

CONTRACT CAPITAL DIGEST

Your Partner in Contract Financing and Working Capital for Over 35 Years

At THE WATSON GROUP, we've partnered with countless growing companies to secure financing for their contracts and purchase orders. Whether their customer or prospect is government or large commercial, we specialize in developing FUNDING SOLUTIONS to support their performance.

Our diverse range of innovative, "out-of-the-box" funding options include, Contract Mobilization Funding, Contract Payroll Funding, Vendor Trade Credit Financing, Supply Chain Financing, Purchase Order Financing, Construction Subcontractor Financing, Factoring and Express Pay Financing, Contract Manufacturing Financing, or Financial Commitment Letters, just to name a few.

CONTRACT CAPITAL DIGEST is designed to share with you the HOW TO's for some of the practical and proven techniques and methods we teach and use in our practice on a DAILY BASIS, regardless of business credit standing.

Please feel free to reach out if you have any questions or would like our input on any Contract Financing opportunities or challenges you may be having.

Gerald C. Watson
President & Publisher



THE BASICS OF CONTRACT MANUFACTURING FINANCING- 101 A TRUE CASE STUDY

Congratulations! You have just been notified that after a successful market test of your new healthy beverage drink for kids, a national grocery store chain has awarded your company a HUGE PO to begin rolling it out into their stores on a national basis!

The product will be manufactured by a co-packer, a third party manufacturing company you have contracted with to produce the order to spec. The co packer will blend the ingredients, formulate the finished product, bottle, label, package and drop ship to each regional distribution center for your customer. You have also been informed by your customer that, based on their forecasts, they will be placing periodic re-orders on an on-going basis to meet their minimum warehouse inventory requirements. Payment terms are net 45 days.

Turnaround time from your co-packer is 60 days after receipt of all raw material ingredients, and supplies from your vendors. Payment terms with your co-packer is 50% deposit to start production, and the balance before each shipment. In addition, you have 6 major vendors you have to pay as well. While your bottle and label suppliers have agreed to net 30 payment terms, payment will actually be due BEFORE your order is shipped. In addition, your raw material ingredient suppliers require payment in full before they ship to your co-packer.

You had an investor, but unfortunately, the deal fell through in the 11th hour. In addition, you've depleted your 401K, and maxed out your credit cards, along with friends and family who jumped in to help you cover upfront product development costs. In addition, your bank turned down your loan application because the business is new with no track record or collateral, despite the large order from a national grocery chain.

WHAT WOULD YOU DO?

THE BASICS OF CONTRACT MANUFACTURING FINANCING- 101

THE DELIMA

A PRACTICAL SOLUTION

Every day, business owners all over the country who have developed new products, and can get PO's, struggle with getting financing to manufacture them. For some, it's the opportunity of a lifetime they've been waiting for but it's slipping through their fingers because they just can't get the juice!

Factoring is not an option because you can't invoice until the product is delivered, and the product can't be delivered until it's manufactured by your co-packer, and your co-packer won't manufacture until they've received money upfront from YOU.

PO Funding is not an option because most PO lenders typically don't finance contract manufacturing especially where raw materials, ingredients, and supplies all have to be secured, then delivered to a third party for production. As a rule, they only finance PO's for off the shelf finished products drop shipped directly to your customer.

Vendor Trade Credit Financing is not an option because your raw material and ingredient suppliers won't accept a Payment Assurance Letter from your lender because, as far as they're concerned, delivered and accepted has occurred once they've delivered to your Co-Packer, and not when the finished product is manufactured and delivered to your customer.

You've literally tried EVERYTHING, including calling Shark Tank for an audition, only to find out they're already booked up for the season!

You've even read through all the back issues of CONTRACT CAPITAL DIGEST and STILL couldn't find any answers! (until this issue which had not published yet)

Over the years, we've helped numerous clients, with large PO's secure Contract Manufacturing Financing SOLUTIONS for products ranging from BBQ Sauce, to hand sanitizer, to greeting cards for kids, to electrical components, to even public transit buses.

To be sure, it's a "little-known, highly specialized" form of financing which is why so many entrepreneurs on TV are willing to give up VALUABLE EQUITY to secure it. But with effective use of these techniques and methods, they'll no longer have to do so.

In this issue, we will touch on the basics of Contract Manufacturing Financing, or what we'll refer to as Co-Packer Financing, including (1) What It is, (2) How It Works, (3) What Are The Costs, and (4) include a few Success Tips. To be clear, while there are numerous options, techniques, and methods for financing PO's and contracts, our newsletter only speaks to those we have actually utilized over the years, with our own clients that have proven to work.

To request a **free subscription** to Contract Capital Bi-weekly Digest scan the QR Code below or email:
info@twgfundingsolutions.com



THE BASICS OF CONTRACT MANUFACTURING

WHAT IS IT?

So, what is Contract Manufacturing? The next time you're in a grocery store, pickup a can of food products off the shelf, and look at the bottom of the label on the back. If it says DISTRIBUTED BY, that means the brand contracted with a third party company to manufacture it.

From paper goods, to frozen foods, to a can of peas off the shelf, more and more brands are electing to outsource all or some of their production to third party manufacturing companies. Typically referred to as CO-PACKERS, these production facilities can range in size from a small factory, to large scale, state-of-the-art, high tech production facilities with millions of square feet. The client provides the recipe or specs for the product, and can either source the ingredients and raw materials, or rely on the Co-Packer to do so.

In addition, many Co-Packers also offer additional services including warehousing and storage for both raw materials and finished production. shipping and logistics, and purchase order fulfillment services.

The benefits, of course, for a start-up are enormous, including faster time to market, access to specialized expertise and certifications, ie FDA, GMP, improved scalability, while eliminating the costly investment and risk associated with a startup production facility.

HOW DOES IT WORK?

Two basic options. The first is to establish an arrangement with your Co-Packer whereby they do everything, ie you provide your recipe, product designs, specs, etc, and the Co-Packer handles all the sourcing and purchasing of raw materials, ingredients, components and supplies, etc pays the vendors, performs the manufacturing, does all the packaging, labeling, and provides you with a finished product ready to ship.

The second option is for you to source and select your own vendors, handle the purchasing, take responsibility for payment, and arrange for shipment to the Co-Packer to manufacture once all the materials and supplies have been received.

Each option has its' own advantages and disadvantages and you will need to evaluate to determine which one makes the most sense for you. Both have financing requirements either incrementally on a vendor-by-vendor basis, or a lump sum payments to your Co-Packer if they are handling everything.

In addition, your Co-Packer and each vendor will have their own respective payment terms. Typical vendor payment terms are 50% deposit with the order and the balance once it is ready to ship. In some instances, the vendor may request full payment in advance. Typical Co-Packers payment terms are 50% deposit and the balance due upon completion.

No matter which option you select, below are a few financing products and instruments we have used for Co-Packer Financing. The option(s) you select will be based on what's available from your PO/Production Financing lender, and the payment terms you are able to negotiate with your Co-Packer and vendors. Your lender will also offer to take the lead and assist in this process. Nothing like having " your bank" do the talking on your behalf, right?

THE BASICS OF CONTRACT MANUFACTURING

CO-PACKER FINANCING INSTRUMENTS

DIRECT CASH PAYMENT

Lender submits bank-wire transfer or ACH payment directly to vendor(s) and/or Co-Packer to cover deposit and final payment

PAYMENT GUARANTEE LETTER

Irrevocable Letter confirming payment will be made upon delivery and acceptance of supplies if a vendor, or upon completion and acceptance of production order if a Co-Packer, payable in accordance with the mutually agreed net payment terms.

LETTER OF CREDIT

Bank issued document, secured by cash, providing guaranty of payment to vendor upon presentation of required documents. Typically issued to overseas vendors

CO-PACKER FINANCING INSTRUMENTS COST

DIRECT CASH PAYMENT

3% to 5% per 30 days

PAYMENT GUARANTY LETTER

Varies per lender from flat rate of \$250-\$500, to 1%-2% flat rate based on Payment Guaranty Letter amount

LETTER OF CREDIT

Varies based on many factors but can range from 4% to 8% or more

WHAT ARE THE COSTS?

Ultimately, your actual "transaction cost", will be based on the mix of financing instruments you use and how long they are outstanding. In addition, not all PO/Production Financing lenders offer all the same instruments. For example, some will pay direct cash deposits, and others won't. Some will offer Payment Guaranty Letters and others won't. With regards to Letters of Credit, some lenders will offer, and others don't. In addition, some PO/Production Financing lenders require you to have a Factoring lender pay them off from the first Factoring Advance once the order has been delivered and accepted and the invoice has been approved and funded.

In the interim, use the table below as a guide for generating rough estimates of these costs:



KEY SUCCESS TIPS

- VET YOUR CO-PACKER! Make sure they have the technical , operational, and financial capacity to meet your product specifications and delivery requirements. Find out their minimum order quantity for both initial orders and reorders as well.
 - Visit your co-packer's facility to "kick the tires". Try and arrange for them to produce a test article as a sample BEFORE your production run, especially if the order is for a government agency or commercial customer. A test article will enable your customer to inspect and accept the sample product IN ADVANCE. Also, find out your CO-PACKER'S Quality Control protocol for BOTH process and end product as well.
 - VET YOUR INGREDIENT AND MATERIAL SUPPLIERS. DITTO No 1 above.
 - Negotiate extended Prompt Pay Discount Periods to give you the maximum time to pay at the lowest possible cost and still pickup the discount, whether you use a Payment Guaranty Letter or not.
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- Minimize your financing cost by MAXIMIZING use of Payment Guaranty Letters and MINIMIZING Direct Cash Payments.
 - All PO/Production Financing lenders do not provide Direct Cash Payments, Payment Guaranty Letters, or Letters of Credit. Be sure to find out UPFRONT what funding products your lender provides and determine if it meet your requirements.
 - Find out UPFRONT what the criteria is for you to be approved by your PO/Production Financing Lender. For example, some have minimum time in business requirements, while other don't. Some have minimum annual revenue requirements, while others don't. Some require a Factoring lenders while others don't, etc. Finding this out in advance will save a lot of time later.
 - Finally, calculate your "all in" financing costs and add to your " all in" direct product cost. Remember, MONEY IS A MATERIAL, and an important "ingredient" you don't want to leave out in determining total cost, selling price, and target gross margins.

Finally, if you'd like a copy of our Top 10 List of Things To Know BEFORE Signing a Purchase Order, click on the link **below**



Don't Let a Lack of Cash Flow Hold You Back From Taking On New Contracts!

Struggling to secure financing for your contracts and purchase orders? You're not alone. The fact is almost 50% of small business owners who applied for bank credit were denied. That's where we step in. Using our highly specialized, *alternative financing techniques*, we have helped growing business owners all over the country secure millions of dollars in financing for their government, and commercial contracts and purchase orders.

Transaction Engineering ©

COMPREHENSIVE DIAGNOSTICS

We begin by conducting a Preliminary Underwriting Interview to better understand your Contract Financing needs and timing, existing business condition, and identify any potential business or financial issues that could impact funding approval. We then compile a Checklist of Documents including a copy of contracts to be funded, along with standard business documents for internal review and analysis.

CUSTOMIZED FUNDING STRATEGY

With the results of our diagnostic review and analysis, we "engineer" a Funding Strategy to include the "optimal" funding products for each phase of your contract, ie at the beginning for mobilization or start-up, if required, in the middle to cover payrolls, vendors or subcontractors, if any, and at the end to speed up cash flow while waiting to get paid. We also develop a game-plan for addressing any business or financial issues which could impact funding approval.

LENDER SELECTION AND UNDERWRITING

Based on your Funding Strategy and our history and working relationships with our funding partners, we determine the "best fit options" including structuring of your Financing Facility, and negotiating of funding amounts, rates and terms. Once you have elected to move forward, we will continue to work with you and your lender on a day-to-day basis, including preparation of your formal app package, underwriting, due diligence, addressing any business or financial issues as required, ie UCC filings, all the way through final approval.

CLOSING AND FUNDING

Upon final approval, we work with you and our funding partner to expedite and facilitate the closing process through your review and execution of Closing Docs Package and funding.

Contract Financing Product's We Offer

- Contract Mobilization Funding
- Contract Payroll Funding
- Supply Chain Financing
- Vendor Trade Credit Financing
- Purchase Order Financing
- Subcontractor Financing
- Material Supply Financing
- Factoring and Express Pay Financing
- Contract Manufacturing Financing
- Financial Commitment Letters
- Working Capital Term Loans
- Revolving Asset-Based Lines of Credit

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