Greensill

FINANCING THE FESTIVE SUPPLY CHAIN

The Christmas holiday season is a crucial time for the global economy, with many retailers and their suppliers relying on this hectic five-week period to generate the largest proportion of their profits for the whole year.

$110bn
accounts receivable outstanding at Christmas

It is a nerve-wracking time as stores bet on the popularity of items ordered months ago, literally by the boatload, and wrangle supply chains that stretch across the globe to meet demand.

This year that supply chain will be the longest and most valuable ever – a vast global trans-shipment which has locked up within it $110 billion of accounts receivable outstanding.

That's $110 billion of invoices waiting to be paid to thousands of suppliers, according to the latest seasonal supply chain research from Greensill, the world's leading non-bank provider of working capital finance, and the Centre for Economics and Business Research (Cebr), the UK-based economics think tank and advisor to the UK Government.

18%
rise in the value of invoices owed across the festive season supply chain in 2018

Just imagine what all those suppliers could do if that cash were paid to them today. The possibilities are endless.

The research also shows that this accounts receivable problem is getting more acute all the time, as this year's forecast $110 billion is $16 billion greater than the total for the same period in 2017, a projected increase of 18%.

Accounts receivable outstanding represents all the payments associated with the manufacture, shipment and sale of the goods we buy each day. The longer it takes for suppliers to get paid the more accounts receivable they will accumulate.

Greensill monitors accounts receivable outstanding to gauge the health of the global economy from the perspective of all of the companies doing business in it, and in particular, all of the companies waiting for payment.

Lex Greensill, founder of Greensill says: "We analyse the Christmas holiday supply chain in this way as it gives us a really good look under the hood of the global economy, revealing the finely tuned engine that every business on earth relies upon to run efficiently.

"Greensill uses technology to level the playing field for all businesses in the supply chain, to give them access to cash at rates that until now have been available only to giant corporates. Greensill calls this process the democratisation of capital – making affordable cash easily available to all businesses."

Lex Greensill, founder and CEO of Greensill

The accounts receivable outstanding phenomenon is most pronounced for consumer electronics such as phones and tablets, as well as clothes and toys – the top three categories of gifts received during the festive season.

The consumer electronics category, including smartphones and tablets, is forecast to have the greatest sum of accounts receivable with almost $40 billion outstanding globally for the 2018 festive period. Clothing is expected to accrue $23 billion in the same period, while toys are forecast to accumulate more than $2.4 billion.

The corresponding figures in 2017 were: consumer electronics $34 billion; clothing $19 billion; and toys $2 billion.

To better understand this phenomenon, we have provided detailed analysis of the top three gift categories overleaf.

WORKING CAPITAL CRUNCH

Clothing, toys and electronics suppliers are owed a total of $65 billion in the festive season supply chain, +17.7% on 2017

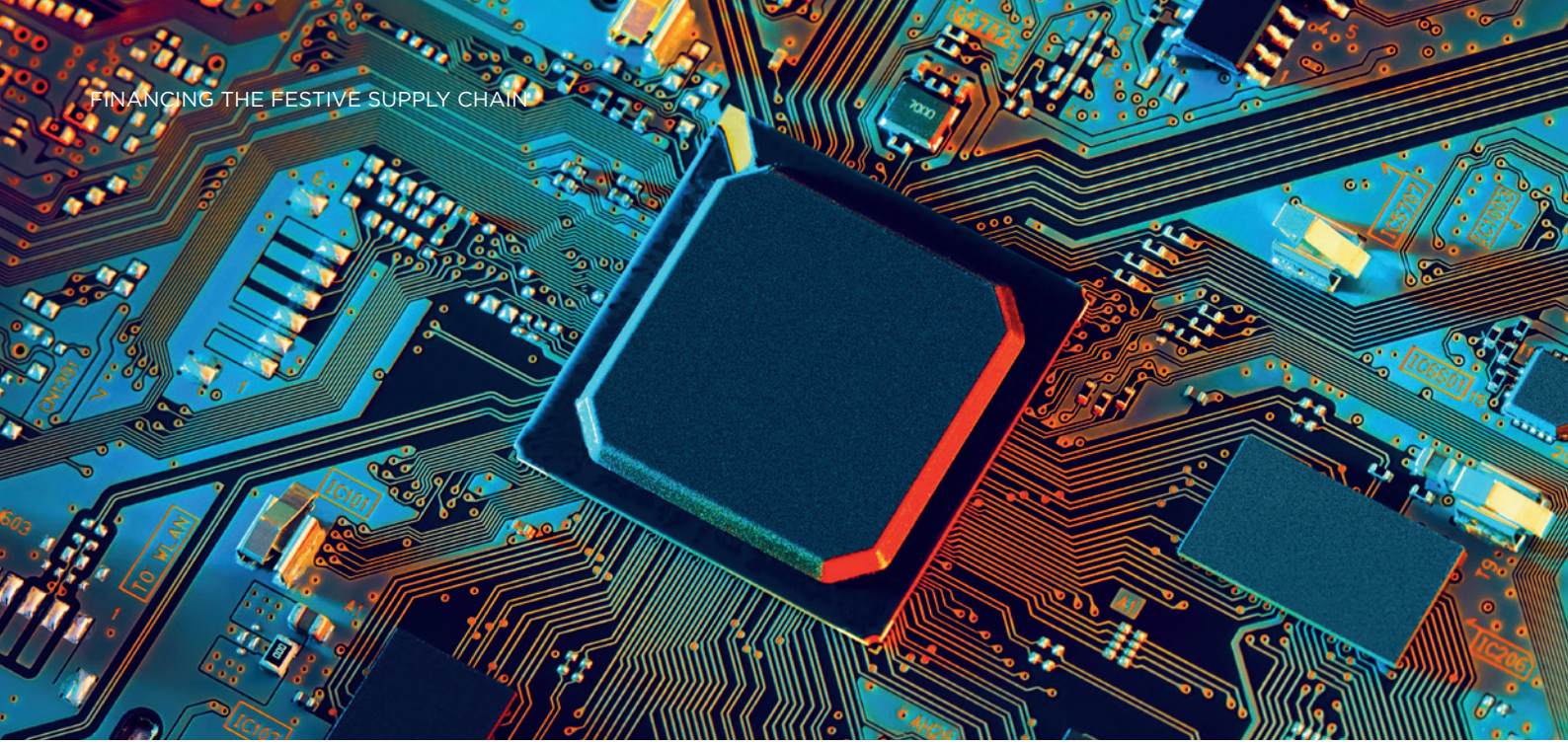
Total amount owed to suppliers in 2018 holiday season

$110 billion

+18% year on year

Electronics	Clothing	Toys	Other gifts
$39.7bn	$22.8bn	$2.4bn	$45.1bn
+16.9%	+19%	+16.9%	+18%

Source: Greensill and Cebr



Consumer electronics

Consumer electronics have become increasingly popular gifts during the festive season, with 40% of US consumers telling Deloitte Holiday Survey in 2017 they planned to purchase electronic goods.

Economists are watching this sector very carefully because global sales of consumer electronics have increased at a slightly slower pace than other retail sectors during 2018. On this basis, Greensill and Cebr predict accounts receivable for the sector of $39.7 billion for the 2018 festive season compared with $33.9 billion last year.

That still far outstrips the combined total of clothing and toys and represents a 17% increase over Christmas 2017.

With more than 20 major sets of components in each device, the supply chains for these products are highly complex and involve an array of different companies and countries. However, the collective accounts receivable are heavily influenced by the activities of a handful of very large companies such as Apple and Samsung.

As a result, the assemblers of smartphones and tablets such as Foxconn Technology Group, Pegatron Corporation and Wistron are among the largest players in the global festive supply chain.

The forecast rise in accounts receivable can be attributed to a combination of strong revenue growth for the sector as a whole, as well as an overall increase in the ratio of accounts receivable to annual revenue. This suggests a general uptick in the amount of time between the delivery of products and receipt of payment for those goods.

$39.7bn
value of accounts receivable for electronics suppliers

This widening gap between supply and payment has meant phone manufacturers have embraced supply chain finance. Roland Hartley-Urquhart, vice-chairman of Greensill and head of US operations, created the first finance package for the mobile sector in the late 1990s and has tracked the evolution of the industry ever since.

"Twenty years later we are financing the supplier side and consumer side in the handset business," says Hartley-Urquhart. "With today's expensive phones, companies want to get them off their balance sheets because the receivables take several years to materialise as everyone is now on one-, two- or three-year deals."

This creates several challenges for carriers, the greatest of which is cashflow related.

Manufacturers need to be paid for their phones within 90 days, at most, while the customer pays for them over 24 months. At up to $1,000 a handset over millions of customers, that's quite a lot of pressure on the balance sheet.

The second is recognising revenue. The global accounting standard IFRS 15 has made calculating how much income carriers can take from these financing deals extremely complex, as it relates to the residual value of the phone financed.

In the past, carriers would alleviate the balance sheet pressure by securitisation—selling bonds secured on the revenue streams from the phone plans. These are cumbersome, taking up lots of time and legal fees, so only worth doing in tranches of at least $100m.

Greensill looked long and hard at this challenge and developed a better way. It used the techniques it developed to aid companies globally with supply chain finance to create an off-balance sheet handset receivables purchase programme.

In short, Greensill sets up an off-balance sheet purchase facility and the carrier regularly sells portfolios of handset deals. Greensill then sells bonds to investors secured on the handset receivables. The carrier can sell as many, or as few, portfolios as it needs to, making the process totally flexible.

"Our product is really simple to set up," says Tim Armstrong, UK origination managing director for Greensill. "You don't need a special purpose vehicle or a rating from an agency. The investor is essentially buying corporate risk from some of the biggest companies in the world."

"We take 95% of the risk, which allows the carrier to recognise revenue and free up their balance sheet."

Tim Armstrong, Greensill UK origination managing director

"We look at the historical default rate and project the probability of future defaults to calculate the purchase price," Armstrong adds. "We take 95% of the risk, which allows the carrier to recognise revenue and free up their balance sheet, but importantly, they still have an incentive to improve collections if the portfolio deteriorates."

The Greensill programme was first dialled up for Vodafone, and is now also being developed for a number of other carriers worldwide, with more than a $1 billion of bonds already sold.

In the rapidly evolving mobile phone market, this sort of flexibility allows the carriers to keep pace with changing consumer behaviour.

$22.8bn
value of accounts receivable in clothing supply chain

Clothing

Clothing was still the most popular category of gift in the US last year, according to the Deloitte Holiday Survey, and global clothing sales have grown faster than other product categories so far in 2018.

Based on this, Greensill and Cebr forecast that accounts receivable in the clothing sector will show an above-average rise of 19% this festive season to a total of $22.8 billion outstanding. Last year's figure was $19.2 billion.

The annual value of the clothing supply chain is around $300 billion. The proportion attributable to Christmas gifts rose 18% last year to almost $20 billion as clothing sales became more concentrated in the festive period.

As well as seasonal changes, Greensill and Cebr's analysis highlights another fundamental shift affecting the industry: the squeezing of small suppliers by major chains.

The value of invoices owed by major clothing retailers to garment manufacturers and other suppliers rose by $6 billion in the period under review but the fabric producers' accounts receivable are estimated to have fallen by $24 billion.

This may be a consequence of the high degree of fragmentation in the garment sector. Most stages of the clothing supply chain involve a huge number of firms, each with a relatively low market share. For instance, the largest garment manufacturer – Crystal International Group – has a market share of just 0.3%.

$6bn
rise in value of invoices owed by clothing retailers to suppliers

The denim production cycle provides a perfect illustration of the problem facing those at the bottom of the supply chain.

Raw denim is bought by the big brands and, in most cases, the producers have to ship the agreed quantities to buyers' own contracted mills overseas – typically, in Mexico, Bangladesh, Sri Lanka and Pakistan.

The raw materials are then made into jeans, shirts, jackets and other garments but the original material supplier only gets paid when the retailer is happy.

Supply chain finance can make a real difference here, explains Greensill's Roland Hartley-Urquhart. "The original supplier often has to make payments well in advance of getting paid. For example, they often have to ship material to the buyer's mills at their own expense. We can use information held by buyers to see when materials are delivered on a consignment basis."

As with phones, there is an ever more sophisticated order tracking and processing IT infrastructure that can calculate how much material has been produced, how much has been dispatched and, crucially, what percentage of the consignments of finished garments have firm orders against them.

Once again, having the right level of information allows for accurate risk assessment. That, in turn, allows for the packaging of confirmed invoices into bonds that the financial markets understand and find attractive as investments.

$2.4bn
value of accounts receivable for toy suppliers

Toys

The popularity of games and toys spiked in 2017 with four out of ten US consumers buying them as gifts, according to the Deloitte Holiday Survey.

Like consumer electronics, sales of toys have grown more slowly than the average this year, so Greensill and Cebr economists are predicting a 17% rise in accounts receivable outstanding at Christmas to $2.4 billion, from $2 billion in 2017.

Some 70% of the accounts receivable along the toy supply chain is attributable to manufacturers typically owed funds by wholesalers and retailers. With the general squeeze on retail margins, and the collapse of Toys R Us earlier in 2018, it is a worrying time for toy suppliers owed money.

Lego, Mattel, Hasbro and Bandai Namco, the four largest toy makers, have a market share of 34% and total revenues of around $20 billion, according to the latest publicly available data. However, the amount owed to major toy manufacturers rose at a faster pace than the growth of their annual revenues, leading to a rise in the ratio of accounts receivable to annual revenue.

Greensill and Cebr say this suggests a growing gap between the manufacture and delivery of the toys themselves and payment by retailers and wholesalers.

The collapse of Toys R Us has also caused supply chain headaches among toy makers, as Hasbro chief executive Brian Goldner explained in an earnings call in October. “Many retailers set their shelves later in the quarter to begin their holiday efforts, but retailers are stepping up to capture the Toys ‘R’ Us market share,” he said.

The wider spread of stores to be stocked not only means smaller quantities of goods per truck but also more cartons of high-demand toys and games delivered later in the festive cycle. "Hasbro shipped more products domestically in September than ever before, and we were unable to meet all of the demand within the quarter," Goldner told analysts.

Just a few months after Toys R Us filed for bankruptcy, US retailers Walmart, Target, Kohl's and J.C. Penney and others signalled plans to increase toy offerings in the fourth quarter. Walmart is displaying 2,500 new and exclusive toys this year, double the number of last year, while Target said it was clearing 250,000 square feet of space for toys.

Looming large over the sector, as with many others is Amazon, which captured one out of every six dollars spent on toys in the US during 2017, according to One Click Retail.

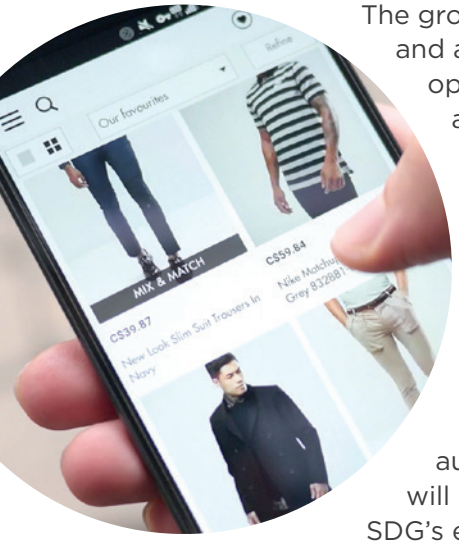
It all adds up to an anxious Christmas for the toy trade. The strength of their balance sheets may insulate the big four toy manufacturers for some time but smaller suppliers could have cause for more immediate concern.

74%
Shop Direct sales made on mobile devices

Like the denim producers and the small electronic components manufacturers, they have little power to influence events in a market that is changing rapidly. However, the increasing sophistication of data analysis, risk assessment and financial markets means their position is looking brighter.

Shop Direct Group, a Greensill client and one of the UK's leading online retailers of clothing, sportswear, electricals, homeware and toys, provides a perfect example of how supply chain finance helps oil the wheels of the global economy.

SDG has more than 128 years trading history and is the UK's second largest pure play online retailer, trading under the brands of Very and Littlewoods.



The group has been forward-thinking when it comes to online sales and although SDG had a history of owning stores, it has not operated on the high street since 2005. The group now has an average of 1.4 million online hits per day with 74% of sales made on mobile devices, and UK-wide delivery within 24 hours.

Greensill has worked with SDG since 2015 and pays more than 100 of their key suppliers within five days of goods being delivered to any one of three distribution centres. This reduces the stress on their merchandising suppliers at a time when the UK high street is under pressure.

Greensill is further supporting SDG's development of a new automated distribution centre, in the East Midlands, which will be on-stream in 2020 and will secure the next phase of SDG's evolution.

The biggest and most complex global supply chain is gearing up for one final push at Christmas. Retailers are adopting ever more sophisticated just-in-time ordering systems and waiting as long as possible before placing orders.

In just a few weeks, when the forecast $110 billion of invoices will have been submitted, we will know which of products soared and which sank.

How long suppliers have to wait to receive their share of the festive windfall will determine the prospects of many small and medium sized companies – and even some large multi nationals – well into 2019.

Greensill's supply chain finance programmes are one of the most effective ways of alleviating cashflow pressures on companies of every size and scope at all points on the supply chain.

For companies with volatile cashflow, supply chain finance offers a more efficient alternative to taking on debt. Invoices are paid within days and fees are low.

Greensill keeps the process friction-free, easy to implement and run using the latest technology and leveraging access to capital markets.

The firm buys hundreds of thousands of invoices from companies every day and pays them immediately. It packages them into short-term, buyer-backed bonds and sells them to investors. In fact, Greensill is one of the most prolific bond issuers in the world, issuing about 26 bonds every business day of the year.

"What is critical in the DNA of all the structures that we provide is the accurate, timely and complete information that reflects what is really going on in the physical supply chain – even the most complex supply chains on earth such as this one," says Lex Greensill.

"Greensill can find a solution to unlock billions of dollars of capital so our clients can put it to work. At Christmas, and throughout the year."

Lex Greensill, founder and CEO of Greensill

GREENSILL: CHANGING FINANCE TO CHANGE THE WORLD AT CHRISTMAS AND ALL YEAR ROUND

Greensill's supply chain finance programmes are one of the most effective ways of alleviating cashflow pressures on companies of every size and scope at all points on the supply chain.

Suppliers submit preapproved invoices that are paid quickly at a discount by a third-party financier while buyers settle bills much later. In so doing, SCF helps both sides in a transaction manage cashflow and risk with much more certainty.

Greensill, which was born a little over seven years ago, pioneered a technology-driven SCF platform for the digital age that employs easy online sign-up for suppliers, simple integration with existing Enterprise Resource Planning Systems, and a robust financial foundation in the capital markets to bring what was once an exclusive privilege for large suppliers to any supplier of any size that can provide a pre-approved invoice.

Greensill's approach is evolving every day as technology continues to improve. The increasing sophistication of machine learning and artificial intelligence today offers the ability to analyse supplier data in more detail than ever before, and in real time.

The result is that thousands of financially robust suppliers that may slip through the net of traditional risk profiling can at last find a simple solution to the seasonal squeeze that relieves pressure on their balance sheet and allows them to participate in the most lucrative time of the year.

METHODOLOGY

To estimate the value of accounts receivable throughout the supply chain, Greensill and the Centre for Economics and Business (Cebr) examined the annual reports of major companies in clothing, consumer electronics and toys at various stages of the supply chain. In each case, accounts receivable provided information on the amount owed to the company downstream in the supply chain, while the accounts payable helped identify what the company owes to its suppliers. Cebr then scaled up the accounts receivable to arrive at sector-wide estimates using data on the market share of each company under review.

ACTION POINTS

The total value of accounts receivable outstanding in the festive season supply chain is $110 billion globally, +18% year on year

Balance sheet optimisation with Greensill's range of working capital finance solutions is the best way to unlock the capital trapped in accounts receivable

Greensill constantly analyses the levels of accounts receivable outstanding worldwide as a real barometer of the global economy

Making capital available for all suppliers on the same terms as giant corporates improves the global economy. Greensill calls this the democratisation of capital

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