Commercial Bank

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Taking a Holistic View of Supplier Payments

Supply chain finance and virtual card accounts have a crucial role to play in unlocking working capital opportunities.

The COVID-19 pandemic means that the outlook for firms in many countries remains precarious given sporadic lockdowns and considerable uncertainty about the national and global economy over the medium term. When times are tough, companies are more reluctant to draw on their revolving credit facilities and invariably place greater emphasis on unlocking working capital, which has long been a key metric for treasurers and CFOs. The past year has been no different: companies are looking for new ways to optimize their cash conversion cycle.

THE SCF PROGRAM

At the same time, most companies have seen a drop in their Travel & Entertainment (T&E) card spend – as much as 80% in some instances – as a result of remote working and restrictions on domestic and international travel. Many companies see income share, also known as rebates, as a revenue line to invest back in the business - for example funding new treasury workstation technology.

The solution to both these challenges is to take a holistic look at accounts payable (AP). Historically, there has been a tendency – among both banks and companies – to see each type of supplier spend in isolation and try to find an appropriate solution. Given today's challenges, it makes sense to adopt a fresh approach. By looking across their supplier base, companies can ensure that no opportunities to optimize working capital are overlooked.

Citi Commercial Bank does this by reviewing clients' AP files and analyzing their suppliers, spend patterns, geography, payment terms, payment instruments, and many other variables using sophisticated tools. Suppliers are then segmented – for example, into high value, low volume spend or low value, high volume spend – so that solutions such as supply chain finance (SCF) and virtual card accounts (VCA) can be deployed in tandem to deliver working capital efficiency across the payments continuum.

Supply chain finance comes to the fore

Once only the preserve of large multinationals, SCF is now a mainstream tool that companies of varying sizes can take advantage of. Setting up an SCF program costs nothing for a buyer and offers a proven way to enhance working capital by enabling buyers to extend payment terms to their suppliers, which results in improved DPO.

While at first suppliers might be hesitant to accept longer terms, especially given the current economic environment, SCF also provides significant benefits to a company's supplier base. Suppliers can benefit by selling their receivables to banks like Citi at a borrowing cost comparable to the buyers' own cost and, in doing so, get paid at a much quicker pace. This, indeed, helps to strengthen supplier relationships, provide additional visibility, and enhance supply chain stability.

In an SCF program, the buyer's bank purchases suppliers' receivables and then advances funds to the supplier. This enables suppliers to get paid earlier, improving their days sales outstanding (DSO). SCF leverages the buyers' superior credit rating so the effective cost of finance is much lower cost than suppliers would ordinarily pay. This is particularly preferential for suppliers that are non-rated or based in countries where the cost of borrowing can be quite high. Suppliers can also choose to sell their receivables to Citi at will, giving suppliers flexibility and additional liquidity at will.

> It is important for a bank or SCF provider to have the expertise, platform capabilities and global reach to facilitate engagement with the client's supplier base regardless of their jurisdiction, language, and time zone.

This helps to ensure that robust support is available throughout the onboarding process. When assessing a client's AP files for working capital optimization opportunities, Citi checks to see if any suppliers are part of SCF programs run by other Citi clients, which might indicate suitability to take part in another program. Other potential SCF targets are identified by scale of spend, the supplier's importance to the client or their business segment. The supplier outreach is very collaborative and Citi will work very closely with the company's procurement team to ensure alignment.

VCA helps fill the spend gap

With T&E spend sharply lower due to COVID-19, companies need to target other B2B areas to close the spend gap and protect their card program rebates, which are tiered according to spend. Indirect non-travel spend can take many forms, and much of it is not on companies' radar when it comes to working capital efficiency. Categories such as telecoms, ad or publishing spend, and office or computer equipment are prime candidates for payment via VCA.

As with SCF, Citi can analyze AP files to help companies find suitable suppliers for VCA; these are then checked against Mastercard and Visa databases to ascertain if they accept cards; many longstanding suppliers are paid by check or wire simply because these arrangements were put in place many years ago; suppliers may have subsequently begun to accept cards. Alternatively, some suppliers may already be paid by purchasing card; moving to VCA can lower administrative costs and improve control.

Moving spend onto VCA does more than just increase companies' rebate and improve return on investment: it also improves working capital efficiency. By moving B2B spend to VCA, companies can leverage the card statement cycle to increase their cash float and enhance their working capital. In addition, they can potentially extend terms beyond the immediate payment usually associated with cards. There are also benefits for merchants' working capital. Most merchants are happy to trade off card-related costs in return for getting paid earlier. While they have to pay card fees, those vendors targeted by VCA usually already accept card payments and will likely have added a small premium to their pricing to account for interchange and other card-related costs.

For the buying company, moving spend to VCA has a number of additional benefits. VCA can be easily integrated into cash management and payment solutions, making implementation quick and straightforward. VCA is also more secure and easier to reconcile; paper-based processes can be switched to a web-based portal or even integrated into the company's ERP system using APIs, so that payments are made direct from the company's own systems. Savings of as much as 80% are possible compared to a traditional purchase order process involving checks or wire payments; in addition, AP staff can be freed up for more value-added tasks.

Furthermore, VCA generates a unique 16-digit virtual and cardless account number for each specific transaction, and offers embedded and enhanced controls such as credit limits, usage timeframes, and the ability to restrict merchant types, all of which can be conveniently set up by program administrators. VCA also provides simplified reporting capabilities and offers visibility into where and how purchases are made by employees. Companies can then use this information to potentially negotiate supplier discounts.

Today's challenges present an opportunity for spend optimization

The challenges facing companies as a result of the pandemic have rightly prompted companies to take a fresh look at their spend and find ways to optimize their cash conversion cycle. By looking across the payments continuum, companies can not only offset low T&E spend by moving indirect non-travel spend to VCA in order to maintain their rebates, but also enhance their working capital when it comes to bigger ticket items using SCF.

Citi can enable clients to achieve the benefits of such a holistic approach because of its comprehensive analytical tools to assess clients' spend files, deep experience of onboarding vendors, and broad range of capabilities, including VCA and SCF, that can be deployed around the globe. By looking at payables in the round, Citi can enable clients to improve their working capital, lower costs and achieve greater visibility and control.

Marco Vernazza
Senior Treasury Sales Consultant
Citi Commercial Bank

Hayley Davidson
Trade Sales Consultant
Citi Commercial Bank

Jennifer Ware
Commercial Card Specialist
Citi Commercial Bank

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