TAKING A FRESH LOOK AT PAYMENTS

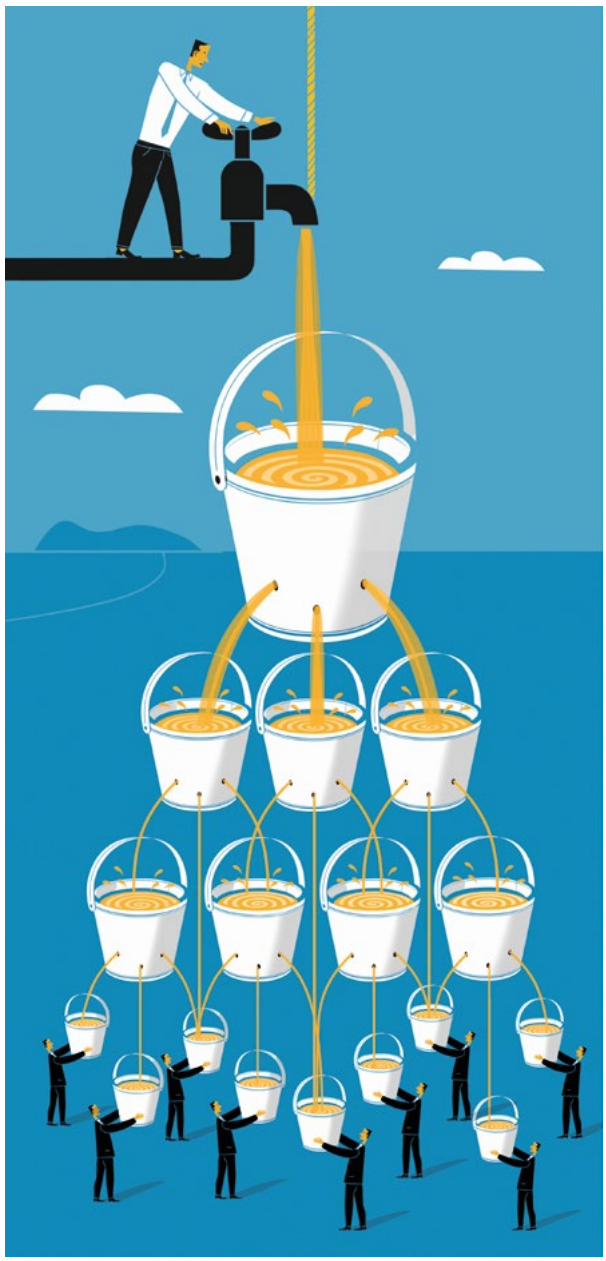
CORPORATES ACROSS THE MIDDLE EAST ARE FINDING NEW WAYS TO IMPROVE PAYMENT EFFICIENCY AND BOLSTER THEIR OWN – AND THEIR SUPPLIERS' – WORKING CAPITAL, WRITES EMRE KARTER

The falling oil price, weaker global growth and slowing worldwide trade have significant repercussions for the Middle East. Liquidity in much of the local bank market has dried up and, despite historically low interest rates, which should encourage lending, regional and international banks have also become more cautious in their lending (partly as a result of regulations such as Basel III). In response, corporates need to reduce their reliance on external liquidity.

One of the most important ways to do this is by unlocking value in their accounts payables (AP) and accounts receivables (AR) processes. Ideally, corporates want to transform what has historically been a cost centre into a profit centre and maximise gains from improvements in AP processes – by extending terms, for example. Solutions such as supply chain finance (SCF) and commercial cards are now more widely used in the Middle East to achieve these goals than ever before.

The current liquidity environment has convinced many buyers that there is only so much value to be squeezed before suppliers are dangerously undermined. This risk has been increased by the current liquidity environment, which makes it harder for suppliers, often smaller than buyers, to access financing. As a result, corporates are increasingly seeking to use SCF and commercial cards as mechanisms to provide suppliers with timely access to working capital.

This new focus on benefits for suppliers does not negate the benefits of SCF and commercial cards to buyers. Corporates still gain the opportunity to release liquidity trapped in their working capital cycle – reducing their need for external liquidity – and also improve the efficiency of their processes. Indeed, by supporting suppliers through the provision of finance that would otherwise be unavailable or too expensive, buyers are arguably gaining the greatest benefit: a more robust supply chain.



IAN WHADCOCK/IKON IMAGES

Taking a holistic approach

As well as increasing their use of SCF and commercial cards, many corporates are adopting a new mindset in an effort to derive the maximum benefit – both for themselves and their suppliers – from their payment arrangements.

Historically, SCF and commercial cards have been viewed as completely separate products. This is largely because they target different types of suppliers. SCF is beneficial for larger suppliers: typically, the 20% of firms that account for 80% of payables; commercial cards are more suitable for the 80% of firms that account for 20% of payables, most of which receive low-value, high-frequency payments.

As a result of these differences, SCF and cards are usually offered to clients by different product groups within banks: typically, trade is responsible for SCF, while commercial cards are offered by cash management, which often results in isolated rather than combined solutions. This split also reflected the arrangements at most companies: payments were generally not considered in a joined-up way.

Indeed, different individuals or teams were often responsible for managing SCF or commercial cards within treasury.

Now, the tight liquidity environment and the increased importance of supporting a wide range of suppliers have prompted a change in thinking. Corporates need to squeeze more value from their AP and AR process without harming their supply chains. As a result, they need to ensure that any solutions they implement have the widest possible reach across their supplier spend in order to deliver the greatest benefits for them and their suppliers.

Getting the right support

To ensure that corporates provide appropriate support to suppliers, they must first understand exactly who they pay and how they do it. This can be more difficult than it sounds. Undertaking a thorough analysis of payments in order to determine which suppliers are suitable for SCF or commercial cards can be challenging for corporates, given the thousands of payments they make on a regular basis.

One solution is to work with a bank that takes the company's payment data, working capital metrics and information about AP processes and platforms, and analyses it on the company's behalf. This snapshot is then compared against peer performance and industry benchmarks so that shortcomings can be identified. Opportunities to improve practices and payments efficiency, as well as better supporting suppliers by improving their access to finance are then identified.

By taking a holistic view of payments through such an analysis, corporates are able to ensure their payments strategies achieve optimum efficiency and also that the largest possible number of suppliers receive appropriate support in a cost-effective way. From the bank's perspective, the analysis makes it straightforward to segment suppliers and offer them either an SCF programme or payment via commercial card depending on the size and frequency of the payments they receive.

Taking an integrated approach to payments is also advantageous in the current environment in which treasury need to be able to demonstrate a clear return on investment. By analysing real payment data and devising an integrated solution, it is possible to quantify the efficiency gains delivered by various options, including SCF and commercial cards, and make decisions accordingly. It is also easier to demonstrate how AP can be transformed from a cost to a profit centre, while also ensuring that the utilisation of the organisation's enterprise resource planning is maximised.

> The tight liquidity environment has prompted a change in thinking

Government takes the lead

The holistic approach to supplier payments has most effectively been demonstrated in the Middle East by the government of one leading country, which has a large supplier base. Its solution uses both a bank corporate purchasing card and an SCF working capital management solution to unlock liquidity and pay suppliers almost immediately. This improves their working capital management and reduces the need to borrow at high rates. It also enhances the government's transactional efficiency by automating supplier payments.

An expected 9,000 local suppliers, mostly SMEs, will participate in the new payment solution. By supporting SMEs, the solution bolsters efforts by the government to promote a more conducive environment for the establishment of new businesses in the country: ultimately, the solution should enhance the country's competitiveness.

Other innovative uses of supplier finance solutions in the region include the use of purchasing cards by international logistics firm Aramex, which is headquartered in the United Arab Emirates, to make high-volume cross-border customs fee payments on behalf its customers.

Commercial cards offer similar benefits to SCF for buyers because their extended payment terms deliver a working capital benefit. Moreover, cards increase efficiency, lower costs and improve visibility and control through automation and streamlining. There is no longer a need to approve, check and pay individual invoices, for example; instead, all payments are detailed on a single statement every month for checking. Commercial card payments are also straightforward for suppliers to manage – they simply have to swipe cards or input numbers remotely – and reconciliation is easier because of the electronic nature of payments and the data that is captured for each payment.

Platform innovations offer additional options

While banks are continuing to innovate with solutions that combine SCF and commercial cards in an integrated offering, there are also new platforms emerging that offer buyers and suppliers additional flexibility in managing their payments and receivables, ones that enable buyers and suppliers to agree early payments using dynamic discounting.

On these kinds of platforms, buyers upload their approved invoices into the platform and establish their target return and input their available cash. If they have excess cash, they can pay invoices early, improving their balance sheet efficiency, while earning a better return than would be available on bank deposits. Similarly, suppliers can request early payment of their approved invoices at a specified rate. Algorithms then route and match the orders.

Corporates eager to find new efficiencies in their AP and AR process and discover innovative ways to support their suppliers – ultimately, strengthening their own business – should ensure that their bank is investing in new proprietary technology as well as building relationships with fintech providers: that way, they can be certain of having the greatest flexibility in the future.

Emre Karter is region head for treasury and trade solutions for the Middle East, North Africa, Pakistan and Turkey, at Citi

citi