Once upon a time supply chain management was a rather mundane and paper-intensive task. Granted it wasn't easy, but the main thrust was that after a negotiated price for goods, managers were mainly concerned with getting needed supplies moving, product out the door, and getting paid. Make the sale, find the most economical way to get from point A to point B—without disruption—and get paid. Upfront if you can.

Today, the changes are even more dramatic. Logistics and financial technology companies are stepping in with validation tools and notifications along the “A to B” processes. Things get done faster. Transparency along the supply chain enables transactions between companies and their suppliers. Moreover, authentication opens up opportunities for companies to partner with financing channels earlier in the process—to extend their terms and still accelerate payments to the sellers. This provides both sides with benefits, including greater liquidity and less inconsistency in the timing of payments. More simply put, get paid. Faster.

And many companies are beginning to realize this. According to NeuGroup meeting surveys and anecdotal evidence, companies are looking at their supply chains as available pockets of liquidity. While uptake has been slow, indications are that more focus on the supply chain will begin picking up in 2017 and beyond. In a recent survey, many companies revealed that they were looking to improve their days’ payable outstanding. And typical of the responses has been this from a treasurer at a global data and analytics company: “We don’t currently have an SCF program; however, working-capital optimization is a priority this year. We are considering a vendor finance program to…help us extend DPO and offer attractive financing rates to vendors in the program.” The treasurer said he also wanted to study p-cards and dynamic discounting.

So the supply chain can offer companies and their treasurers software platforms to facilitate consistency and liquidity. Yet underneath the technology there remains a core question to answer for the supply chain to work. What is the most efficient source of credit to enable the supply chain?

And preferably—for parties along the supply chain—unsecured. Is it the suppliers’ credit, the company’s credit, the customer’s credit or the lenders themselves?

What if it is the same entity for all four? For global supply chains it often is. A primary source of credit for facilitating global supply chains is the commercial credit insurance market. Commercial credit insurance is the working-capital credit instrument that protects against counterparty default or simple nonpayment in the supply chain. Available for accounts receivable, accounts payable, as an alternative to letters of credit, for confirming letters of credit, for factoring, AR purchases, payables finance, project finance…the credit along the supply chain. And since working capital makes up a sizeable portion of a company’s assets—some reports put the average at 40%—protecting those assets is critical.

But it’s not just the risk. Credit insurance offers a wide range of value to multinational corporations and their treasury departments beyond financing, including opportunities to generate sales, reduce parent guaranty commitments and offer customers better payment terms if needed. Unlike many lending products, insurance is available whether the commercial counterparty is a publicly traded or private, a government, a municipality, a financial sponsor or even a private equity firm.

Insuring commercial payment obligations against non-payment for working capital has existed in the US since at least the end of the 19th century. And while credit insurance was invented in the United States, it was further developed in Europe between the first and second World Wars. And in Europe—with all its borders—it took off. Favored over letters of credit for its ease of use, it is often reported that over 40% of European corporations’ accounts receivables are credit insured. In the United States that figure is less than 1 in 10, although it’s growing. Credit insurance provides unsecured non-notification credit protection. A valuable tool that ties up neither the seller’s nor the customer’s balance sheet.

Recently iTreasurer sat down with Dawson Beattie, CEO and founder of Credit Eureka, a firm that offers companies unsecured credit alternatives for protecting their working
Globally, insurance has always been a part of the supply chain experience. When getting a financing in place, a company’s insurance purchase was often indirect—via a bank. However, given myriad banking regulations this wasn’t always the best way to access the insurance market, says Mr. Beattie. Nor were banks equipped to pass on several of the insurance benefits to the company itself.

Stepping back a bit, when large banks purchase insurance their goal is often simply to satisfy a different master—their credit officer—and behind her or him—Basel. Large banks often use insurance to optimize their own internal capital allocations. It makes sense; credit enhancing the obligation may lower the lender’s capital requirements and offer flexibility in the structure. In some instances, companies may be unaware that the lender has purchased the insurance. For regional lenders, the experience may be different. Regional banks are less regulatorily encumbered. They simply report that insurance is required because the financed account name is not a familiar one—i.e., offshore. Further, if a company is selling to a customer that has, say, a third-party intermediary or private company that’s not on anyone’s radar screen credit-wise, i.e., not exactly investment grade, a bank might not be eager to help take on that risk without insurance.

Mr. Beattie offers an example of a US company going to a bank to help finance the larger part, say 80%, of $300 million in receivables. The bank says great, we’d...
love to do that but then it sees 50% of those receivables are offshore from customers where credit quality is obscure, unknowable or just too low. The bank then goes back to the US company and says it’s not comfortable with that set and only offers 80% financing of only 50% of receivables. Now instead of getting 80% financing of $300 million, the US company is left 80% of $150 million and forced to allocate different assets to the bank. A trickier asset allocation as inventory—next on the list—may also be offshore, or, if eligible, advanced by lenders at 50%.

But enhancing those receivables with insurance, from an investment grade company, makes them eligible with lenders. Returning to the above example, the company can get that 80% of the full $300 million. “Each and every time companies go to finance their global working capital, which is one of the easiest, cheapest sources of financing you can get, some version of this conversation with banks takes place,” Mr. Beattie says.

If insurance is what makes the assets financeable, a company may do better managing the insurance purchase directly. Direct engagement by companies often results in higher levels of availability and lower insurance costs and enables them to pass along insurance benefits to a company’s own team. “Naturally lenders become less interested in optimizing the insurance for their clients once their financing closes,” reports Mr. Beattie. “It’s not their product; they want the conversation to move on to other fee-related business.”

CALL FOR BACKUP

In terms of credit, insurance is often cited as the deepest credit market of all. Depending on which insurer you contact, they report covering 40 to 80 million individual companies worldwide. For companies, “going direct” to an insurance market—unencumbered by the same banking restrictions, and with more means for analyzing risk—can increase the amounts of credit available, save money and offer operational flexibility. And companies can do this at a reasonable cost through specialized firms like Credit Eureka.

The credit insurance market is not just for companies looking to finance the receivables. Many companies—in oil & gas, technology, pharma, etc.—have enough money where they don’t need banks but they are still interested in the insurance, Mr. Beattie says. “That company says, ‘I don’t really need to set up a supply chain financing to get more cash; why would I pay an unnecessary discount? It’s a waste of shareholder money. But I’m really interested in that insurance product.’” As product margins shrink, the value of insurance protection and its global reach increases. That’s because they realize that getting insurance can directly empower their sales team.

FROM START TO FINISH

From Start to Finish

| Make Introduction | Customized RFP | Submit to Insurer* | Review Terms | Nominate Insurer | Lend |

*Terms available from RFP submission:
7–10 business days for portfolios
1–3 business days for single names

Source: Credit Eureka

business lenders, factors, directors of credit, …they’re familiar with the territory and maybe they’re familiar with this local [distributor].”

Robert Morgan, a consultant to Fortune 500 companies and who has advised and implemented both SCF & commercial credit risk management platforms for multinationals, says “receivables are low-risk generally,” so insurance companies have found that being in the sector can prove a winner. This means that it can also be a reasonable option. According to Credit Eureka, insurers that partner with a seller will share up to 90% of the face value of accounts receivable (or in the case of a political or civil event, as high as 95%). The insurer and seller set pre-agreed-to dollar maximums for the buyers and the countries to be covered (for example, domestic vs. international, country-based limits, for individual buyers or whole portfolios).

The price of the insurance is dependent on which insurer is used, but for the most part, premiums are usually calculated by:

- a quoted insurance rate (a % of 1%) \times estimated dollar value of annual insured sales, or
- a quoted insurance rate (a per annum rate) \times dollar balance of accounts receivable to be covered. (i.e., similar to a loan).
For example, in many countries, selling to the customer isn’t a straight-through process. Outside of insurers, very few financial entities cover these countries and companies. There is minimal capital markets coverage, and traditional lenders are not active locally. Moreover, local practices may be such that purchasing is through a “daisy chain of distributors” which often means instead of selling to a known credit, companies have to sell through unknown smaller firms. Mr. Beattie says a US company weighing this problem might say, “I can see you and I can see your balance sheet and it’s worth $100 million, but this little entity that’s set up as the purchasing agent has a balance sheet I can’t see or has little net worth; I have a problem with that.” Traditional ways to combat this are to have the customer pre-pay or issue an LC. But in the current competitive environment, the company might go to another provider. So the only option is to stay in the deal but do it in the best way possible.

This is where AR insurance can help in so many ways. If the company can get non-notification unsecured credit protection on selling/purchasing entities from an investment grade insurer, it can be more comfortable advancing its products to the buyer on open account terms. In this case, Mr. Beattie points out, the company is ultimately buying the insurance not necessarily as a financing tool “but as way to build its revenue line. This is where most companies who purchase insurance end up. Once the insurance benefits reach the commercial teams, the insurance often outlives the original financing.”

**THE OVERALL BENEFITS**

AR insurance continues to grow and its expense and flexibility make it a good option for supply chain, and a variety of other situations. Most notably as an inexpensive yet deep resource for counterparty risk mitigation. Most companies, even for very large MNCs, don’t want to ask their customers for security or updated credit information when making a sale—at home or abroad. Thus going to an agency that can locate the right insurer for you makes sense.

But beyond risk mitigation, AR insurance can help increase sales without decreasing credit quality. It can help smooth the relationship between buyer and seller by enabling the seller to offer open account terms to a wide variety of customers or countries. The insured AR can also be used as security for financing/sale to banks or other financial institutions, as part of a supply chain or a simple working-capital revolver. It can also help eliminate or reduce cap limits due to customer concentrations, and it can help companies easily enter new channels and unfamiliar territory and get off to a fast start.

Like many parts of modern supply chain management, seizing the reins of the credit conversation becomes a win-win for users and benefactors.

**“The credit insurance market is not just for companies looking to finance the receivables. Many companies have enough money where they don’t need banks but they are still interested in the insurance.”**