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## Small Business

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# An Alternative to Expensive Alternative Financing

By Patrick Clark May 29, 2013

(Corrects examples of companies that use Taulia's dynamic discounting platform)

For many small businesses, credit is hard to get and slow in coming. With fewer companies getting bank loans, alternative lenders are positioning themselves to fill the gap by offering faster financing to companies with weaker credit profiles than banks would typically consider. While alternative financing is easier to get, it's also more expensive.

Taulia is a San Francisco startup positioning itself as an alternative to alternative lenders for small businesses that sell to big corporations. It gets corporate buyers to pay suppliers earlier than they usually would. In return, suppliers give buyers discounts. The upshot for Taulia's supplier clients is that they decrease their dependence on pricy credit and improve their cash flow.

Joe Hyland, a vice president of marketing at the four-year-old venture, says demand for its service is driven by two trends: First, big companies sitting on cash reserves are earning near-zero interest rates; second, they're taking longer to pay their vendors. "Back in the 1970s or '80s, many of the world's biggest corporations started stretching out payment terms" and earning interest on cash earmarked for suppliers, says Hyland. "Today, those companies are paying suppliers later and later, only now they're earning lousy returns on that money."

Taulia's pitch is that the discounts suppliers will accept for early payment are worth more than what large corporations are earning on their cash reserves.

Since Taulia processed its first payment in 2011, the company has signed up about 100 companies, including PG&E (PCG), John Deere (DE), and Coca-Cola Bottling (COKE), and has processed about $30 billion in early payments. It profits by charging large corporations an annual fee to use the startup's automated platform for formalizing these real-time bargains.

What Hyland calls "dynamic discounting" is a new wrapper on an old practice, says Bill Hettinger, a consultant at the Institute for Finance & Entrepreneurship. "Go down to the local lumberyard and they're probably doing it for the construction guys—'Pay me at such a time, and this is the price,'" he says. What Taulia and its competitors—including SAP's (SAP) Ariba and J.P. Morgan's J.P. Morgan Xign—are doing is automating the process for large companies that don't have time to haggle with all of their suppliers. "It makes sense as long as the credit markets are tight and suppliers have difficulty obtaining more favorable financing," Hettinger says.

Peter Loughlin, who writes about supply chain finance at the blog Purchasing Insight, explains the math that makes it work here. In Loughlin's hypothetical, a company that pays its supplier 20 days early in return for a 2 percent discount is getting an annualized return of about 36 percent, far more than the company would earn in interest on that cash over the same period of time. "It gives the supplier a way to avoid the payday loan kind of financing that's out there," says Loughlin.

Hyland says that the model can sustain a rise in interest rates or looser small business credit and that discounts will vary to reflect market conditions. How big can the market for dynamic discounting get? “We look at the opportunity as equivalent to the size of the factoring market,” says Hyland, referring to the practice of raising working capital by selling receivables before they’re due. According to Factors Chain International, a network of factoring companies, that global market was $2.6 trillion in 2011.

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