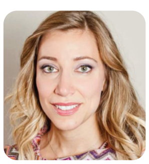
Trade Working Capital Viewpoints

January 2024

Using Structured Accounts Receivable Finance as a Dynamic Funding Source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Working Capital in an Evolving Environment

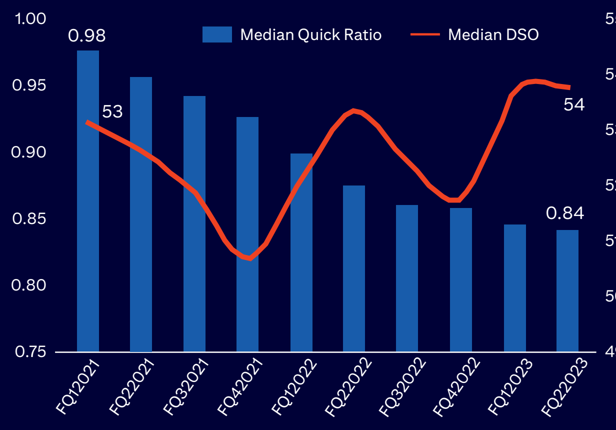
Corporates have faced extraordinary margin pressure over the last two years as geopolitical conflict and hawkish monetary policy among other reasons have contributed to a costly funding climate. Treasurers are largely focused on minimizing the effects of the increased financing costs experienced up and down the supply chain. Despite reported falling inflation in many western economies, it is very much a "wait and see" moment as to when interest rates will retreat from their historic levels.[1]

The time frame for a return to lower interest rates is still unclear. At their September meeting, the Federal Reserve officials opted to hold steady at 5.25% – 5.50%, while Chairman Powell reiterated the Fed's commitment to a 2% inflation target, leaving the door open for further increase(s).[2] Moreover, at their September meeting the Bank of England voted by a slim majority to hit pause on their own hiking cycle whilst maintaining guidance that further hikes could be necessary if persistent inflationary pressure warrants it.[3]

The effects of high costs of funds have had impact on all areas of business. Median quick ratio for S&P Global 1200 constituents has decreased steadily to 0.84 for the previous nine fiscal quarters underpinning the effects that the current environment has had on corporates' liquidity. Days Sales Outstanding has ticked higher to 54 days after having decreased to 51 days in FQ4 2021 (see Figure 1 below). With the demand for liquidity at record highs, customers are largely focused on extending payment terms in an effort to conserve cash.

[1] Citi Velocity, US Economics: FOMC Minutes – Fine-tuning a very dovish meeting, 2024
[2] Citi Velocity, US Economics: FOMC – "Dots" Signal Higher-for Longer Policy Rates, 2023
[3] Citi Velocity, European Rates Weekly: Not the time to flip bearish, 2023

Figure 1. Median Quick Ratio, Median Days Sales Outstanding (Right Side), for S&P Global 1200 Constituents



Source: S&P Capital IQ, Citibank

Figure 2. Objectives of Portfolio Accounts Receivable Securitization

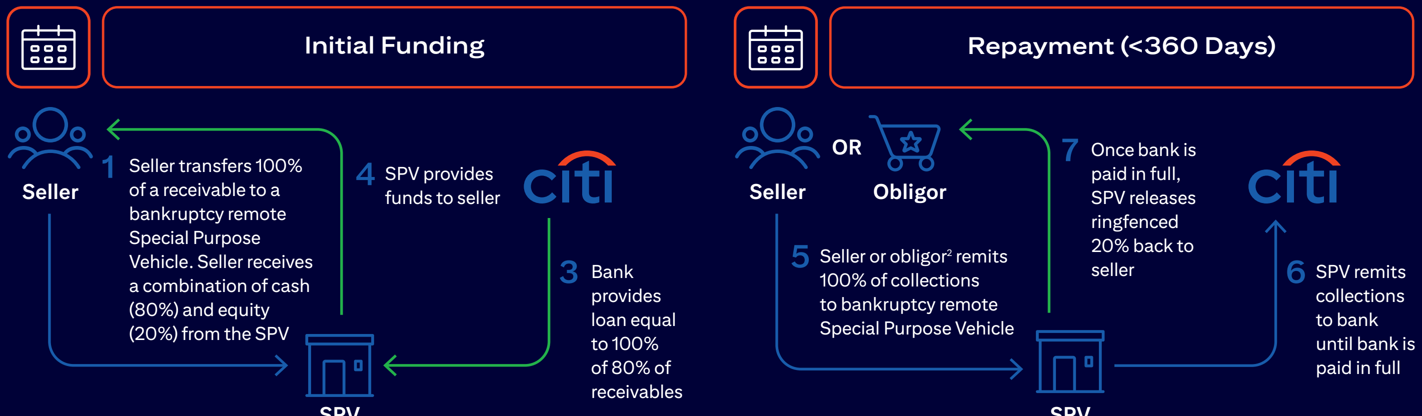
Source: Citibank

Navigating the current environment requires adept working capital management while prioritizing efficient funding sources that are aimed to help organizations be opportunistic and strategic. Treasurers have utilized accounts receivable financing structures to support the organization's various customers. At a time when funding costs and pricing are chief concerns, treasurers and CFOs may want to consider how a Portfolio Accounts Receivable Securitization structure could be beneficial for their organization.

How Citi Can Help Attain Efficient Liquidity While Supporting Sales

Amid varied economic conditions and with the high cost of funds, accessing liquidity at the most cost-effective rate possible while continuing to support customers need for flexible payment terms has become top priority for sellers. Sellers focused on pricing with a diversified customer base can utilize a Portfolio Accounts Receivable Securitization structure to inject liquidity into sales distribution channels while managing DSO. As an example, a large multinational foods corporation utilizes an AR securitization facility in addition to their commercial paper program to optimize their liquidity. This corporate was primarily motivated to use an AR securitization facilitation to access liquidity and reduce DSO because of its low cost. Additionally, the AR securitization facility may potentially offer the corporate an additional source of liquidity. Citi may require corporates disclose or consult with their auditors or professional advisors on the potential benefits of the program structure, accounting treatment and documentation. For corporates in many industries, accounts receivable securitization can be a powerful working capital optimization tool that aims to help reduce DSO while simultaneously helping corporates meet their customers' demands for longer payment terms.

Figure 3. Example of Portfolio Accounts Receivable Securitization Flow



[1] Amount retained as collateral varies and it's based on receivables' payment history.
[2] Repayment flow of funds to be agreed upon.
Figure 3 is for illustrative purposes only and is subject to change. Terms and conditions apply.

Staying Resolute on Working Capital Management

Throughout varied economic conditions, careful working capital management has helped corporates maintain flexibility. It is paramount that organizations have access to a diversified source of funds that they can readily add to their funding mix to help promote operational stability, as well as fund strategic investments and expansions. Today, Citi offers many mature Trade and Working Capital solutions as well as the structuring knowledge needed to help corporates meet even their most complex working capital aspirations.

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