THE FINANCIAL DIRECTOR'S GUIDE TO CORPORATE TRADE

2020 Whitepaper

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7 THINGS EVERY FINANCIAL DIRECTOR MUST KNOW BEFORE ENGAGING IN CORPORATE TRADE

INTRODUCTION

Businesses today are faced with tremendous pressure to navigate between now and next. EBITDA is everyone's responsibility, and financial professionals are tasked with uncovering and bringing opportunities to the table that will drive efficiency and value to the business.

Corporate Trade is a smart strategy to unlock cashflow and deliver financial flexibility as businesses balance delivering on today's needs with tomorrow's vision. This guide offers an in-depth look at Corporate Trade through the lens of a financial professional. It will equip you with insight, questions, examples and best practice to help along your path.

IN THIS GUIDE:

Evaluate whether your business is a good Corporate Trade candidate

Identify areas of untapped value that can have an immediate impact on your financial performance

Understand 2 basic types of Corporate Trade transactions and identify which is right for your business

Accounting for a Corporate Trade transaction

Meaningful questions to ask a Corporate Trade provider

Outline best practice in implementing a Corporate Trade partnership in your business

WHAT IS CORPORATE TRADE?

Corporate Trade is a business transaction that enables companies to pay for marketing expenses like media, using their own assets. Paying for what you need with cash alternatives is a powerful way to drive untapped efficiency in your business.

Most people are familiar with the concept of a 'contra-deal' where a business exchanges its own product for another product. This type of arrangement has its limitations as the two parties need a direct swap at the same time, with the same value. It is difficult for most businesses to sustain on an ongoing basis as it takes internal resources and time to source contra partners and manage the various relationships.

Corporate Trade is a more flexible and financially beneficial approach to contra. A Corporate Trade company acts as a financial and relationship facilitator between businesses so that one good does not need to be exchanged directly with another. Instead, a product can be exchanged for a variety of goods and services depending on business priorities.

There is also no requirement for change to existing relationships or processes. Corporate Trade is simply a different way of paying for goods and services; relationships with existing media partners remain the same, as does the quality and price of the media plan.

The type of assets with potential to be traded typically include (but not limited to):

- Unsold inventory
- Product returns that are eligible for re-sale
- Capital equipment
- Seasonal merchandise
- First-line product
- Gift cards

HOW THIS IS DONE: TRADE CREDITS

The common exchange currency used in Corporate Trade is called a trade credit

- In a typical transaction, the Corporate Trade company issues trade credits for receiving a product or service.
- For instance, a retailer receives trade credits in exchange for their excess stock which they can then spend on ways to drive more people into their stores, like media.
- There is a strong incentive to use Corporate Trade as the business receives significantly more trade credits than their asset is worth on the open market.
- Trade credits are combined with cash to pay for a product or service. The ratio of cash to credit usually ranges from 85% - 95% cash / 15% - 5% credit.

WHY YOU CAN PAY FOR MEDIA WITH TRADE CREDITS: TRADING PARTNERS

A trading partner is a term given to a business who has a special negotiated agreement with one or more Corporate Trade companies, and thus accepts trade credits as a form of payment for their services.

In Canada, the majority of trading partners are media owners who sell advertising space - radio stations, television networks, digital media properties, social networks, and more.

Why would a media owner accept trade credits as payment for advertising? To understand this, let's look at an example of how a trading partnership is built.

TRADING PARTNER EXAMPLE

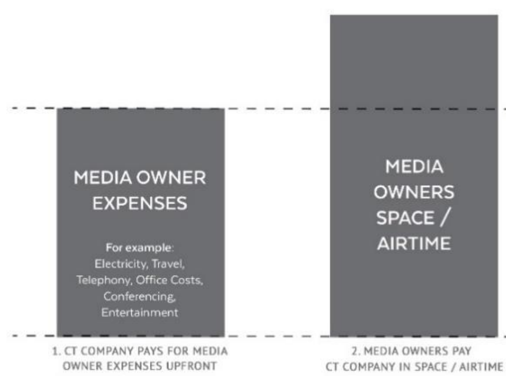
Below is an example of a trading partnership structure with a television network. Every trading partner structure is different and tailored to their business needs.

1. A Corporate Trade company makes an investment in the television network's business – for example, they may offer to pay their utility bill for a year.

2. In exchange, the network provides the Corporate Trade Company an agreed upon bank amount of media value that can be purchased with trade credits over time.

3. Anyone with trade credits can use them as currency to partially pay for media space on that television network.

4. Because the media space is purchased using a combination of cash and trade credits, the television network's cashflow is not majorly impacted. This combination of cash and trade



THE 2 MOST COMMON TRADE STRUCTURES

1. ASSET VALUE RESTORATION

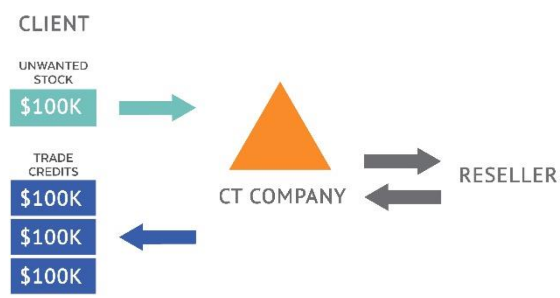
Restoring the value of a depreciating asset using trade credits

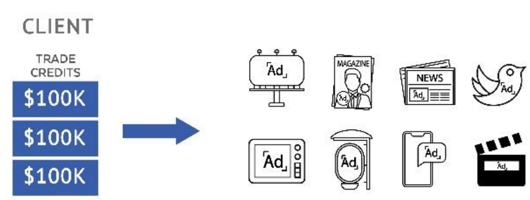
Suitable for businesses that:

- Have taken a write-down on obsolete inventory
- Want to avoid a potential write down on excess inventory
- Want to increase the return on their unsold inventory
- Have an expectation of at least $500k in media spend each year

How it works:

1. Your business identifies a depreciating asset, excess inventory for example
2. The Corporate Trade company, in collaboration with you, determines the current market value of that inventory, and any resale restrictions
3. The Corporate Trade company evaluates your annual media plan to determine the volume of trade credits relevant to your business *(this ensures that you will be able to spend those trade credits in a reasonable period)*
4. The Corporate Trade company makes an offer for your inventory that is typically x3 market value
5. You are paid for that inventory in trade credits, or a combination of cash and trade credits depending on your organization's ability to spend those trade credits *(as explained in point 3)*
6. The Corporate Trade company then sells your product to buyers that meet your resale restrictions *(the Corporate Trade company receives cash payment for that inventory, which is used to create trading partnerships with media owners)*
7. Over time, the Corporate Trade company works in a tripartite relationship with your business, and your media agency to use your trade credits as partial payment against your media costs





2. FIRST LINE PRODUCT PURCHASE

Generating incremental sales revenue without the use of trade credits

Suitable for companies that:

- Do not have a depreciating asset or excess inventory
- Want to attribute more ROI to their media investments
- Want to sell more first line product
- Have an expectation of at least $500k in media spend each year

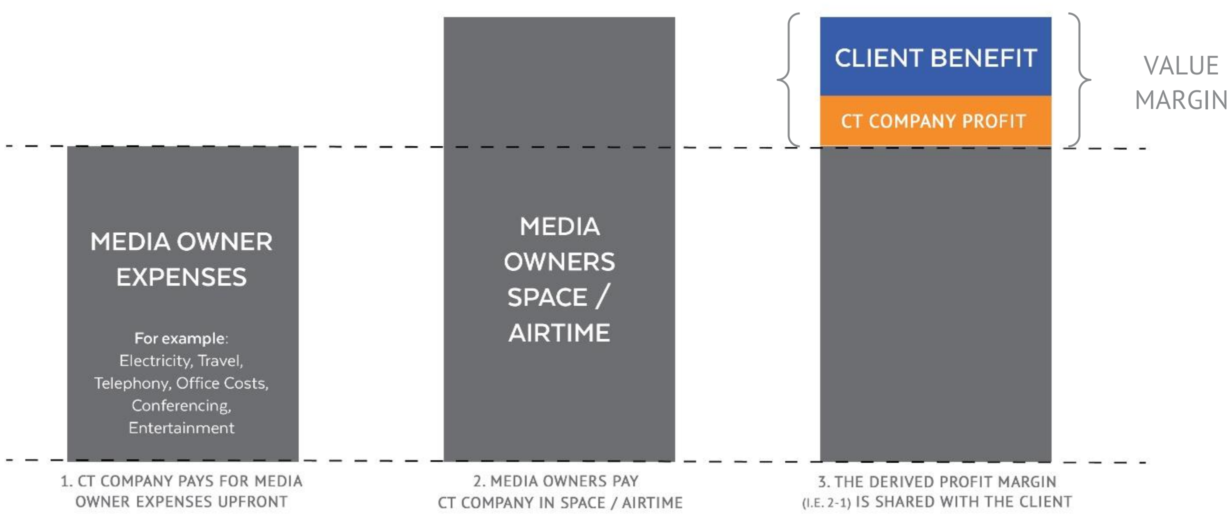
How it works:

1. The Corporate Trade company works with your media agency to identify and recommend media opportunities in your plan which they can trade
2. The Corporate Trade company purchases an agreed upon amount of your product – typically a % of the value of your media plan
3. Products purchased by the Corporate Trade company are sold to buyers that meet your re-sale restrictions *(for example, they can be traded with media owners in exchange for media space or sold through private networks)*

HOW DO CORPORATE TRADE COMPANIES GENERATE REVENUE?

When trading with media owners, the Corporate Trade company receives a higher value of media space in exchange for paying for a lesser value of their business expense.

The difference between these two amounts is the value margin. This value margin is then used to fund both the client benefit and the Corporate Trade company's profit. The shape of the client benefit will vary according to which Corporate Trade solution maximises the value to their business (as outlined on pages 5&6).



Asset Resale

When a client's asset is resold, the Corporate Trade company receives the cash proceeds from the resale of the asset.

Accounting rules state that a Corporate Trade company should only record the revenue from the resale of the asset as and when the trade credits are spent. Why does this matter? Corporate Trade companies have a vested interest in ensuring the timely and effective use of a client's trade credits.

ACCOUNTING FOR A CORPORATE TRADE TRANSACTION

1. ASSET VALUE RESTORATION

Restoring the value of a depreciating asset using trade credits

TREATMENT OF THE TRADE CREDITS: AS A MEDIA PREPAYMENT

This common treatment is to derecognize the asset/inventory in your accounts and recognize the invoice issued to the Corporate Trade company as turnover, with the book value of the asset/inventory being the cost of sale - giving a net impact on gross profit of zero.

The prepayment can then be dealt with in two ways:

1. If your accounting standards and/or policies do not allow for the inclusion of a media prepayment at the full value of the trade credits issued, the prepayment may be written down to the market value of the asset / inventory sold. The difference between the market value and the trade credit value (the value created) is then recognized in the profit and loss account as and when the trade credits are spent.
2. The prepayment is carried at full face value of the trade credits and this balance is reduced as the trade credits are spent. In this case the value created is recognized at the beginning.

BEST PRACTICE: IMPLEMENTING A CORPORATE TRADE PARTNERSHIP

Corporate Trade brings together different areas of the business in order to uncover value and efficiency. Communication and alignment between different teams is necessary to achieve optimal delivery.

1. Stakeholder alignment.
   Stakeholders will vary business to business, but typically those who will be impacted include CEO/CFO, finance, marketing, brand management, supply chain, procurement, and your media agency of record if one exists.
2. Asset / inventory evaluation.
   A Corporate Trade company will take the time to understand your asset or inventory to accurately assess its market value considering resale restrictions. This helps determine an accurate current market value, and its value in trade credits.
3. Media evaluation.
   A Corporate Trade company will need to understand a client's media plan before making a trade credit offer. This ensures that the agreement is right sized to their spending patterns and can use the trade credits in a reasonable time period.
4. Determine how the unlocked value will be applied to your business.
   To be successful, it is important to provide very clear communication about the process and the key benefit across departments. Will the marketing department receive an increased media budget, or cash savings against the current budget? Will the sales team receive a recovery on the loss of the inventory profit? Will it be used to generate cashflow for other initiatives like research & development? This will not only impact how finance accounts for the transaction but aligning all stakeholders behind the "why" is vital to ensure a smooth implementation.
5. Set a trade credit spending plan.
   Work in collaboration with your marketing team, media agency of record and the Corporate Trade company to align on common goals and expectations for trade credit spending.
6. Launch meeting.
   Direct accountability and a clear communication plan are imperative to a successful launch. Once an agreement has been signed and you're ready to go, your Corporate Trade partner should kick things off with a launch meeting. Successful launch meetings must include the wider stakeholder group and communicate the overarching goal of the partnership (see point 4), address key questions and provide clarity around process, roles, and expectations.
7. Quarterly reviews.
   Connect regularly with your Corporate Trade company to review and monitor progress against the trade credit spending plan and identify areas of opportunity. Assign clear responsibilities about who needs to be involved - typically finance and marketing.
8. Annual planning.
   An annual planning session where marketing strategies and media plans are shared serves to uncover new opportunity. This process most likely already happens between most marketing teams and their agency. Armed with insight around your key priorities and media strategy, Corporate Trade companies can proactively find and negotiate custom trading agreements with media partners that deliver impact and value against that plan.

IMPORTANT QUESTIONS TO ASK OF YOUR CORPORATE TRADE PARTNER

1. Is their advice independent? (i.e. Do they have an affiliation with a media agency holding company?)
2. A specific, timely plan to spend trade credits
3. If you are trading in an asset, ask for visibility and sign off to where product is sold
4. Do they have international / cross border flexibility?
5. Case studies and references from their current clients

Active International is a commercial innovation company with Corporate Trade at the heart of our business. We help businesses achieve more with the financial flexibility to innovate for tomorrow while driving results today. Established in 1984, we are the largest independent Corporate Trade company in the world, backed by a powerful global trading network, approximately 600 employees across 14 countries, and a media buying powerhouse of approximately $1.6 billion each year.

TO LEARN ABOUT THE ACTIVE DIFFERENCE:

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