SME Finance Opportunities

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Obstacles to SMEs increasing growth, profitability, employment and exports:

- Lack of working capital to buy raw materials and packaging, to employ additional direct labor to produce new orders and to market the products, especially to new customers and export markets
- Lack of credit experience and track record with commercial banks to obtain needed financing
- Inadequate financial statements and financial controls, making credit evaluation of the business and its trends difficult
- Insufficient real estate to satisfy collateral requirements of the banks
- Inexperience in preparing adequate business plans and loan applications to modern, competitive standards
- Inexperience in the procedures and mechanisms for exporting of products

Alternative financial vehicles for SMEs:

- Leasing and “Sale/Leaseback” of vehicles, equipment and even buildings
- Factoring of Receivables
- Factoring of Letters of Credit
- Purchase Order Financing
- Lines of Credit secured by equipment, inventories, receivables, and cash balances

Leasing and Sale/Leaseback:

- SME obtains financing to purchase vehicle or equipment

- Bank or finance company ("FI") is secured with collateral of the leased asset which can be readily repossessed and sold if SME in default

- SME can in some cases sell existing assets to the FI, and then lease it back from the FI. This can provide immediate working capital for the SME. The FI can require a certain percentage to be blocked in a deposit account to cover repossession and collection costs if SME defaults on payments.

Factoring of Receivables/Invoices:

- SME receives order from Customer
- SME produces and ships order to Customer
- SME issues invoice, but the invoice/receivable is assigned to bank or finance company ("FI")
- FI advances 70-80% of invoice value to SME
- FI collects from Customer
- FI pays the balance on the invoice to SME after collection minus interest and fees
- Requires that the SME can produce and ship the product and that the Customer is creditworthy
- Improves cash flow of SME by receiving up to 70-80% of the funds for an order without the 30 – 120 day wait for collection from the Customer
- Allows SME to handle greater volume of orders, increase revenues and profits and grow

Factoring of Letters of Credit:

- Similar to factoring of receivables, but it is against a Letter of Credit (LC)
- If the LC is an irrevocable LC from a major bank based on shipment of product, the risk of collection is dramatically reduced because payment is guaranteed as long as product ships

Purchase Order Financing:

- SME receives purchase order from Customer
- FI purchases raw materials and packaging on behalf of SME and in some cases advances funds to SME for direct labor to produce order
- SME produces and ships order to Customer
- SME issues invoice, but the invoice/receivable is assigned to FI
- FI collects from Customer
- FI pays the balance on the invoice to SME after collection minus the amounts paid for raw materials, packaging and direct labor and its interest and fees
- Requires that the SME can produce and ship the product and that the Customer is creditworthy
- Allows SME to take on orders that it otherwise couldn’t handle

Lines of Credit Secured by Equipment, Inventories, Receivables and Cash/Cash-flow:

- Requires understanding of the cash flow of the SME
- Requires ability to use equipment, inventories, and receivables as collateral and to assess the resale value or collectability of these assets
- Can provide needed working capital to the SME but collateral coverage has to be high to cover the risk of default