The Development of Supply Chain Finance in China

Chang Xingjian[1], Deng Shiming[2]
[1,2]School of Management, Huazhong University of Science and Technology
Wuhan, Hubei, China

Abstract- *Fast economic growth in China, as one of the largest manufacturing bases and markets in global economy, has stimulated innovations in financial service for facilitating supply chain operations. We have surveyed the supply chain finance industry in China, and provide an introduction of commonly used financial products. We point out the obstacles and shortfalls in the development of the supply chain finance in China and provide recommendations for both private companies and policy makers on how to facilitate the growth of supply chain finance.*

Keywords-*Supply Chain Finance; China; Economic Growth;SME*

1. BACKGROUND

With the development of economic globalization, cross-border transactions more frequently. Because multinationals more offshore production and outsourcing, multi-party transactions involving transnational additional taxes, transportation delays, interruptions in production , financial regulation , and exchange rate risks and other issues , all of the cash flows of the financial supply chain challenge . Moreover, in emerging markets , higher financing costs of plant and equipment investment. In addition , globalization tends to extend the operation of the value chain cycle for several weeks , thus backlog of up to 30% of liquidity. Also serious is the core enterprise often by delaying payments to suppliers or distributors to accelerate the shift to inventory to achieve their financial economy. However , these practices actually formed downstream of the backlog of funds , resulting in financing costs throughout the supply chain finance increases, and may force suppliers to delay the purchase of raw materials, reduce inventories , and thus delayed the delivery of core business ; or forcing distributors to defer the settlement and cost borrowing , giving the entire supply chain from continuing operations a great deal of risk. In addition, due to the cash flow of the supply chain bottlenecks members of the supply chain and distribution channels, which together affect the stability and financial cost of the entire supply chain. Under such circumstances, the core business and financial needs of small and median enterprises (SMEs) have been some changes, mainly reflected in:

1. A core business (buyers) in order to make their balance sheet data of optimism , as the delay in delivery is included in the vendor 's own name.
2. Since the core business of the delay in acquiring the inventories , delayed payment , vendors need to supplement low-cost sources of funds liquidity needs .
3. Since the core business continued to distributors yahuo , distributors need to reduce their large inventory of funds used .
4. Because outsourcing companies can lead to financing to support its own physical assets less and less.
5. SMEs often face harsh financing environment , the problem of tight cost financing or capital chain , resulting in an increase of the supply chain, product costs or suppliers to exit.
6. strong position in core businesses , making international credit settlement gradually replaces some letter of credit , supplier credit financing through the channel further narrowed.
7. Because of the uncertainty of the date of shipment overseas purchase orders , companies can not accurately predict the time of arrival of the goods and the settlement date . To manage this uncertainty , buyers need to keep inventory in case demand greater security and the need to set aside more cash in the account for a rainy day .

2. DRIVING FACTORS FOR FINANCIAL INSTITUTIONS IN SUPPLY CHAIN FINANCE

Since SMEs is more serious payment arrears, together with its " Evading " phenomenon is more prominent, resulting in a vicious cycle of credit . Therefore, financial institutions need to update the product , risk control services to SMEs and to promote the development of new business, especially to carry out current assets business innovation. Overall, supply chain finance services can provide new ways and new profits for the bank's competitive means . For financial services , the specific financial needs of financial institutions that :

1) Look for new market
2) Reduce credit risk
3) Disposal of certain non-performing assets
4) Effective management of customer information
5) Enhance collateral assessment
6) Provide corporate finance advisory services

3. FINANCING BUSINESS DEMAND FOR SUPPLY CHAIN FINANCE

With regional procurement towards global sourcing, liquidity for operational efficiency and supply chain businesses challenges. Therefore, companies are seeking to own banks and financial supply chain solutions , including new support tools for financial instruments to cope with credit and new solutions receivable financing. Meanwhile, global competition has forced the major companies increasingly seek to achieve sales targets, which makes the importance of distribution channels has become increasingly prominent . Practice has proved that distributors rely on their own strength and credit carry high cost and low efficiency financing , and ultimately become a major global companies to complete the sales target bottlenecks. Because mortgage asset-backed financing distributors can provide is limited, companies simply can not match the big double-digit sales growth targets. This forced large enterprises as the seller had to provide a longer credit period as distributors, their own and then seek new financing to supplement thus occupied liquidity. In this case, the core business, its main requirements are:

1. Change financing to improve its financial structure, reduce debt accounting .
2. Inventories occupied a lot of money making enterprise liquidity shortage might be in trouble, so companies use to generate demand for inventory financing.
3. Due to limitations of the national industry policies or bank risk assessment and credit policy , credit is limited , you need other forms of loan financing.

For SMEs , because of high thresholds for listed SMEs , SMEs difficult to finance by issuing bonds. In addition , due to the presence of the majority of our capital strength of security agencies , insufficient own credit and other issues, for large loans and long-term loans will not provide a strong guarantee. So for SMEs, generally only take charge or pledge loans . However, SMEs may pledge assets less mortgage very difficult to implement . Meanwhile, China's SMEs prevalence of the following questions: 1. Credit is not high , a sense of credit . 2. Financial management is not standardized, capital accumulation unscientific , the smaller the size of the source of financing . 3. High- risk small and medium business , lack of collateral . Features easy mismanaged banks and other financial institutions for SMEs to make on the loan will be careful , so SME financing in general is more difficult . In such cases, the main demand : a financing proposal ; credit guarantees ; information services, financing and other services.

4. SUPPLY CHAIN FINANCE PRODUCTS

4.1 Commonly used Financial Products

Currently, supply chain finance financing products are mainly divided into three categories: Inventory products, Advances and receivables products products, and under each category there are different forms of specific products .

4.2 Inventories Products

4.2.1 Static Collateral Credit

This is movable and title collateral loan business in the most basic of financial products , it refers to its own customers or third person is the legal owner of the real estate collateral in credit operations. Bank commissioned a third-party logistics companies to provide customers with the implementation of regulatory collateral , and the collateral are not allowed to barter , the customer must first enter the bank money to redeem goods. Static collateral credit applies only to stock as appropriate collateral , and its way of buying and selling bulk purchases , sales trading graded based customers . For customers, this product is the cargo charge of business requirements are more demanding one. With this product , customers can be had in the inventory backlog of funds to revitalize and expand the scale of operation . The risks faced by banks mainly in: Collateral market capacity and liquidity, equity and price volatility and other goods .

4.2.2 Dynamic Collateral Credit

This product is based on a static extension of credit collateral development , different banks for customer collateral value of the goods set a minimum limit , the limit allowed more goods out of the library , which customers can within a certain range barter . This product is suitable for stable inventory , goods category is more consistent and easier collateral value was measured by customers. For customers, because you can barter operation, it pledged to set limits for customers who have stable inventory less affected production and business activities , as long as the limits set reasonable, customers can redeem at almost no additional margin on the basis of goods , to a greater extent revitalize inventory. For the banks , although the effect of the product is small margin , but operating costs than static collateral credit has decreased significantly since the operation by a professional third-party logistics companies . The main risks faced by banks include: the introduction of barter unsalable products , price volatility adjustment under the limit.

4.2.3 Standard Loans Secured Warehouse

Standard loans secured warehouse refers customers to its own or third-party standard warehouse receipt for the pledge of legally owned credit business . The so-called standard warehouse receipts which are consistent with the requirements of the Exchange unified by the designated delivery warehouse storage of goods in the completion and acceptance , confirmation pass issued to the owner of the goods for the extraction and standardization of delivery certificates registered by the Exchange effective .For customers, relatively movable collateral , standard warehouse receipt pledge is simple, low cost. For the banks , the cost and risks are reduced. In addition , due to the highly mobile standard warehouse receipt , which will also help banks deal with the collateral in case of default by the customer .

4.2.4 Ordinary Loans Secured Warehouse

Ordinary loans secured warehouse loans secured with standard warehouse receipt broadly similar process , except that the non- delivery futures ordinary warehouse warehouse credit use. The main risks are: the pledge of warehouse receipts can be normative and liquidity.

4.3 Prepayments Products

4.3.1 After the First Shipment Credit

This means that customers want the product (s) to obtain credit from banks to pay a certain percentage of the margin under the premise of the bank to pay the full purchase price to the seller ; seller sends the goods in accordance with the agreement of purchase and sale contracts or agreements , set after the goods arrive collateral , as bank credit guarantees. This product is suitable for operating businesses selling products , because these enterprises are mainly concentrated in demand for funds advances in the field . In addition, in support of bank funds can be carried out under the bulk purchases , and then strive for greater discounts. For the banks , we can use trade chain, will continue to extend the business . Another benefit is that the goods to the customer directly from the seller , so the ownership of the goods is more specific than inventory financing . The main risks are: Upstream customer delivery, refund and repurchase ability to perform , risk prevention and loss in transit of responsibility, such as the transfer of storage .

4.3.2 Credit Guarantee Delivery

This product is a variant of the cash credit line of goods , means customers pay a deposit under the premise of Silver 7

OK lend the full purchase price for customers purchasing a full bill of lading issued by the Seller as a credit guarantee. Subsequently , sub-sub- margin customers to the bank , the bank then fractionated notify seller to customer shipments . This is also called "seller guarantees the buyer a credit model". The product resulting trade background : Customers bulk purchases , once payment pursuit of commercial discounts , and manufacturers can not be a one-time offer due to scheduling ; season play money , season sales. For customers, the bulk purchase price discount can be obtained , and the " off-season play money , season sales," help to reduce future price fluctuations of wind . And because the goods in the upstream , which also reduces the regulatory and storage costs. The seller can receive large sums of advance payment to ease liquidity bottlenecks. For the banks , the seller can be combined and logistics regulatory simplify risk control .

4.3.3 Import Letters of Credit under the Credit Pledged Goods Coming Right

The product is based on the bank 's application for an importer , the importer pay a certain percentage of the margin after its opening letters of credit and goods right through the control of documents under the letter of credit on behalf of the ways to control the sources of repayment of a loan . The product is applicable to imported commodities , and the need to expand the financial leverage effect , reduce the cost of importing enterprise security. For customers, you can use a small margin to expand the scale of a single purchase in order to obtain trade discounts ; For the banks , because the right to control the goods , so the risk is not significantly increased.

4.4 Accounts Receivable Products

4.4.1 Domestic Factoring

Factoring is the customer (Seller) to obtain funds , his pledge of accounts receivable as one way of financing. Factoring Factoring into clear and dark factoring , the difference between the two lies in the transfer of receivables by the buyer whether to notify the buyer to confirm. Factoring applicable to accounts receivable financing needs and want to optimize the reporting requirements of the vendor companies. In a very natural and there is a higher way to protect their business continues to expand . Relative to the Ming factoring, factoring dark to simplify some procedures , but it also brings certain risks.

4.4.2 Domestic factoring financing pool , the pool of credit and export bills receivable financing pool

These three products have in common is that the small-scale,decentralized receivables converging to the "pool " to achieve economies of scale and reduce risk.

4.4.3 Export Credit Insurance Credit

The products that have been insured export credit insurance customers will indemnify the bank's equity as collateral to obtain funds to support the banks , when the occurrence of a covered loss , the insurance company under the relevant provisions , the amount of compensation will be paid directly to the financing Bank. And other financing products the biggest difference is that this product will be included in an insurance company financing system, while at the same time the insurance company to operate its own business , in fact, will also assume the risk of banks . The risk that products that: Pay attention to the impact of the credit recovery deductible amount may be brought ; transfer agreement in the claims , the insurance company claims should be agreed in the policy area of responsibility paid directly to the credit banks.

Third, the difference between domestic and international supply chain finance

5. DIFFERENCE BETWEEN BUSINESS MODEL

International Business Development Bank of supply chain finance most direct and conventional starting point is the core business , while domestic contrary, supply chain finance business began to charge the goods on behalf of the credit business for SMEs to finance self-liquidating trade .For international banks, letters of credit and documentary collection is a supplier settlement means used in the past , but because of the way these procedures are complex , time-consuming and costly , making bank credit gradually popular traditional trade finance products lose market. Customers from supply chain members dispersed financing cash flow difficulties caused by the economic and financial no discrete node supply chain members to make a positive response, international banks together with the core enterprise supply chain financing solutions provide a way to regain customers the new model relationship management , retain existing customers live , but also to cultivate customers in emerging markets and extension services.For most domestic banks, despite the " 1" as an effective risk control variable and the value of the business was gradually discovered a breakthrough , but " 1 " is still a means of marketing intermediaries , target customers still point to "N".

5.1 Difference Financing Products

Supply chain financing international banks to " accounts receivable financing" for orders, invoices and other data streams publicity and assurance , to provide financing for a number of aspects of the application and approval for the supply chain members and banks as keywords , via electronic platforms button. Supply chain financing of domestic banks by the " inventory financing " as key words, through the introduction of the core business of credit as well as the introduction of third-party logistics supervision to some extent , to provide financing for the supply chain members.

5.2 Financing the difference between objects

International Bank of supply chain finance mainly for the core business of upstream suppliers , mainly because of the international banks to provide accounts receivable financing . Core businesses upstream suppliers to accounts receivable to the bank for financing , because the debtor is the core business, the risk of default is low, and with respect to inventory financing , accounts receivable management costs low , this type of bank loan financing more while the distributors' inventory financing and advance financing mostly built on one to one basis , systematic fledgling distributor financing arrangements . Domestic situation on the contrary , most concentrated in the downstream supply chain , namely the scope of " distribution chain finance" or "channel financing" , because the interests of the density of the core businesses and often exceeds the downstream relationships with upstream interests.

5.3 Application level information technology gap

From the international practice, third-party e-commerce platform often become participants in the supply chain finance . Within the supply chain in order to reduce transaction costs for the original purpose of the e-commerce platform , due to enhanced visibility and publicity transaction information flow , as banks and other financial institutions offer a range of financial services to intervene point. Domestic enterprises , logistics, inconsistent Bank IT technology application level , resulting currently no docking information flow supply chain finance desired , the logistics , capital flow and business flow , presenting technical island phenomenon for different enterprises independently discovered to build a data stream to each other in public supply chain financial services platform to be improved.

5.4 Legal and institutional differences

Secured Transaction Law and the relevant set of legal and institutional protection : In recent years , foreign government organizations have developed a Secured Transactions Model Law is designed to help its members to develop a modern and efficient system of real estate secured transactions laws . Domestic , " 2005 global business environment report" shows that the support of the legal and institutional credit markets , China was named one of the worst 20% of the country in relation to the Secured Transaction Law blur , poor operability. Relevant laws and regulations to achieve the Secured Transaction Law : supply chain finance, banking services, the judicial system needs a major presence in the case against the defaulting customer collateral to achieve efficiency , accounts receivable and other collateral. International Secured Transactions realization of the rights of its high speed and low cost characteristics , complex and time-consuming domestic judicial process to achieve Secured Transaction Law so slow and expensive. Fourth, in the domestic supply chain finance universal reason fails. Supply chain finance is the bank for the financing of SMEs in the supply chain to solve the difficult problem , focus on core businesses in the supply chain , collaboration with third-party logistics companies , the risk becomes uncontrollable grasp a single enterprise for the whole supply chain of controlled risk , provision of finance, billing, insurance, and other businesses a financial services for SMEs. In other countries, especially the United States , the development of supply chain finance has been quite a long time , the level has reached a certain height . However , the supply chain in China is still in its infancy , and why supply chain finance is not as fully developed to the United States ? A complete financial market is composed of several parts: supply and demand sides of funds , financial markets, financial products , infrastructure, and laws and regulations. We believe that supply chain finance in the country is no reason why the popular thinking can come from several areas.

6. CONCLUSION

1. **Supply and demand factors**: SME financing has been one of the bottlenecks in China's economic development , a large number of SMEs in the supply chain itself in a weak position , cash flow is not smooth in the event of economic crisis or the government tightening , reduce the money supply , SME financing is worse. Therefore , we believe that the needs of SMEs for financing large, demand is not a problem , the problem lies in the supply side . China's commercial banks accounted for 53.7 percent of state-owned financial institutions in total assets , which is state-owned commercial banks control 53.7 % of the loan money goes . On the one hand , the presence of these banks ' big customers prefer " more inclined to large state-owned enterprise loans, these companies have government backing, default risk is very small. On the other hand , these banks are reluctant to take risks of financial innovation , competitive differentiation not provide the same types of products , stick to the price competition, low-level connections competing ecosystem . Therefore, the lack of supply is one of the development restrictions in the domestic supply chain finance .

2. **Awareness of enterprise supply chain management is relatively weak**. In fact,China's enterprises in the context of globalization of production has long become part of the supply chain, the division of labor gradually refined , from the vertical integration of production. However, in the sense of the degree of attention for our enterprise supply chain management is not high enough , still only concerned about their own individual enterprise management. We believe that this has a certain relationship with our economic system . Our free- market economic system is not perfect, most of the core business in the supply chain is still state-owned , these SOEs lack of competition , lack of sense of urgency to improve the efficiency of supply chain management awareness is also inadequate. The core enterprise supply chain finance needs the participation and cooperation. Without the support of the core business , for risk control also a problem for SMEs , will lead to supply chain finance in the country did not pop up.

3. **Third-party logistics companies can not give good support**. The need for cooperation in the supply chain finance banks and third-party logistics companies , to make up for deficiencies in their own areas of expertise , reducing information asymmetry problem. Especially in inventory financing , third-party logistics companies play a regulatory collateral , the task of monitoring the logistics activities in support of the bank's business development , help banks effectively control the risk. In China, the third party logistics enterprises lack awareness in this regard , cooperation with banks also just stay in the warehouse level, no more deeply involved in the supply chain finance business to go , to support the bank in a professional field .

4. **Development of domestic financial IT and e-commerce is lagging behind**.High operational costs of supply chain finance , and the application of information technology to reduce such costs. Currently, confirmation documents, transfer files, the account , redeem the goods , accounts receivable is the most labor -intensive part , but also on supply chain finance business economics largest part of the damage,but also an additional source of risk. Meanwhile , e-commerce will help to enhance the Visibility trade background , reduce transaction costs. Due to lack of development of information technology, can not effectively reduce the cost , which is an important factor in supply chain finance is no popular .

5. **Laws and related regulations are inadequate, not in the system to support supply chain finance this business**. For example , the relevant domestic law Secured Transaction Law is still inadequate, resulting in supply chain finance business uncertainty in many areas of operation and expected loss . Meanwhile, the regulatory authorities for supply chain finance is still largely remain in the traditional understanding of liquidity credit level , the core value of the supply chain finance limited understanding of the relevant norms, guidance, supervision is still a lack of work .