INVOICE FINANCING

HOW DOES IT WORK?

Introduction

Invoice financing is a generic description used to refer to the raising of financing by companies using the invoices that are issued by a supplier to a buyer for the supply of goods or services. Invoice financing helps companies to secure cash immediately and hence, improving cash flow for working capital and growth purposes rather than waiting for their customers or buyers to pay them in the future.

Generally, invoices can be financed in two ways.

Sale of invoice or factoring

The first is through the sale of the invoice to an investor – this allows the supplier to "monetise" the invoice immediately instead of waiting for the buyer to pay in accordance to credit terms set out in the invoice. This method is also commonly known as "factoring". Invoices are verified before funding takes place. Verification ensures that the invoice is due and payable and that there are no issues that may prevent payment e.g. disputes.

Receivables-backed loan

The second is to use the invoice to secure a loan through a receivables-backed loan. This allows the borrower to use its invoices as a security or collateral for the loan taken out. The invoices will be identified and recorded as a charge in favour of the lender.

Invoice Financing at Minterest

At Minterest, we do invoice financing for our clients using the first method i.e. the sale of the invoice to our investors or "factoring". Most invoice factoring transactions are structured in such a way that the company (i.e. the supplier) gets paid in two instalments when it sells the invoice. The first instalment may cover up to 90% of the invoice value with the remaining being paid once the buyer pays the full invoice value. Typically, the supplier is also obliged to buy the invoice back if the buyer does not pay within the terms of the sale of the invoice. In very rare situations, investors may only take the payment risk of the buyer.

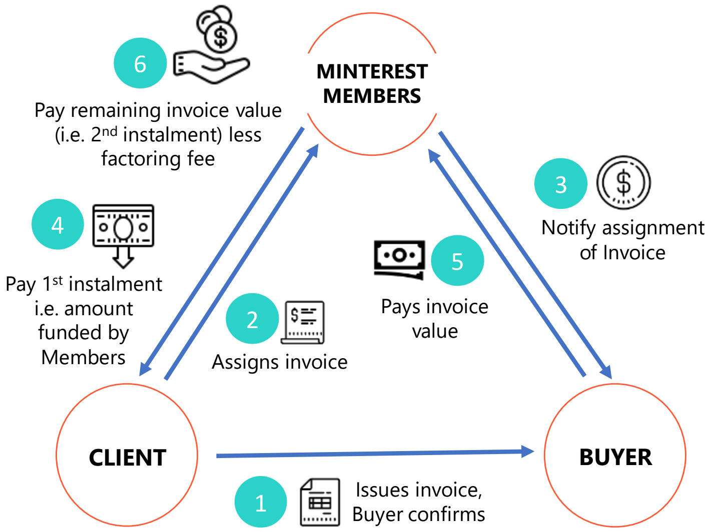
Invoice financing or factoring represents a low risk method of providing financing to a SME as investors get paid in priority to the supplier when a buyer makes payment on the invoice. Unlike an unsecured working capital loan, invoice financing does not rely on the "borrower" paying the investors.

Every factoring transaction goes through the Minterest's proprietary MintGrade credit scoring algorithm that rates the creditworthiness of a particular factoring deal. The algorithm used for factoring transactions differs to that of used for normal loans although the approach and methodology is similar.

An Illustration

The various stages of how an invoice is financed / factored on the Minterest platform and how investors are repaid can be summarised and illustrated as follows. Minterest facilitates the various steps and flows as well as acting as factoring agent for the investors.

Diagrammatic flows



Invoice financing steps

1. A client on the Minterest platform issues an invoice or invoices to its customer i.e. the buyer. As part of Minterest's factoring terms, the buyer is required to confirm the invoice is valid.

2. The client assigns or sells the invoice(s) to investors (i.e. members) on the Minterest platform. This will be done via a factoring request on the Minterest platform where members are able to participate in the purchase of the invoice(s) when the factoring request is launched on the platform.

3. Once the factoring request is fully funded, Minterest, as factoring agent for the members, notifies the buyer of the assignment.

4. Minterest, on behalf of the members, makes the first instalment payment to the client. The first instalment is typically between 80% and 90% of the invoice value. In exceptional circumstances, the first instalment may fall outside this range.

5. The buyer makes full payment in accordance with the credit terms set out in the invoice. The payment will be made to a collection account managed by Minterest.

6. Once full payment is received from the buyer, the second instalment (less factoring fee and any other charges) will be paid to the client. Members will get repaid at the same time.

What are the risks associated with invoice financing or factoring?

All investments carry risks and it is no different when participating in invoice financing or factoring on the Minterest platform. While there are numerous risks inherent in every type of investment, there are four major risks associated with invoice factoring i.e. sale and purchase of invoice(s).

Credit risk of the buyer

This is the risk where the buyer of the goods or services does not make payment on time or does not make payment at all. Delay in payments could be due to cash flow constraints, administrative oversights and other issues facing the buyer. Total non-payment could be due to the insolvency or liquidation of the buyer. This is the main risk in any invoice financing through the sale of invoice(s).

This risk is mitigated through a number of ways. At Minterest, we analyse the **creditworthiness of the buyer** which forms a big component of the MintGrade rating methodology used for invoice financing. We also assess the client's creditworthiness and in the event of the buyer not making payment within the required period of time, the invoice(s) are sold back to the client.

Incorrect payment flow risk

This happens when the buyer makes a payment of the invoice to an incorrect bank account e.g. payment is made to the client instead of Minterest's collection account. This risk is mitigated by having the buyer involved in the invoice financing process with the **buyer being notified** that the invoice(s) has been sold. The bank account details will be provided to the buyer as well. Even if an incorrect payment is made, the legal documentation ensures that the money received by the supplier from the buyer belongs to the Minterest members as the invoice(s) has been sold in the first place.

Discount or dilution risk

This risk may arise when the buyer will not pay the full invoice value for various reasons including non-performance of the supplier in respect of previous supply of goods or services. This is mitigated through the notification process where the **buyer confirms the invoice** and its value as well as up-front and continuous engagement with the buyer in the entire invoice financing process.

Supplier fraud risk

In rare situations, a supplier may try to sell invoice(s) multiple times or sell fake invoice(s). If this happens, investors may not receive the entire invoice value if invoice(s) is sold multiple times. Minterest mitigates this risk by engaging with the buyer up-front and seeking to have **multiple touch points at the buyer level**. History of business dealings between the supplier and buyer and other factors are also taken into consideration during the due diligence process.

At Minterest, we take the interests of our members and clients very seriously. All parties - client, members, buyers (where applicable) and Minterest enter into **trade related documentation** to ensure that all parties' rights and obligations are clearly set out.