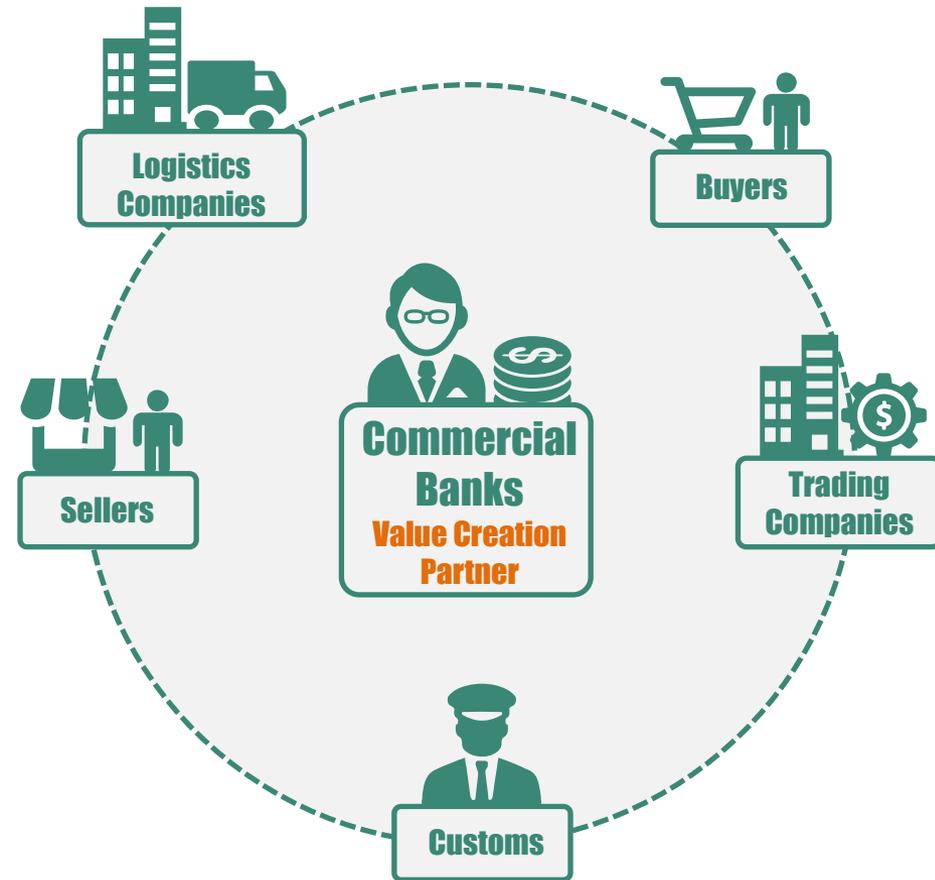
HSBC



- Established in Hong Kong in 1864
 - In the 1980s, HSBC expanded and became a global bank by seizing the the golden opportunities:
 - Financial liberalization
 - Economic integration in Europe, and
 - The banking crisis in the United Kingdom in 1980
 - Today, HSBC has 9,500 branches in 85 countries and regions globally
-
- From the viewpoints' of HSBC, the international trade landscape is now undergoing profound changes:
 - Companies today prefer sourcing or importing directly from other countries, especially developing economies. To secure supply, they recognize the importance of maintaining a closer collaboration with upstream players. They are also putting forward more stringent requirements for their suppliers in terms of financial health and compliance.
 - Open Account has replaced Letter of Credit to become the most popular settlement method in international trade, as it reduces working capital tie-up and shorten document processing time.
 - More companies are outsourcing their non-core operations. Many are also seeking to improve supply chain efficiency and cash turnover with the use of information technology.
 - Today, many traditional financial products can no longer fully satisfy market demand. To accommodate changing market needs, HSBC customizes different solutions for its customers, including document process services, accounts receivable discounting, etc.

Model 3: Integrated supply chain finance

- Today, operating an integrated supply chain finance model is a major development direction for big international banks, which offer information-oriented multinational supply chain finance service:
 - Extracting key transactional data through integration of multiple stakeholder databases to achieve full control of the end-to-end supply chain process and better manage risk
 - Helping stakeholders to integrate their funds flow, logistics flow, and business flow
- Commercial Banks serve as a value creation partner of their clients.



JPMorgan Chase

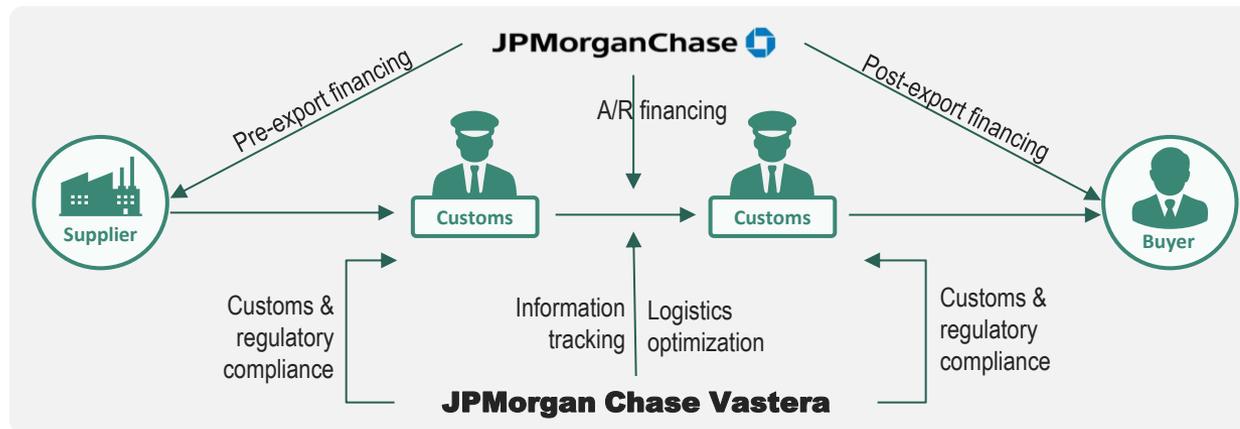


JPMorganChase

- Established in 1968, JPMorgan Chase is a multinational financial institution headquartered in New York
- It is one of the largest banks in the U.S. and operates in more than 60 countries across the world

JPMorgan Chase Vastera

- In 2005, JPMorgan Chase acquired Vastera, a customs clearance and logistics software provider to form JPMorgan Chase Vastera and established a new logistics team in Asia that specialized in offering financial service support for supply chain and agency sales businesses
- Service framework:



- In addition to traditional and structured trade finance solutions, JP Morgan also provides global supply chain management service to its customers in China to facilitate cross-border trade flow, billing, and supplier financing. The waybill audit service is supported by Vastera.
- In 2012, JPMorgan Chase sold off Vastera to Livingston International and the latter is now providing all operations previously conducted by Vastera.

REPORT SERIES

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- 2 Supply chain finance innovations in manufacturing industry [Please click [Here](#)]
- 3 Supply chain finance innovations in trade and distribution industry [Please click [Here](#)]
- 4 Supply Chain Finance Innovation in the Logistics Industry [Please click [Here](#)]
- 5 This series
- 6 Supply chain finance innovations in e-business

Source

This report is based on the book “Supply Chain Finance”, written by Prof. Song Hua.



Song Hua is a Professor of supply chain management at the School of Business, Renmin University of China. He is also a market research and regulative expert at the Ministry of Commerce, the Assistant Secretary General of the Chinese Society for Management Modernization, and the Chairman of the Beijing Modern Institute of Enterprises Research. His main research interests include service supply chain, inter-firm relationships, and supply chain flexibility.

Prof. Song has published over 60 papers in refereed conferences and journals including Asia-Pacific Journal of Management, Transportation Journal, Decision Sciences, International Journal of Operations and Production Management and Chinese Management Studies.



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