PROCUREMENT'S GUIDE

to successfully extending supplier payment terms

PrimeRevenue

Introduction

What makes a supply chain finance program successful? What are the common points of failure? Historically, answers to these questions have focused on factors like platform ease of use, availability of funding and geographic reach.

One aspect, however, has been routinely overlooked. According to research conducted by McKinsey, the support and education of procurement and suppliers is one of the most important factors in determining supply chain finance program success (source: McKinsey on Payments, October 2015).

How important is a strategic roll-out of extended supplier payment terms? Just ask industry giants like Boeing, Delphi Automotive and Rio Tinto. Critical missteps in their programs resulted in public backlash and poor program performance.

This is especially true when it comes to navigating supplier payment term extensions. These conversations require an understanding of finance strategy, skillful messaging and objection handling – responsibilities geared more towards a finance or sales rep than a procurement executive.

Yet, few procurement teams are given the appropriate support and education required to extend payment terms across a broad group of suppliers. It's a point lost on many supply chain finance vendors (including financial institutions) that spend months training procurement teams to use portals and platforms, but little time preparing them to message and sell the actual extension to suppliers.

This lack of preparation and a well thought plan can spiral downwards quickly. Take global mining giant Rio Tinto, for example, whose supplier payment term extension was doomed at the onset. In early 2016, the company unilaterally doubled supplier payment terms via a blanket announcement from its outgoing CEO. Without any insight into the company's larger supply chain finance strategy, and an "effective immediately" timestamp, suppliers protested vociferously. By mid-month, the company reneged on the term extension as the ill-conceived strategy became a public battle.

Backed by its experience optimizing cash flow for more than 20,000 customers across the globe, PrimeRevenue recognizes that successful supplier payment term extensions only happen when procurement receives the right training and ongoing support. Before companies implement an extension with suppliers, they must first understand the traits (and barriers) to success.

Barriers to Supplier Payment Term Extension Success

In most cases, the success of a supplier payment term extension program is determined long before the program is introduced to suppliers. The missteps that undermine performance are directly tied to organizational readiness – not just within the procurement function, but across multiple facets of the business. Common barriers to success include:

Procurement processes and operations are all over the map (literally and figuratively). For some global corporations, procurement is a highly decentralized function. There may be different buying groups for different supplier sectors (e.g. electronics, plastics, etc.) or different geographies (e.g. EMEA, APAC). Companies that have grown through acquisition may have multiple procurement teams that continue to operate autonomously. In these instances, companies lack standardization and synthesis across procurement cultures, processes, payment terms and negotiation guidelines – making it difficult to execute any strategic supplier initiative.

The alliance between procurement and finance is weak. The relationship between procurement and finance isn't always a strong one – and that's because they don't speak the same language nor do they have the same goals and MBOs. Procurement should be viewed as a strategic lever to improving working capital and given a seat at the table during these discussions. This will demonstrate commitment from both teams to align their functions to achieve common objectives.

The objectives aren't clear. It's difficult to rally an entire organization – one that's tasked with managing hundreds (or thousands) of suppliers – around a task without understanding what's at stake. Finance and procurement teams need to set clear objectives for supplier payment term extensions. Why are we doing this? What do we want to accomplish? What role does procurement play? Answers to these questions need to be clearly defined and well-communicated to the procurement team.

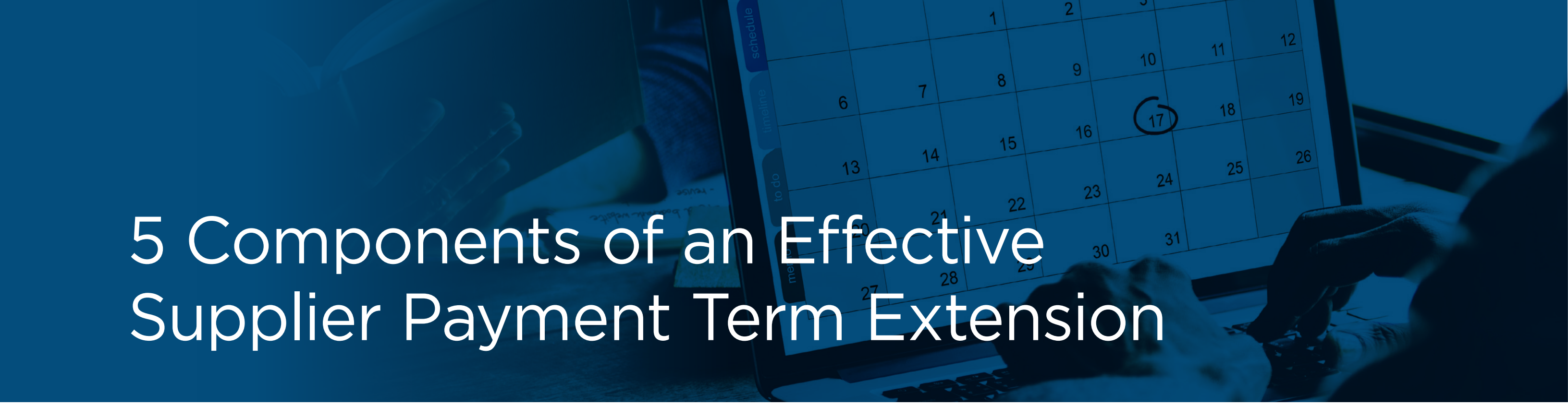
When it comes to goals, precision matters.

Wrong: Increase cash flow with suppliers.

Right: Add minimum of 50M USD cash flow gain in FY17 to offset new acquisition costs. Target 50 suppliers in Phase I.

The incentives are tied to the wrong metrics. Historically, procurement team compensation has been based on how well they negotiate supplier pricing and quality. While these metrics are valuable, they do little to motivate performance around extending supplier payment terms and materially increasing cash flow.

The length of the extension is a shot in the dark. Companies often use a blanket approach to determining the number of days by which supplier payment terms are extended. This a critical misstep as standards and thresholds vary by industry, commodity and jurisdiction. It's important for companies to benchmark term extensions to understand if the increase is reasonable and if the market will bear a higher or lower increase.



5 Components of an Effective Supplier Payment Term Extension

To successfully execute a supplier payment term extension, companies should focus on five core components:

1. **Analysis Procurement needs to establish a strategic and conscientious direction for the term extension program.** Why does the company need to extend terms? What is the cash flow goal? Which suppliers should be targeted to help achieve this goal? Which should be avoided? By how long should terms be extended in relation to what the market will bear, and how will this increase be justified? These questions can't be answered by estimation or gut-check. They require deep analysis of financial and supplier data.

2. **Mandate Supplier payment term extensions are large-scale, strategic initiatives and should be communicated as such.** They should be introduced internally from a position of authority and leadership (e.g. CEO, CFO, CPO) and driven by mandate. The mandate should clearly communicate what the organization is trying to accomplish and why. For example, a company may want to increase working capital by 30 percent to fund specific infrastructure upgrades that will help them meet a new regulatory requirement. It's this sort of granularity that helps procurement understand that the mission at hand isn't just another item on its to-do list – it has a specific and strategic purpose.

3. **Messaging How will better cash flow for your organization benefit suppliers?** It's the million-dollar question, and one that few procurement teams answer carefully. Suppliers instinctually see longer payment terms as a negative. Procurement must help them reframe their thinking and be prepared to handle objections skillfully. More working capital for new production facilities could mean more business opportunity for the supplier. If an influx in cash flow helps your business invest in innovation that will thwart competitive threats, then stability becomes a key value proposition for suppliers. Keep messaging tailored to each supplier segment.

4. **Execution Don't try to boil the ocean.** In other words, don't attempt to rollout extended payment terms to all suppliers at once. Focus on certain supplier segments (by industry, geography or size, depending on the company's unique objectives). Establish phases, timelines and metrics to determine who will be targeted when and how success will be measured.

PrimeRevenue's SCiMap solution makes supplier analysis easy.

- Identify how much potential cash flow you can generate to meet goals
- Analyze suppliers using industry benchmarks to prioritize them for rollout
- Create profiles for all suppliers along with a customized strategic plan for negotiation
- Develop appropriate messaging to help obtain supplier buy-in
- Personal support during negotiations

5. Training **This is the step that synthesizes the analysis, incentive, messaging and execution strategy into a playbook for how procurement will get the job done.**

Training should address several topics including:

- Cash flow and supply chain finance fundamentals – What is it and how does it work?
- Messaging and objection handling – What are the key benefits and value propositions by supplier segment? What are common supplier objections and what are the best ways to handle them? These need to be reinforced in training.
- Preparation – Team members need to know how to prepare to “sell” a term extension to a supplier. This includes putting together a picture of the supplier’s current situation, including current contracts, terms, commitments and payment history.
- Outreach protocol – What is the step-by-step process for how procurement should reach out to suppliers? What tools should be used to expedite this process?

Creating an effective supplier payment term extension program

Confidence – Procurement’s Most Powerful Tool

The role of procurement within large supply chain organizations is changing quickly. The extension of supplier payment terms is just one example where team members are expected to demonstrate a strong understanding of financial, supplier management and selling dynamics. It’s also a sizeable opportunity for procurement teams to demonstrate a broader strategic value to the organization.

However, the education and training of procurement during this initiative is critical and requires the full support of financial and executive stakeholders. Procurement teams must be equipped with the right messaging and become highly proficient in navigating complex conversations with suppliers. They must also have access to the right stakeholders on the supplier side of the table – those people who have a strong financial background and can understand the benefits and value of supply chain finance.

While tech-enabled tools may facilitate supply chain finance, it’s only one small part of the education and training that has to happen to further program success. Ultimately, the path to optimized cash flow is paved with confidence and strategy.

Cash flow matters.

About PrimeRevenue

PrimeRevenue, the leading provider of working capital financial technology solutions, helps organizations in 70+ countries optimize their cash flow to efficiently fund strategic initiatives, gain a competitive advantage and strengthen relationships throughout the supply chain. PrimeRevenue's unique approach to supply chain finance places heavy emphasis on procurement readiness and support.

Headquartered in Atlanta, with offices in London, Prague, Hong Kong and Melbourne, PrimeRevenue's diverse multi-funder platform processes more than $180 billion in payment transactions per year and 1.1M invoices per month.

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