

Purchase Order Finance

So you are interested in Trade finance but you're not exactly sure what it is or how it works.

Purchase Order finance is funding to your suppliers. *It is where your product is drop shipped direct from your manufacturer to your customer or via a third party logistics provider.*

Why would you need Purchase Order Finance?

Let's say you're an SME, with lots of small clients. You have potential to grow from a small to medium sized business by taking on larger orders with one or more of the big players - yet you don't have the capital to take on the order. You know you can make the money you just need to fulfill the order first. Your supplier demands payment before producing the goods. With Purchase Order finance we can help you capitalise on the opportunity and catapult yourself into massive growth.

What types of businesses do we finance?

Always wholesalers, producing a finished product which is third party manufactured. E.g. Electrical and beverage wholesalers.

Who don't we finance to?

Retailers that sell direct to consumers.

We provide funding to wholesalers, producing a finished product which is third party manufactured

You can accept large orders, growing your company since you have the money to look after wages, materials, etc

What are the benefits?

- It is a no-debt finance solution which funds your business from its own purchase orders
- You don't have to go through a bank loan application and the possibility of rejection
- Purchase Order finance gives you cash savings that you can use
- You no longer have to refuse orders just because you don't have the funds to take care of the operating costs
- You can accept large orders, growing your company since you can keep working capital aside to look after wages, materials, etc
- You don't have to worry about collections, since the Purchase Order finance company takes care of it
- Your credit standing does not matter; instead, your customer's creditworthiness is more important

How does Purchase Order Finance work?

Purchase Order Finance is easy to use. The work flow can be summarised as follows



So what's required of you?

Some of the following points require detailed research from your end, but are an absolute necessity for the deal to go ahead.

Can you demonstrate experience in this type of exchange?

- Copy of purchase order (quantity, delivery date, price)
- Supplier agreement (terms on which bind you and your customers to the order)
- Identify who your manufacturer is. What kind of quality control processes have you put in place to ensure that the specifications of the PO are being met? Have you considered and allowed enough time to meet your customer's deadline?
- Funding reports detailing associated costs such as stamp duty, freight and manufacturing costs etc
- Warranties - Looking at warranties in place for the goods. Is the manufacturer covering the warranty?
- Do you have enough profit margin? (More than 30% is our preference).
- Can you demonstrate experience in this type of exchange? – As this is a very detailed, specialised and risky exchange, experience in buying from overseas suppliers is vital.
- Foreign Exchange Risk – have you considered if you order fails inspection or to achieve delivery date? What if it gets cancelled? How is this risk covered?
- Factory review (see below for more detail).

What is involved with a typical factory review?

* Information sourced from China Blue print www.chinablueprint.com.au

A factory review is imperative before locking in an order, in the long run it can save you time, money, disappointment and avoid potential disaster.

A typical review includes a full examination of the factory's corporate documentation, their assembly and machinery, their quality control processes and their financial information.

Why is a factory audit necessary?

When selecting a supplier, you need accurate information to help determine their suitability. Some factories are notorious for poor quality, unfair working conditions, child labour and environmental degradation, so it's up to you to know this information prior to entering into any business agreement. A Factory Audit includes the following important information;

- A review of the factory's formal business documents; business registration, exporting license, testing certifications, accounting documents;
- A report on the factories operational structure; systems in place, employee breakdown, machinery types, recording processes, quality assurance and systems related certificates, inspection track record;

Some factories are notorious for poor quality, unfair working conditions, child labour and environmental degradation, so it's up to you to know this information prior to entering into any business agreement.

- Photographic representations: factory entrance, factory production line, machinery, administrative offices, business documents, storage facilities, packing rooms, sampling rooms;
- Charts: factory organizational flow chart, production work flow chart;
- Production information; production line/capacity calculations, daily output checks, information of sensitive points/bottle necks, machinery condition, power supply, transportation;
- Raw materials; supplier and sub-supplier details;
- Sampling; details of sampling capacity; and
- Any client special requests.

What happens next?

A lot of clients are in the habit of paying deposits for products being manufactured. ARTF won't do this.

- Once we have the Purchase order and all above requirements from your end have been met we draft a Letter of credit and confirm the manufacturer is happy with the terms set. (A standard, commercial **letter of credit** (LC) is a document issued mostly by a financial institution, used primarily in trade finance, which usually provides an irrevocable payment undertaking **sourced from Wikipedia*)
- Once manufacturer signs off, we issue LC.
N.B a lot of clients are in the habit of paying deposits for products being manufactured. We won't do this. The main reason for this is risk management. If goods are faulty or can't be produced on time or perhaps the factory burns down, you will lose your deposit. That's why we issue an LC. It helps protect us and it helps protect you.

The products have to go direct from manufacturer; using ARTFs approved shipping and customer agents direct to the end

- Once production begins and goods are made, we send in an auditor to check and inspect the goods to see they match the order. If approved we do a loading inspection to check the goods aren't damaged and they are actually going into the container. This increases the likelihood that goods are accepted once they hit Australian shores. E.g. If you don't have a loading inspector some of the boxes might not be loaded into container or damaged product ignored.
- The products have to go direct from manufacturer using ARTFs shipping and customer agents direct to the end customer. One order for one customer is our preferred delivery situation. Third party logistics is contracted if product needs to go to multiple destinations.
- Once product is delivered the client raises an invoice to the customer within 24 hours of delivery, at the same time sending ARTF a copy of the invoice. From there we will begin the Invoice Finance facility. **N.B** Because we have taken on the purchase order as collateral, the actual invoice is where we get compensated for that. You can't have Trade Finance without Invoice Finance; there is no way to secure the order without the invoice.

Purchase Order Finance Case Study

We have helped a lot of clients with a trade finance facility. See below a case study.

PRODUCT: \$500,000 COMBINED DEBTOR AND PURCHASE ORDER FACILITY

Background: Client is a well established electrical wholesaler. Their products are imported from China. A purchase order to supply one of the larger retailers within Australia has been won. Taking advantage of this opportunity will result in a dramatic transformation of the client's business.

Problem: Suppliers demand payment upon shipping. Local customers won't pay until 60 days after delivery. These large orders therefore require a substantial working capital investment. This cash flow crunch results in a net short fall in working capital.

AR SOLUTION: CLIENT WAS OFFERED DEBTOR FINANCE. THIS WAS USED TO FINANCE HIS EXISTING CUSTOMERS. A PURCHASE ORDER FACILITY WAS ALSO PUT IN PLACE. THIS WAS USED TO PAY HIS SUPPLIERS UPON SHIPPING. THE RESULT: A MASSIVE INCREASE IN THE CLIENT'S TURNOVER AND BOTTOM LINE PROFIT.

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Purchase Order finance check list

So now you know more about Purchase Order Finance. If you think you want to go ahead with a facility make sure you have the following items before proceeding.

- Copy of Purchase order**
- Supplier agreement**
- Enough margin to make at least 30% profit**
- Experience in dealing with the type of exchange**
- Detailed factory review**

To talk to a product specialist and book in an appointment please call the office on 1300 652 158.

For more information visit our website and check out our latest video at www.arcashflow.com.au/videos

