

PARTNER FINANCE

Partner Finance as a concept is the fall out of risk control measures set within banks that cap the exposures that the banks can take towards a borrowing entity. This is conceptually similar to consortium lending or syndicated finance that is prevalent in the banking world. The latter deals with large ticket capital expenditures incurred by large corporates or for project finance requirements of such behemoths. Post 2008 crisis, when banks started tightening finance avenues for corporate entities both big and small, partner finance started gaining strength. Banks started partnering even more than usual with other banks as well as non-banking financial institutions to strengthen their financial supply chain. Prior to the crisis, the lending directives in banks did have ceilings in terms of the quantum of finance that could be provided to an entity - country caps, currency caps, ceiling on industry exposures, to name a few. After the crisis, these credit controls were made tauter, pushing banks into intensifying partnerships with other financial intermediaries to retain client relationships and also open up non-interest income streams.

Dynamics of partner finance:

Banks onboard partner banks/factor houses and other financial institutions based on multi-factor due diligence process. Such lead banks are required to be aware of the risk appetites of their partners. They also mirror the credit limits that the credit partners have set up in their organizations in terms of the risk entities, credit caps for each risk entity and the utilization of the credit caps. Risk entities are usually the borrowing client ids, industries or counter parties on which invoices are drawn. When the lead bank receives a finance request against approved invoices under reverse factoring programs, they evaluate the finance amount with respect to their own bank credit limit head rooms. Whenever the head rooms are unavailable, they refer the finance request to the empanelled partners based on the knowledge of availability of partner credit lines. In a situation where a single partner cannot fund the client entirely, they distribute the finance amount among multiple partners. More often than not, they do not let the partner directly interact with their clients. They remain the lenders for their clients but have back-to-back sale agreements with the credit partners. This arrangement can therefore have a recourse for the lead bank. All repayments are routed through the lead bank which are then distributed to the credit partner(s) based on the share contribution. In case of a complete outsourcing of finance, the lead bank may end up moving the finance out of its books on to the credit partner albeit with booking of contingent entries to reflect any recourse. All credit servicing and collection efforts put in by the lead bank generate fee income for it.

System expectations:

Following are some of the system features expected in the area of partner finance:

1. Registering invoice portfolios: This feature is expected on self assisted channels as well as back office. Bulk capture as well as singular capture of approved invoices are required

2. Recording credit partner profiles: Registration of credit partner profiles can happen after the credit partners have been on-boarded. Supply chain finance application may not necessarily handle the on-boarding process.
3. Setting up and tracking of credit partner limits as well as own bank limits: This requires the ability to set up credit limits for the lead bank as well as the limit details shared by the partner banks. Partner bank limits are an extension of the credit partner profile
4. Generation of optimal mix of partners: For a given finance request, the supply chain finance solution is required to determine the minimum number of financing entities to be involved. The idea is to avoid the complex orchestration required in moving repayments to the credit sharing finance institutions
5. Repayment servicing: This requires the ability to receive repayments through various modes – checks, electronic payments and account to account transfers. After the repayments are received from the borrower, routing the credit partner shares to the destination banks and also recording the release of the used up credit limits for the credit partner. This is challenging as it requires the splitting of the repayment to first recover the servicing fees for the services provided by the lead bank and then breaking down the net repayment amount into shares for the credit partners. Splitting the credit partner share further in terms of repayment into principal repayment, interest repayment is hugely complex and usually not a system expectation.

Conclusion:

As the industry evolves to design new ways to adapt to crippling credit norms self imposed by banks, to control risks and to sustain marketable portfolios of advances, system support takes centre stage. The ability of the supply chain finance applications to devise new products that match new credit arrangements with strong reporting and data presentation enabling closer and real time monitoring of credit limits becomes crucial. This is the new reality for system vendors that pitch for technology mandates from banks that aggressively strive to remain relevant for their clients and the financial ecosystem as a whole.