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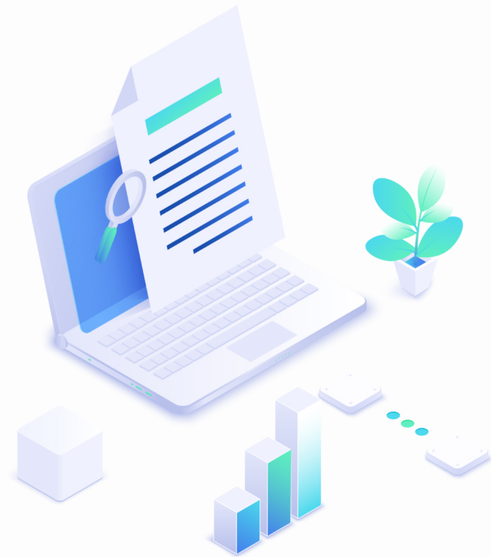
Moving towards Finance Transformation

Overview of the Logistics sector | Challenges in Finance | Connected Finance Ecosystem in Logistics

Overview of the Logistics Sector in India



The logistics sector is the backbone of any economy. It includes all supply chain activities such as transportation, customer service, inventory management, the flow of information, and order processing. Other supply chain activities are warehousing, material handling, purchasing, packaging, information dissemination, and maintenance, amongst others.

As per the Indian Investment Grid[2], an initiative of the Ministry of Commerce and Industry, the Indian logistics sector was valued at **USD 160 billion** in 2019. By the end of 2022, it is to become **USD 215 Billion.**

According to research, the sector will grow at a compound annual growth rate (CAGR) of 15.5% between FY 2019 and FY 2024. It employs around 22 million people and will create another 1.2 million jobs by 2025.

This industry remains largely unorganised despite contributing to such a large portion of the GDP. The unorganised sector amounts to more than 90% of the logistics sector, including owners of less than five trucks, brokers or transport companies' affiliates, small-scale warehouse owners, customs brokers and freight forwarders, among others. During the pandemic, logistics was one of the only sectors allowed to operate, with a limited workforce.

Digital transformation across all functions, including finance, is the key to reinventing the overall business. **A recent survey states that 92% of CFOs in the Asia Pacific region plan to increase digital spending this year with the adoption of Finance 4.0.**

To enable this, Finance Leaders must focus on adopting digital technologies such as Artificial Intelligence (AI), the Internet of Things (IoT), automation, and blockchain. The technology aims to digitally transform finance functions such as budgeting, financial planning and analysis, treasury, and order-to-cash management.

Challenges in Finance

1. Operational challenges due to a large base of unorganised vendors

Logistics companies tend to have an extensive vendor base (2000-3000 vendors for a company with a turnover of INR 500 cr). These vendors include first-mile, middle-mile, and last-mile providers, warehousing hub rental landlords, housekeeping staff, equipment providers, truck repair providers, etc. They have different formats of invoices, many of which are paper-based and shared via various means. Most of these vendors need to be more organised or under the purview of e-invoicing.

This poses several challenges-

It takes 8-15 days to onboard a vendor since the onboarding and manual KYC process. This does not allow vendor due diligence at the onboarding time, heightening the risk of dealing with non-compliant vendors.

A vast team (team of ~30 people for managing 2000-3000 vendors) needs to be employed for just data entry for recording invoices, thereby increasing person-hours unnecessarily and the risk of errors due to manual processes.

There needs to be more visibility on vendor acceptance of the purchase order and the status of the fulfilment.

Paper-based invoices are prone to errors involving the place of supply, invoice numbering, and others, which leads to increased efforts during monthly ITC reconciliations. Tax teams must spend hours correcting these errors and communicating with the AP team and vendors.

Companies should automate the entire 'invoicing to payment process' and onboard vendors on a mobile-friendly vendor portal.

- Begin with vendor onboarding and KYC (and more frequent vendor risk profiling).
- A vendor portal where vendors can view and accept POs, update the status on fulfilment and flip the PO into a draft invoice
- Enable invoice capture, digitisation and validation to reduce manual effort and errors at this stage. This will help early detection of fraudulent behaviour
- During the creation of the purchase register, auto-fetch GSTR-2A/2B data and trigger reconciliation.
- Enjoy blocking of payments for non-compliant vendors.

2. Lack of vendor visibility leads to inefficient business process

Dealing with a vast unorganised vendor and truck owner base that, too, with many processes involved, leads to a lack of vendor visibility for a logistics company. Also, it is easier to communicate discrepancies or issues with the vendors with a proper communication system.

Hence, logistics companies must opt for technological solutions to streamline vendor activities. For instance, they can use an integrated vendor portal to onboard vendors and allow them to raise GST-compliant invoices. Also, they can establish two-way communication using vendor communication tools for quick dispute resolution. This would mitigate the working capital issues of stakeholders, create trusted business relationships and ultimately improve the business.

3. ITC blocked/delayed due to non-filers and quarterly filers

The average percentage of invoices missing in the GSTR-2A/2B is ~30%, which can be as high as 50% in logistics. This is due to the kind of vendors that the industry typically deals with:

- A long tail of small one-time vendors
- Non-filers
- Quarterly filers

As Input Tax Credit (ITC) claims are now allowed only if the invoice gets reported by the respective vendors in their GSTR-1 and appears in the recipient's GSTR-2B, non-filing of returns or missing invoices results in ITC leakages. This escalates the GST cash liability and impacts a business's working capital.

Companies should leverage flexible payment-blocking solutions that block only the GST amounts for non-compliant vendors until the invoice appears in their GSTR-2B and the vendor files their GSTR-3B. This will reduce the impact on their cash flow due to delayed/ non-filing of GST returns while ensuring that the company is not violating any MSME laws.

4. Receivables cycle are typically much longer than payables cycles

Due to the nature of expenses involved and the type of vendors in this industry (drivers, diesel, repairs, etc.), payments are more frequent than in other sectors, as high as daily or weekly. But the collection cycle can range from 1 - 3.5 months. Subsequently, companies are often strapped for cash and need to identify levers to improve cash flows constantly. One such lever is identifying the right rates for each vendor based on the frequency of payment and risk status of the vendor to optimise cash outflow.

Common solutions or platforms ensure transparency and, in turn, promote formal and easy access to supply chain finance or invoice discounting. This will help companies build a healthy vendor ecosystem by providing access to standard credit facilities to vendors that need it the most and otherwise would not have access to it, making them cash-crunched. This also has second-degree effects on their compliance solving for your problem of ITC delays due to non-filers. Compliance of long-tail vendors goes up by ~30% when financing solutions are offered.

Companies should explore innovative early payment solutions to negotiate better rates with vendors while earning a higher yield on discounts extended to specific vendors. A discounting platform provides flexibility to both the vendor and company to choose between what's essential to them mutually - payment sooner but with a higher discount or an amount slightly later but with a lesser discount.

5. Complex and extensive tax compliances

Logistics companies are present nationally with multiple registrations in each state, which means a higher number of GSTINs and TANs are to be dealt with along with voluminous data. While the GST laws have put the onus of input tax credit claims on the recipient business, the income tax laws have heightened TDS compliance measures.

Having to deal with thousands of vendors and invoices daily makes it challenging for teams to verify every vendor and invoice frequently without automation. This creates a dire need for automation and consolidation of compliances under a single solution. Logistics companies, in particular, also need to have scalable tax technology since volumes tend to peak during festivals and sales.

ERP

Companies would benefit from a single source of data entry in the ERP and automatic data extraction for e-invoices, e-way bills, and GST returns. Likewise, where TDS compliance is warranted, a solution that incorporates the automatic detection of such vendors, computation of the TDS amount, and challan generation and return filing from one platform would be ideal. This would be even more efficient if fueled by automated reconciliations, vendor communication and vendor payments. Non-compliant vendors need to be flagged and detected early on. The goal should be to mitigate discrepancies immediately and minimise the risk of notices.

6. Additional rules and laws governing transporters

Adherence to e-way bill protocols is a must for this industry, and any error can cause a loss of business. Further, when the mode of transport or vehicle is changed, the e-way bill has to be updated. Transporters may be required to carry a consolidated e-way bill for multiple consignments. And sometimes, there are complications surrounding the validity and cancellation.

Companies should opt for an integrated solution with features such as bulk and automated generation of e-way bills, in-built data validations, auto-retries of failed e-way bills, and automatic validity extensions. Further, companies should look for a solution that consolidates GST and e-way bill compliance (and e-invoicing where applicable) to eliminate any loopholes.

Another significant aspect on the compliance front is that logistics companies are required to pay GST on a reverse-charge basis when they use the services of a Goods Transport Agency (GTA). Without an automated system to detect unpaid GST, companies could omit specific invoices, leading to notices and penalties. It would also help to have a solution that tracks reverse charge applicability where GTAs are involved and tax liability calculation for every month.

Connected Finance Ecosystem in the Logistics Industry

Digital transformation can help the sector reap significant benefits, such as:

- Superior customer experience
- Better accessibility to information or data
- Improved efficiency and productivity
- Improved business insights

The connected finance system improves digital maturity, interconnects the finance functions, and aids in achieving the organisation's digital goals.

Clear Finance Cloud (CFC) is an integrated solution to digitally transform the finance function across the AP, Tax, and Treasury teams. It helps manage the entire invoice lifecycle of the entity by synchronising the AP process, vendor communication, and tax compliance. It uses more innovative integrated solutions for standard information flow.

OUTWARD

Customer Onboarding	E-Invoicing & EWB Creation (**Acc Receivable**)	Recon of E-inv & EWB vs SR (**Taxation**)	GSTR 1 prep and Filing (**Taxation**)	Revenue Recon Tax GLs vs Income GL (**Taxation**)	GST Notices Tracking and Replies (**Taxation / AP**)

INWARD

Vendor Onboarding	Invoice Capturing & processing into ERP/ PR (**ACC Payable**)	ITC Recon & Claim management (**Taxation**)	Vendor payments & Communication (**ACC payable**)	ITC update in GSTR 3B (**Taxation**)	Early Payment Invoice Discounting (**Treasury**)

With a connected finance ecosystem, businesses can optimise the time-to-value window of the entire process. One single solution (CFC) anchors and syncs multiple processes to streamline the entire ecosystem and mitigate compliance risk exposure.

Watch Demo Video