

Research on Risk Control of Supply Chain Finance from the Perspective of Commercial Banks

Wei Xing

Hunan Vocational College of Modern Logistics, Changsha, 410131, China

760933676@qq.com

Keywords: Commercial Banks; Supply Chain Finance; Risk Control

Abstract: Currently, banks in China mainly face problems of credit environment, industry gap, the core customer etc. in terms of supply chain, which leads to higher requirements for the credit risk, operational risk, and legal risk of the supply chain. To strengthen the control of supply chain risk in commercial banks requires that all members in the supply chain are regarded as a whole of financing needs, and that the financial risk management of the supply chain is promoted.

1. Introduction

As the undertaker of capital flow in social and economic activities, commercial banks are more closely involved in the supply chain by providing settlement, credit granting and other services to the members of the supply chain, and can carry more functions in the continuation of the trade chain. [1] The bank-enterprise relationship formed by the supply chain finance will bring comprehensive economic benefits to banks, including credit granting, deposit and settlement.[2] Therefore, banks should keep a clear mind in carrying out supply chain finance and pay special attention to the prevention and control of related risks.

2. Current Problems in Supply Chain Financial Services

2.1 Credit Environment and Credit System Construction

The biggest difficulty in developing supply chain finance in China lies in the information asymmetry between enterprises and banks.[3] Due to the "self-compensation" feature of the supply chain system, it is easy to cause the core enterprise to falsely report the trade transaction background for its upstream and downstream enterprises, and generate internal collusion to transfer funds. The main reason for this situation is the lack of a rating system for upstream and downstream enterprises in the supply chain in China.

2.1.1 Limitations of Credit Substitution

The bank-based supply chain finance business was established from the credit substitution of core large enterprises, which is very obvious in the financing process of small and medium-sized enterprises.[4] In its development process, although the business relationship such as "N+1+N" or "1+N" is established through effective management of the supply chain, such organization mode of financing management is to concentrate more financial resources towards the core group of enterprises, which tends to expand the credit of core enterprises so that more enterprises in the supply chain can get credit to develop the business.[5] As a result, the diffusion and aggregation effect of credit resource risks will expand correspondingly. Therefore, it has great limitations to carry out supply chain financing business by relying on credit substitution, which will lead to more risks and ultimately affect the healthy growth of supply chain financial business innovation.

2.1.2 Limitations of Credit Management

The innovation of the supply chain finance in China is that its main modes include the supply chain financing mode which is established based on the cooperation between banks and third-party

logistics enterprises in supply chain management, and the structural trade financing business mode which is built based on the business innovation of traditional commercial banks. The highest profit of the innovative business of the supply chain finance model cannot reach that of the traditional banking business model, so the bank-centred supply chain financing model lacks the innovation motivation and is difficult to become the mainstream business.

2.2 Differentiation of Different Customers and Industries

Due to the geographical dispersion of the supply chain itself, the target region of supply chain finance is also dispersed, and core enterprises are often not in the same province as upstream and downstream enterprises, or even logistics companies, which makes the management of supply chain finance difficult. However, at present, most commercial banks in China still use the traditional hierarchical system of general branch, branch and sub-branch, and the coordination and cooperation between the head branches across the region are not smooth. Supply chain financing business will encounter the following problems when operating across regions:

2.2.1 Habitual Differences

Cross-regional operation will lead to the differentiation of business habits, which makes the supply chain financing service scheme unable to adapt to the differences in business modes between different regions. In view of this situation, banks mainly carry out inter-bank cooperation to provide each other with complete standard information and make up for the supply chain financing business problems caused by the differences in regional business habits.

2.2.2 Cross-regional Logistics

The long time cross-regional logistics takes often leads to some problems in the supervision of logistics by banks, which is caused by the change in the value of goods. In view of the risks that may occur in logistics operation, including transportation safety and quality assurance factors in the logistics process, cross-regional logistics will lead to certain impairment risks of quality. Among the main industries carried out by banks in their supply chain financing business, losses caused by logistics are very common in the transportation of goods such as household appliances and auto parts. In this case, the banking industry mainly carries out risk aversion according to the qualification examination of logistics companies, and relies on the claims of insurance companies and the compensation liabilities of logistics companies to reduce the losses after the occurrence of accidents.

2.3 Core Enterprise Customers

2.3.1 Reviewing Credit Requirements

The minimum length depends on whether the enterprise is in line with the bank's internally developed and implemented credit requirements. If the enterprise is even difficult to get the credit approval from the bank, then it does not have the qualification to obtain financing from the bank, let alone provide guarantee for other enterprises.

2.3.2 Examining Company's Position in the Supply Chain

If a relatively stable supply and demand network has been formed around the enterprise, it can be said that the enterprise has a dominant position over its upstream and downstream enterprises and has strong market competitiveness, such as home appliance manufacturing enterprises, steel manufacturing enterprises, and so on. This type of enterprises can be preliminarily judged to be the core enterprises.

3. Strengthening the Risk Management of Supply Chain Finance

Based on the existing problems of banks in supply chain financial services, this paper proposes the risk control countermeasures of supply chain finance from the perspective of commercial banks, as shown in figure 1.

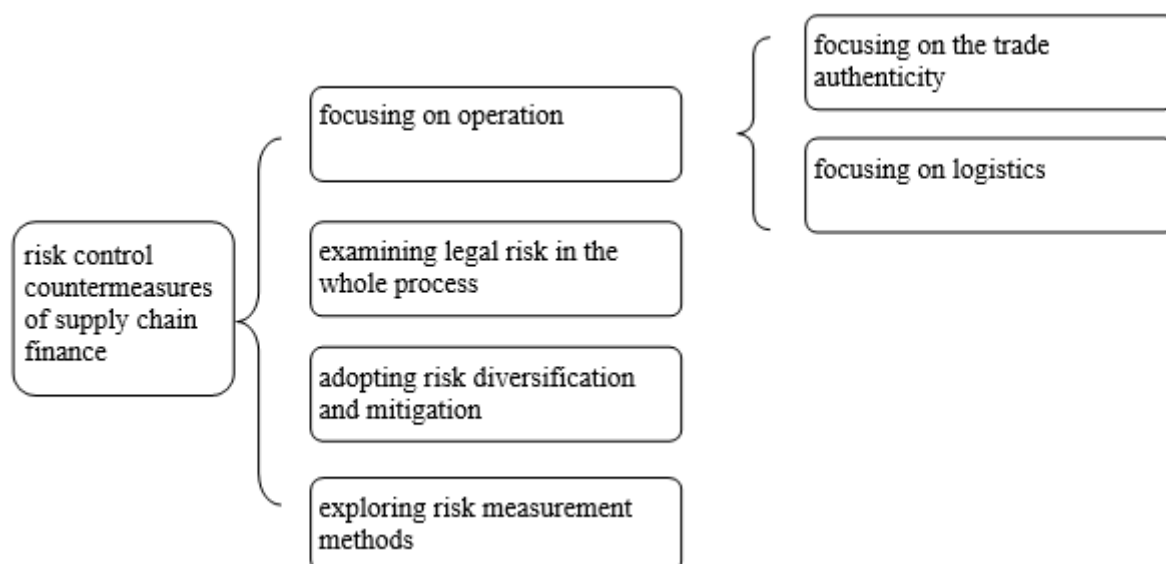


Figure. 1 Risk control of supply chain finance from the perspective of commercial banks

3.1 Focusing on Operation

Risks caused by the service targets of supply chain finance are from many small and medium-sized enterprises, and the credit granting to them is carried out around the core enterprises, that is, the credit granting to these small and medium-sized enterprises is bound on the core enterprises, which makes up their deficient credit level. But the premise is that the relationship between enterprises in the supply chain remains unchanged. Thus, banks must keep an eye on the progress of trade relations.

3.1.1 Focusing on the Trade Authenticity

The biggest difference between supply chain finance and traditional credit granting is that not only the borrower should be evaluated, but also the transaction mode and process should be evaluated. In some cases, the evaluation of the transaction subject can be weakened appropriately, while the evaluation of the transaction itself can be emphasized, that is, its self-compensation can be fully emphasized. Therefore, the authenticity of trade contracts and the effective connection of the transaction are particularly important. Once the authenticity is lost, there will be huge risks in bank credit granting.

3.1.2 Focusing on Logistics

In supply chain finance, capital flows along with material flow. Therefore, keeping an eye on and controlling the material flow at all times are the premise to ensure that the capital flow is not out of control or interrupted. No matter where the goods are in, such as in the seller, the transport party, the supervision party, the buyer or any other parties, the bank should timely grasp accurate logistics information, and restrain each other's behaviours through various prior agreements with the participants. On in this way can the normal capital flow and the timely repayment of credit funds are ensured.

3.2 Examining Legal Risk in the Whole Process

There will be many legal relationships that have not been involved before due to the multiple participants, links and long process of supply chain finance. Therefore, this new situation should be regulated from the perspective of law that clarifying the legal responsibility of the participants. In terms of credit extension, if factoring business is carried out, it shall determine different notification methods according to explicit factoring and implicit factoring, and register in the receivables mortgage registration system of the People's Bank of China to ensure the validity of the bank's rights as creditor. In a word, the whole process should be operated under the premise of legal compliance.

3.3 Adopting Risk Diversification and Mitigation

The business of supply chain finance is complex, and some decentralized management methods can be adopted to disperse or mitigate risks. For example, goods may be regulated by an independent third party, who may be required to take out property insurance, including transportation insurance, for goods traded. With regard to risk mitigation, in addition to the above safeguards embedded in the business process, other safeguards may be added, notably credit insurance. In reality, in quite a number of supply chains, core enterprises are not so strong as bank expected. Although a complete supply chain has formed around the core enterprises and their trade activities also meet the supply chain, it is still difficult to obtain bank credit support on their own. In this case, external support is needed to provide some credit service, such as credit insurance. Insurance companies are also willing to use credit insurance as a means of intervention to lay a foundation for the subsequent all-round promotion of other insurance business. Credit insurance can also be combined with third-party supervision. For example, if the insurance company acts as the logistics regulator, it can not only meet the needs of supervision on goods, but also provide conditions for the implementation of counter-guarantee measures of credit insurance.

3.4 Exploring Risk Measurement Methods

If the main risks such as credit risk and operational risk are measured according to the standard of general credit granting business, the risks in supply chain finance may not be accurately described since there is a transfer of credit risk to operational risk and there is also credit binding. Therefore, data and information for such operations shall be separately recorded so that it can set up independent risk measurement model that assesses whether risks and benefits are matched after a period of time.

4. Conclusion

In the process of developing supply chain finance business, commercial banks should monitor the authenticity of trade and gradually transform risk assessment from a simple credit offset to trade self-compensation. To some extent, this is a change of bank risk management ideas, a great step of credit review from value orientation to substance orientation.

References

- [1]The response of the external finance premium in Asian corporate bond markets to financial characteristics, financial constraints and two financial crises [J]. Paul Mizen, Serafeim Tsoukas. *Journal of Banking and Finance*. 2012 (11)
- [2] The new monetary and financial initiatives: finance regaining its position as servant of the economy [J]. Sandrine Ansart, Virginie Monvoisin. *Research in International Business and Finance*. 2015
- [3] He significance of financial self-efficacy in explaining women's personal finance behavior [J]. Lisa Farrell, Tim R.L. Fry, Leonora Risse. *Journal of Economic Psychology*. 2015
- [4] The impact of supply chain risk on supply chain integration and company performance: a global investigation [J]. Li Zhao, Baofeng Huo, Linyan Sun, Xiande Zhao. *Supply Chain Management: An International Journal*. 2013 (2)
- [5] The contingency effects of environmental uncertainty on the relationship between supply chain integration and operational performance [J]. Chee Yew Wong, Sakun Boon-itt, Christina W.Y. Wong. *Journal of Operations Management*. 2011 (6)