Global Supply Chains and Working Capital

Ensuring resilience to enable recovery

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HSBC

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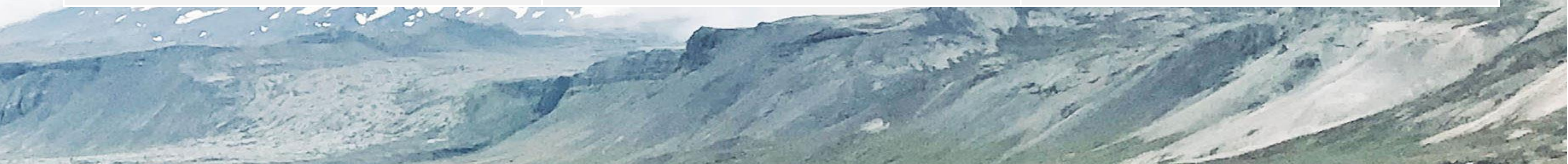
Taking stock of the treasury function post COVID-19

Having dealt with the "survival" aspect of COVID-19, a number of firms are now moving ahead with more strategic topics. While resiliency is still key, Treasurers should be continue to be mindful of the opportunities that exist when markets begin to open again[1]. Even in the face of economic strife, as treasury teams seek to assess liquidity, risk capacity and operational flexibility, the potential to unlock synergies increases.

Operational Flexibility	Exposure	Treasury Setup
▪ Ensure sufficient cash levels and credit lines ▪ Substitute and localise / regionalise parts of the supply chain as needed (i.e. shift from "just in time" to "just in case") ▪ Consider the time needed for adjustment ▪ Review any capex requirements that need to be transitioned	▪ Gauge ability to recover lost revenues when the outbreak ebbs ▪ Manage ongoing need to service customers (and for customers to purchase goods / services) ▪ Review sales model, potentially increasing e-commerce / direct sales (considering new methods of collection) ▪ Reconsider reliance on any unfinished goods sourced abroad	▪ Accelerate and automate treasury functions through digitisation, while ensuring systems offer real-time, global information / payment execution ▪ Deploy a centralised liquidity and risk management framework ▪ Leverage treasury hubs in key regional markets ▪ Review risk management guidelines for FX, commodities and rates



1. HSBC: Mitigating the corporate impact of the Covid-19 pandemic (May 2020)

Optimising working capital post-COVID blends operational efficiencies and financial tools, enhancing cash flows and reducing costs

Operational Efficiencies

People | Policy | Process | Systems

Purchase to Pay

- Regional, localised suppliers
- Much greater focus on financial stability of key suppliers – large & small
- Injecting liquidity into supply chain tiers
- Digitising PTP process

Forecast to Fulfil

- Building supply chain resilience
- Near-shoring production
- Low-tier supplier focus
- SKU rationalisation
- Re-tasking production lines
- Postponing final assembly

Order to Cash

- Enhanced credit risk mitigation
- Payment terms extension to facilitate sales
- Digitise OTC process
- Re-energised, targeted collections & dispute resolution

Cash & Liquidity

- Accelerating digital solutions
- Centralising liquidity, control, risk management
- Cash flow forecasting
- Investment strategies
- Funding structure (e.g. In-House Bank)

Financial Tools

Trade | Payment | Liquidity | Risk

Purchase to Pay

- Accelerate supplier on boarding to Supply Chain Finance (SCF) programs
- Sustainable SCF
- Pre-shipment Finance
- Virtual Purchasing Cards
- Documentary credits
- Guarantees and bonds
- Transactional FX solutions

Forecast to Fulfil

- Asset-based finance
- Commodity finance
- Pre-shipment finance
- Tokenisation

Order to Cash

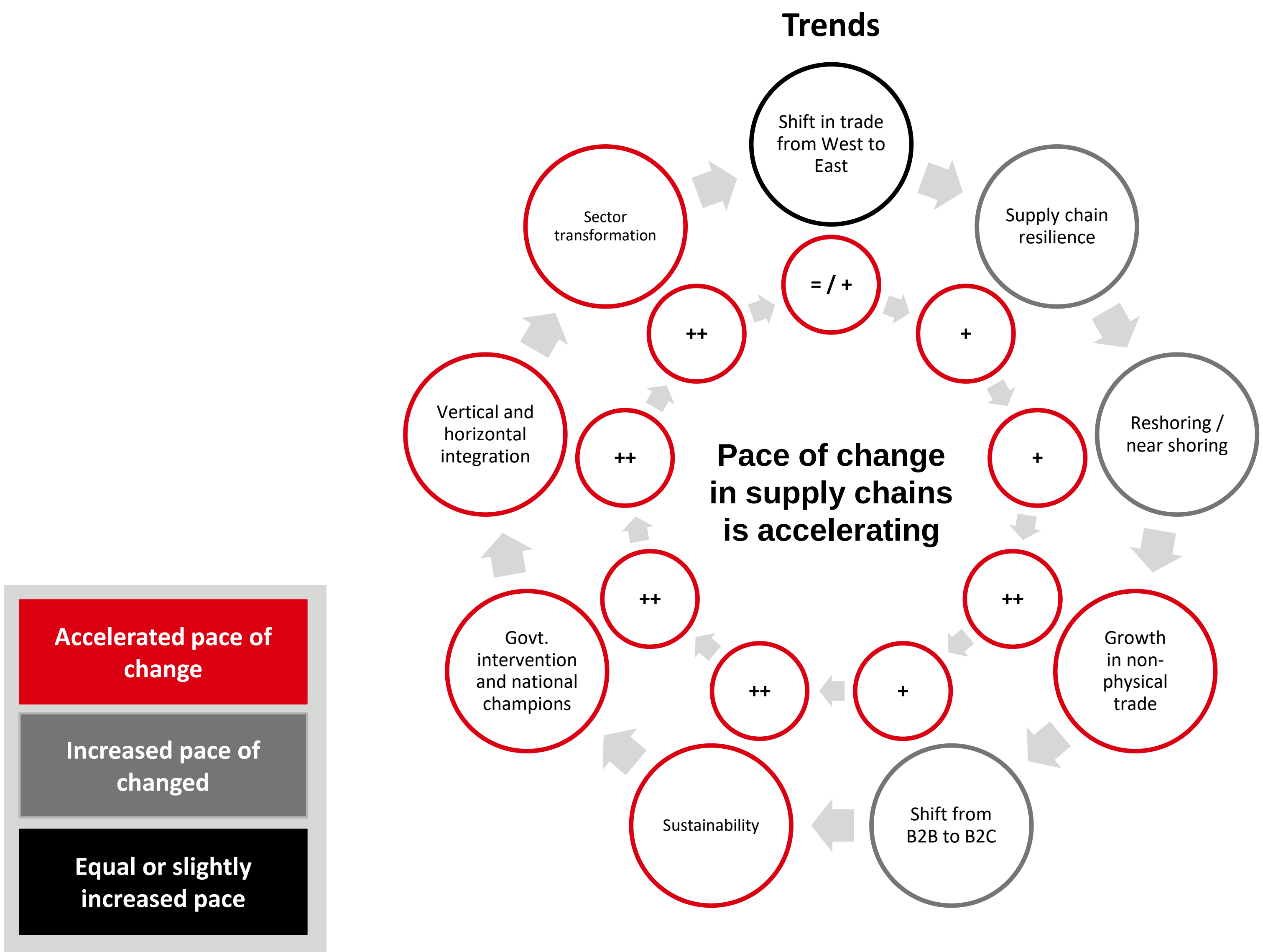
- Receivables finance – to enable terms extension, accelerate cash flow and mitigate credit risk
- Documentary credits
- Forfaiting

Cash & Liquidity

- Mobile Collections
- Real-time payments
- Cross-currency / cross-bank pooling
- SWIFT GPI tracking
- Interest enhancement and liquidity solutions
- Virtual accounts
- Settlement and cashflow database (via DLT)

Source: HSBC analysis

Trends and anticipated shifts in supply chains[1]



1. HSBC: Mitigating the corporate impact of the Covid-19 pandemic (May 2020)

Trends and anticipated shifts in supply chains[1]

Trend	Pace	Drivers	Considerations
1. Shift of trade from West to East	=/ +	• Middle Income population growth in Asia • Growth in intra-Asian trade; RCEP, ASEAN, CPTPP • ***New***: higher impact of Covid in Europe, US compared to Asia	• Growth in imports/ domestic trade of high value added products in developing markets
2. Supply chain resilience	+	• Focus on diversification, agility and transparency of supply chains, avoiding single point of failure; data analytics as key enabler • Geo-political tensions between US and China; • Partial decoupling from China; "China+" strategy	• Higher risk and revenue mitigation needs (e.g. documentary trade and related financing) • Capex/ investment in ASEAN, India, Africa • Higher working capital requirements; built-in buffers, higher inventory
3. Reshoring/ near-shoring	+	• Production coming closer to point of sale, aided by automation and new technologies, such as 3D printing; • Protectionism; push for re-shoring and domestic sourcing • Shift from "low labour cost" hubs to "skilled labour/ specialised" hubs	• Working capital implications from high inventory levels and higher operating costs; • Reduction in trade of intermediate products • Shorter supply chains; domestic trade growth
4. Growth in non-physical trade	++	• Increased pace of digitisation, eCommerce, IOT, cloud-based services; • Shift from physical to digital	• Continued expansion in Tech & Telecom space (e.g. 5G); extension of payment terms as sales tool (e.g. tech licensing, cloud computing services)
5. Shift from B2B to B2C	+	• Change in consumer buying behaviours, accelerated during lockdown • Growing importance and protection of brands and client experience • Networked and digitally connected supply chains • Transparency leading to reduction of intermediaries in value chains	• Place less reliance on retailers and distributors by making use of third party marketplace platforms and developing subscription services

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Trends and anticipated shifts in supply chains[1]

Trend	Pace	Drivers	Considerations
6. Sustainability	++	• Consumer preference for more environmentally sustainable goods and for companies/ brands with clear purpose and a social contract • Relevance of ESG across businesses' broader stakeholder base, leading to more balanced operating models; e.g. lighter carbon footprint • ***New***: renewed ESG focus driven by increased role of Government I	• Supply chain reconfiguration and the ability to tap into sustainable financing solutions; e.g. green bonds, green loans, supply chain finance • Working capital implications from higher operating costs (e.g. Wage increases, green standards)
7. Government intervention and national champions	++	• Focus on self-sufficiency in areas of critical goods and services • Protection of strategically important sectors • ***New***: Increased role of government, given bail-outs/ businesses operating backed with public money	• Export/ investment curbs in certain sectors • Working capital implications: tariffs, self-sufficient operations, high inventory
8. Vertical and horizontal integration	++	• Significant restructurings; weaker companies going out of business • Consumer and company preference for larger/ safer suppliers • Vertical integration as companies look for self-sufficient supply chains	• M&A activity • Change in working capital needs from emergence of intra-Group Supply Chains
9. Sector transformation	++	• Some sectors will fade in prominence (e.g. real estate, retail, travel & tourism, hospitality), with economic models transformed • Emergence of new sectors and business models	• Darwinian principles applied creating new opportunities for the fit and agile

1. HSBC: Mitigating the corporate impact of the Covid-19 pandemic (May 2020)

Post COVID-19 Megatrends

	Leading indicators	Enablers	Examples
1 **Building supply chain resilience**	▪ **Decoupling / Diversification**: reduce supply concentration and form new partners ▪ **Deep tier suppliers**: more focus on previously **"**invisible" lower-tier suppliers that cause disruption – transparency, finance, sustainable sourcing ▪ **Vertical integration:** forward / backward acquisition to be more self-sufficient – natural selection; there will be bargains to be had	▪ **Data**: providing supply and inventory visibility ▪ **AI for decision support**: real-time forecast of variable supply/demand/cashflow; digital controls tower; accelerated decision making ▪ **3D print** (replacing imported parts)**; virtual inspection systems** (replacing onsite checks) ▪ Transactional data enabled **working capital finance**, integrating pre- to post-shipment	▪ Establishing parallel supply chains mirroring the IT industry's disaster and recovery plans – i.e. redundant suppliers, engaging factories in different countries that make some of the same parts/components ▪ Efforts such as IBM Food Trust to access deep tier suppliers ▪ UK health service supply chain mapping
2 **Interplay of protectionism vs. market openness**	▪ **Reclaiming certain parts of supply chains:** re-shore / near-shore production, intra region / domestic sourcing / manufacturing, shorter supply chains ▪ **Protectionist policies**: export controls on critical goods, punitive tariffs, regulatory barriers ▪ **Exporting tech innovation**: geographic concentration of R&D spend in science/tech sectors; diffusion requires open export markets	▪ **New tech** e.g. automation, robotics, and 3D printing in manufacturing process ▪ **Policy-making**: protectionist / nationalist measures build up trade tension; bilateral / multilateral trade deals liberalise trade ▪ **Market openness** + **IP protection**: access to import/export markets for tech-intensive products	▪ **US-China Phase One trade deal** in progress: e.g. tariff cuts / exclusions, non-tariff barriers removal ▪ **COVID-19 implications** e.g. US temporary deferred tariffs / exemptions for certain importers or products

1. Source: HSBC analysis

Post COVID-19 Megatrends

	Leading indicators	Enablers	Examples
3 **Ever closer to customers**	▪ **Shifting away from distributors**: B2B or D2C sales via own online channels and/or e-commerce marketplaces; online-to-offline delivery ▪ **Diversifying / enhancing** sales/export markets by directly served customer base, data ownership ▪ **Servitisation**: towards use- / output-oriented sales; from ownership economy to experience economy	▪ **Digital tools** replacing distributors to manage long tail B2B customers, AR / credit process, customer data ▪ 'Just-in-time' access to equipment and integrated services, enhancing customer relationships	▪ Global technology vendors are cutting out distributors with direct sales through online platforms ▪ Healthcare / industrial equipment manufacturers evolve towards servitised business models
4 **Accelerated digital connectivity**	▪ **Digital services** prevail – remote healthcare, streaming, entertainment, virtual assistance, cloud services, digital banking, digitised trade ▪ **Increased demand** for connectivity – e-penetration breaking down physical barriers to global trade	▪ Fast tracked **innovation** during crisis times: medical research, digital collaboration tools, home office setups, internet / cloud capacity ▪ Massive **data flows** providing new global trade (and finance) routes	▪ Heightened cloud demand: Microsoft, Amazon, Alibaba, Google ▪ Increased e-penetration within HSBC – significant increase in uptake of HSBCnet (hit YE targets in Q1)

1. Source: HSBC analysis

Modelling the Future

1 Building supply chain resilience

Leading indicators

- **Decoupling / Diversification**: reduce supply concentration and form new partners
- **Deep tier suppliers**: more focus on previously **"**invisible" lower-tier suppliers that cause disruption – transparency, finance, sustainable sourcing
- **Vertical integration:** forward / backward acquisition to be more self-sufficient – natural selection; there will be bargains to be had

Impact/Implications

- Need for risk mitigation in newly formed trading relationships
- Increasing need for liquidity into lower tiers
- Increasing focus on supply chain transparency / visibility, responsible sourcing
- Corporates' increasing ownership of critical suppliers / self-sufficient supply chains

Our Response

- Assist in more supply chain financing across trade cycles (pre-to-post), multiple tiers, and cross borders
- Enhance product capability e.g. pre-invoice approval / pre-shipment finance / contract monetisation
- Collaborate for stronger capacity: fintechs, Multilaterals (EM suppliers), TCI (appetite)
- Technology for transparency: data / document flows, logistics flows, finance flows, DLT

2 Interplay of protectionism vs. market openness

Leading indicators

- **Reclaiming certain parts of supply chains:** re-shore / near-shore production, intra region/domestic sourcing / manufacturing, shorter supply chains
- **Protectionist policies**: export controls on critical goods, punitive tariffs, regulatory barriers
- **Exporting tech innovation**: geographic concentration of R&D spend in science/tech sectors; diffusion requires open export markets

Impact/Implications

- Restrictions on / lack of trust in cross-border trade of critical goods
- Redundancy of manufacturing plants / suppliers across regions
- Increased working capital needs from increased operations and inventory
- Sustained high-tech sourcing and exports; export/investment curbs in certain sectors

Our Response

- Intermediate cross-border trade to mitigate risks / build trust for both sides
- Assist newly outsourced activities by structured working capital finance e.g. trade loans
- Support exports in concentrated science/tech sectors e.g. pharma, chemicals, computers / electronics, electrical equipment, motor vehicles

1. Source: HSBC analysis

Modelling the Future

	Leading indicators	Impact/Implications	Our Response
3 **Ever closer to customers**	▪ **Shifting away from distributors**: B2B or D2C sales via own online channels and/or e-commerce marketplaces; online-to-offline delivery ▪ **Diversifying / enhancing** sales/export markets by directly served customer base, data ownership ▪ **Servitisation**: towards use- / output-oriented sales; from ownership economy to experience economy	▪ Challenges in managing AR / debt collection for long tail (B2B) customers ▪ Further outsourcing / BPO (e.g. research, packaging, AR/AP) for scalable capacity	▪ Point of Sale solutions ▪ Engage with fintechs for direct access to lower value customers ▪ Potential to embed direct access to working capital solutions in client ecosystems e.g. marketplaces, ERPs, AP/ AR/ treasury systems
4 **Accelerated digital connectivity**	▪ **Digital services** prevail – remote healthcare, streaming, entertainment, virtual assistance, cloud services, digital banking, digitised trade ▪ **Increased demand** for connectivity – e-penetration breaking down physical barriers to global trade	▪ Shift in flows from physical to digital / digitally-enabled physical – **increased volume** due to ease of processing ▪ Data flows (audit trails) generating new value	▪ Enhanced focus on capturing services trade / digital flows ▪ Utilising transaction data flows to enable new offerings, risk mitigation (e.g. fraud, performance) ▪ Increased push for e-penetration – new target of 75% by year-end

1. Source: HSBC analysis

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