SUPPLY CHAIN FINANCE FUNDAMENTALS FOR FOOD & BEVERAGE:

What it Is, What it's Not and How it Works

PrimeRevenue

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The last several years have brought seismic shifts to the food and beverage industries. These changes have caused many companies to rethink virtually every aspect of their business – from production and operations to product portfolio and innovation. In a world where entire aisles of the grocery store are threatened by obsolescence, the pressure is on for food and beverage companies to respond with agility and acuity.

Some of the most formidable challenges facing food and beverage companies include:

Changing consumer preferences. Consumer demand has shifted away from processed food and drink to more organic and health-conscious products. Many mainstream brands have seen a decline as niche brands grow in popularity.

Rampant market consolidation: M&A activity continues to be strong across the food and beverage sector. From Danone SA's $12.5B acquisition of organic food producer WhiteWave to the six large-scale acquisitions announced by Anheuser-Busch Companies in 2016, the volume and significance of these acquisitions continues to grow.

Shrinking profit margins: Many companies are feeling the pressure of rising raw material and production costs. Unable to absorb this increase, some have been forced to adjust pricing and/or scale back products. One example is Pringles, which decreased the diameter of its chips and announced a 9.3 percent price increase in 2016.

These challenges have upended business as usual across the food and beverage industries. Many companies are under pressure to reinvent – either through rebranding and product innovation or by securing footing in new markets/sectors through acquisition. The trickle-down effect on suppliers can be equally disruptive as some suppliers find themselves on the losing end of changing consumer tastes or the supply chain politics of a major merger or acquisition.

To respond to these challenges with speed and agility, food and beverage companies need to improve cash flow. Historically, this has required companies to take on additional debt through commercial-based lending. But what happens when the funding required for a major growth or repositioning initiative amounts to hundreds of millions (or billions) of dollars? What if adding extra debt isn't a viable solution?

Enter supply chain finance. The largest food and beverage companies have been using it for years to improve cash flow without negatively impacting balance sheets. Food giant Conagra used supply chain finance to unlock more than $260 million in its supply chain during its 2017 fiscal year, which helped contribute to an 81 percent increase in the company's net cash flow from operating activities.[1] Meanwhile, coffee provider Keurig Green Mountain credits working capital improvements as being instrumental in helping the pay down nearly $1 billion in debt.[2]

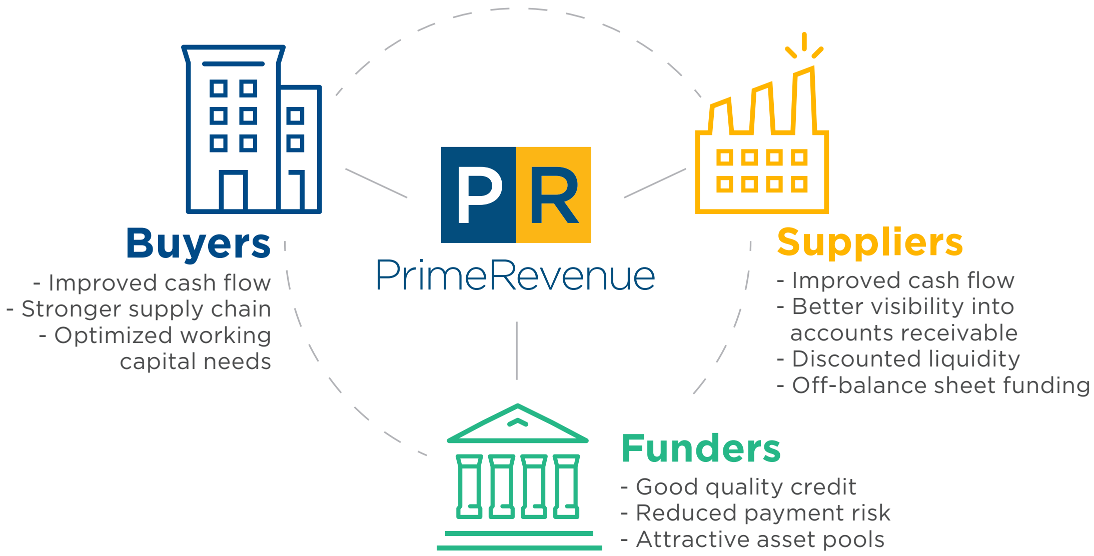
But what exactly is supply chain finance? What is it not? And how does it work?

What is supply chain finance?

The objective of supply chain finance is to unlock working capital trapped in the supply chain –in a manner that benefits all parties involved.

[1]Source: *The Wall Street Journal* [2]Source: *S & P Global*

Understanding the Supply Chain Finance Ecosystem



To operate effectively, supply chain finance requires an ecosystem that improves the velocity of working capital across a supply chain. Participants in the ecosystem are as follows:

Buyers: Typically large organizations that rely on a multitude of supplier-provided goods and services to deliver products for their customers. Buyers often operate on a global basis.

Suppliers: Companies that supply goods and services to buyers in the supply chain ecosystem. Some suppliers are large enough to also operate as buyers thereby having their own suppliers, complex supply chains and the same need to optimize cash flow.

Funders: Bank and non-bank sources of investment capital that advance funds to cover the cost of approved supplier invoices.

Platform providers: Technology solution providers that facilitate the supply chain finance ecosystem and program management. Today, leading platforms are cloud-enabled, meaning they do not require installation and operation of specialty software systems.

Supply Chain Finance Defined

Supply chain finance -- also known as supplier finance or reverse factoring -- is a set of solutions that optimizes cash flow by allowing buyers to extend supplier payment terms. Increasing the time it takes to pay a supplier improves several financial metrics (e.g. days payable outstanding or DPO), and most importantly, frees cash that would otherwise be trapped inside the supply chain. A buyer can use increased cash flow to invest in operational, competitive and innovation initiatives that will drive additional growth. They can also return cash to shareholders in the form of dividends or stock repurchases.

Simultaneously, supply chain finance offers suppliers a way to mitigate the effect of payment term extensions and to accelerate their own cash flow. Suppliers who participate in a program have the option to get paid early – typically as soon as an invoice has been approved by a buyer. The supplier can accelerate payment on some, all or none of their receivables, depending on their financial position and funding requirements. For those receivables that are paid early, the supplier will pay a small finance charge or discount.

All of this occurs without negatively impacting the balance sheets of either company. Accounting treatment for supply chain finance, when done properly, does not count as additional debt for a buyer or supplier.

Furthermore, since the buyer is the obligated party, financing is offered to the supplier at rates that are typically more favorable because they are based on the buyer's credit history and rating. For many suppliers, this access to a lower cost of funding is exceptionally important.

Supply chain finance thus creates a win-win situation for both buyers and their suppliers. The buyer optimizes working capital because it has more time to pay suppliers. Meanwhile, suppliers can generate additional operating cash flow by getting paid early without affecting their balance sheets.

When it comes to optimizing cash flow, supply chain finance is a rare win-win scenario for both buyers and suppliers in the food and beverage industries. It's a way to unlock working capital for both parties without having a negative impact on either entity's balance sheet.

What Supply Chain Finance is Not

The world of trade finance is complex and varied. There are numerous ways to increase business capital on hand and, in many cases, the differences are slightly nuanced. Given this landscape, it's not just important to understand what supply chain finance is; it's also important to understand what it is not.

It is not a loan. Supply chain finance is an extension of the buyer's accounts payable and is not considered financial debt. For the supplier, it represents a non-recourse, true sale of receivables. There is no lending on either side of the buyer/supplier equation, which means there is no impact to balance sheets.

It is not dynamic discounting or an early payment program. Early payment programs, such as dynamic discounting, are buyer-initiated programs where buyers offer suppliers earlier payments in return for discounts on their invoices. Unlike supply chain finance, buyers are seeking to lower their cost of goods, not to improve their cash flow. Dynamic discounting and early payment programs often turn out to be expensive for both suppliers (who are getting paid less than agreed upon) and buyers who tie up their own cash to fund the programs.

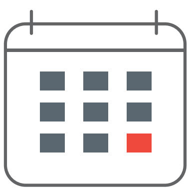
It is not factoring. Factoring enables a supplier to sell its invoices to a factoring agent (in most cases, a financial institution) in return for earlier, but partial, payment. Suppliers initiate the arrangement without the buyer's involvement. Thus factoring is typically much more expensive than buyer-initiated supply chain finance. Also, suppliers trade "all or nothing" meaning they have no choice to participate from month-to-month to the degree that their cash flow needs dictate. Finally, most factoring program are recourse loans, meaning if a supplier has received payment against invoices that the buyer subsequently does not pay, the lender has recourse to claw back the funds.

SUPPLY CHAIN FINANCE:
How it works

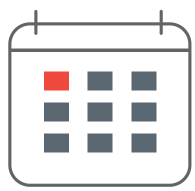
Supply chain finance employs two primary tactics. The first is the extension of supplier payment terms. In this tactic, the buyer extends payment terms with all of its suppliers – for example, from 60 to 120 days. This dramatic slowdown of cash outflow gives the buyer access to more working capital.

The second tactic in supply chain finance is a counterbalance to the first. The buyer gives selected suppliers the option to get paid early by selling their invoices to financial institutions (or funders). This offsets the negative impact of longer payment terms on suppliers, while still enabling the buyer to meet its cash flow optimization objectives.

Two primary methods:



Buyer extends payment terms with all suppliers



Suppliers get paid early by selling their invoices

Invoice selling (or trading) is facilitated through a buyer-side implementation of a supply chain finance platform and program. In this program, buyers identify and invite target suppliers to participate in the program (usually based on the size of spend and/or the strategic value of the supplier). Once a supplier accepts the invitation, they are onboarded into the program and its procurement/sourcing teams are trained on how to use the processes and tools that will facilitate invoice trading. They are also matched to a funding partner or financial institution.

It's important to note the critical role of a strong onboarding program and the availability of multiple funding sources in this process. The onboarding process should be efficient, simple and immediately beneficial to the supplier. Furthermore, access to multiple financial institutions ensures the supply chain finance program is always well funded and suppliers are partnered with a source that understands the geographical, regional and/or industry nuances of their business.

PrimeRevenue Supply Chain Finance In Action

BARRY CALLEBAUT

As the world's largest producer of cocoa and chocolate and $6 billion in annual sales, the **Barry Callebaut Group** is a supplier to the biggest names in the food industry – including Kellogg's, The Hershey Company, Mars, General Mills and Nestle.

Thanks to PrimeRevenue, Barry Callebaut is able to easily accelerate cash flow from one of its largest customers – while enjoying the flexibility of working with a funder it already knows. To date, they have traded over $108M in invoices and receive payment an average of 105 days early.

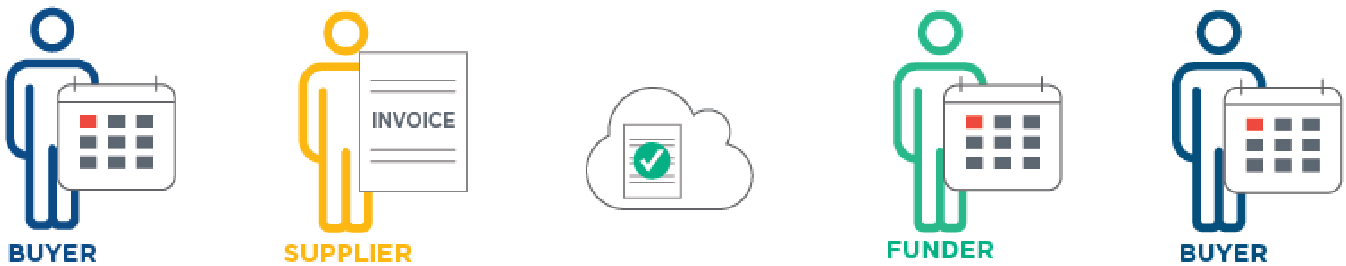
$1B

How do you find $1 billion in working capital during an industry-wide recession? For **one global food company**, the answer is supply chain finance.

In one segment of the food industry, category sales had experienced a 30 percent decline over the last 15 years. The company recognized the need to make large-scale changes to their business strategy, but needed cash to execute. The implementation of PrimeRevenue's supply chain finance solution allowed them to free up $1 billion in cash flow. Today, the company is using this capital to fund a $300+ million innovation initiative that will help the business diversify and thrive.

THE SUPPLY CHAIN FINANCE PROCESS

Following onboarding, it boils down to these five simple steps:



1. Extend payment terms
2. Invoice as usual
3. Approved invoices available for early payment
4. Supplier gets paid
5. When invoice matures, buyer pays either funder or supplier

THE BENEFITS OF SUPPLY CHAIN FINANCE

Supply chain finance is one of the few financial health improvement tactics that works for organizations on both sides of the supply chain. Buying organizations can extend their payment terms, and suppliers can get paid earlier. It's a true win-win solution for both trading partners.

A meaningful increase in working capital can be transformative for today's global food and beverage companies, many of which operate with thin margins. Whereas conventional finance tactics may yield $15M in added cash flow, supply chain finance yields an average of $200M or more for large, multinational buyers. Furthermore, suppliers also realize substantial gains in cash flow as they now have the option to get paid early on each invoice they submit to the buyer.

This translates into much-needed agility for companies in the food and beverage industries. This working capital can be used by both buyers and suppliers to fund new product development or rebranding/repositioning initiatives as well as strategic acquisitions. Money that has traditionally been tied up in accounts payable/receivable can now be used to generate income and strategic advantage in the marketplace.

Supply chain finance also strengthens supplier health and relationships. Not only does it minimize or negate the impact of extended payment terms, suppliers can receive near-immediate payment for invoices at an interest rate often many times lower than other financing approaches. This increase in cash flow can protect suppliers which are often more vulnerable to marketplace dynamics.

Forward-thinking food and beverage companies are using supply chain finance to overcome the challenges of today's business climate. By unlocking cash trapped inside of their supply chains, these companies are rising above the competition and positioning themselves for long-term growth and stability.

PrimeRevenue Supply Chain Finance In Action

The footprint of one of the world's largest brewing companies isn't just big – it's astounding. In fact, it's been estimated that 140,000 bottles of its beer are sold every minute in more than 80 countries.

When the company's bank decided to exit the Central and East Europe (CEE) markets – a region where the majority of the company's suppliers were located – the company turned to PrimeRevenue as its new supply chain finance partner. In the first 90 days, PrimeRevenue and the company onboarded more than 80 percent of its suppliers in the CEE market. Within four months, the company had already unlocked $25.5 million in working capital.

Cash flow matters.

About PrimeRevenue

PrimeRevenue is the leader in cloud-enabled supply chain finance solutions, managing and optimizing cash flow for more than 25,000 customers in over 70 countries. Last year, PrimeRevenue processed more than $100 billion worth of supplier transactions through its platform – helping companies unlock billions of dollars in working capital.

PrimeRevenue uses an extensive database and sophisticated analytics, coupled with proven supplier onboarding processes to drive customized programs across complex global supply chains.

www.primerevenue.com

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