

PROJECT FINANCE – A DETAILED ANALYSIS

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NEED FOR FINANCE

- Finance is life blood of any business organization.
- Organizations require finance to meet basic objectives:
- To set up, modernize, expand business activity i.e to acquire fixed assets for facilitating productive endeavor
- To meet the day-to-day working capital requirements i.e operating cycle
- To meet the former, long term finance is required and the latter, short term finance due to their inherent difference in life of assets.
- A portion of current assets is to be met through long term sources for having long term stability, liquidity etc in the event of exigencies.

What is Project Finance?

- Project finance is a long-term financing of any business venture including infrastructure and industrial projects based upon the projected cash flows of the project rather than appraising the financial statements of its stake holders/ sponsors.
- Project Finance is a process of evaluating and selecting long term investments that are consistent with the goal of shareholders (owners) wealth maximization.
- Project means any commercial or business venture.

PART 1

PREPARATION OF PROJECT REPORT

IMPORTANT ASPECTS

- It is an important document for seeking any type of financial assistance from financial institutions.
- Proper presentation and detailed analysis necessary.
- Imp. points that are necessarily to be incorporated in the project report:
 - a) Nature of Projects.
 - b) General Information.
 - c) Information about Promoters.
 - d) Technical details of the project.
 - e) Marketing & Selling arrangement.
 - f) Financial Feasibility.
 - g) Economic Benefits.

a) Nature of project

- New / Green Field Project
- Expansion /Modernisation of existing facilities at the same or different location
- Forward / Backward Integration
- Cost Reduction Project
- Diversification
- Debt Restructuring Schemes

b) General Information:

- First part of any project and gives general information about the project like:
- Name and complete postal address of registered office and location of the factory.
- Constitution: Proprietary or Partnership or Company.
- Nature of activity i.e. the type of products to be manufactured and its uses.
- Status: Whether small scale sector / medium / large / mega. Details of registration.
- Nature and amount of financial assistance required i.e. Term loan, working capital, non fund based limits.

c) About the Promoters:

- One of the most important part of the project report.
- Hence drafting of this part requires special attention and care.
- Complete family background along with individual bio-data.
- Past experience.
- Associate concerns & its performance.
- (Name/ nature/ turnover last 3 yrs, name of the banker & nature of facilities enjoyed.)

d) Technical details:

- **Capacity:** Available working days/shifts.
- **Manufacturing process:** covers the entire use of Machines proposed to be acq.
- **Location:** Feasible / irreversible one time decision
- **Raw materials:** Availability/ Indigenous / Imported.
- **Power requirement:** work out maximum demand
- **Man power requirement:** Tech. staff/ supervisors/ skilled/ unskilled/ semiskilled.
- **In case of multi products unit, product mix has to be ascertained.**

e) Market feasibility:

- Marketing aspect of the project:
- Whether the promoters can sell their goods in the market.
- Competition / Similar players in the line.
- Nature of product: Industrial / Consumer.
- Distribution system: Directly or through agency.
- Pricing: Competitive.
- (For large projects- demand supply gap)
- (For ancillary- Confirmation from Parent Co.)

f) Financial Feasibility:

- Determination of Cost of the Project
- Finalization of Sources of finance
- Profitability estimates.
- Cash Flow Statement
- Projected Balance sheet

i) Determination of the Cost of the Project

- Land
- Site Development
- Civil Construction / Bldg.
- Plant & Machinery
- Electric installation
- Other manufacturing assets like dies, moulds, cranes, etc
- Laboratory Equipments.
- Technical know-how fees,
- Other assets like furniture, equipments, etc
- Preliminary expenses
- Preoperative expenses
- Contingencies
- Margin of working capital.

ii) Sources of Finance:

- Equity / Quasi Equity.
- Term Loan (Fin. Institutions / Banks.
- State Incentives
- Deferred Payment Schemes
- Unsecured Loans & Deposits
- Internal Accruals (in case of existing units)

iii) Profitability Estimates

- Based on the technical parameters like capacity, raw materials requirement, power requirement, man power requirement and other item of expenditure like maintenance, consumption of stores, depreciation, adm. and selling Exps. Interest on term loan and working capital loan, profitability estimates at different capacity utilization.

iv) Cash Flow Statement

- Helps in ascertaining whether sufficient funds shall be available at different point of time to service the debts. Care has to be taken ensure that there is always long term surplus to meet short term requirements and not vice versa

v) Projected Balance Sheet:

- Helps in understanding the various financial parameters like D/E Ratio, Current Ratio and the composition of various assets & liabilities.

g) Economic Benefits:

- Whether helpful for development of ancillary units.
- Local manpower engaged.
- Foreign Exchange.
- Eco-Friendly.

In addition - the financial viability

- **Debt Service Coverage Ratio:**
$$\frac{\text{PAT} + \text{DEPRN} + \text{INTT ON T/L}}{\text{INTT ON T/L} + \text{INSTT.}}$$
- **Break Even Point**
- **Credit rating-** Marks awarded on different financial parameters.
- Higher comfort level in terms of Debt Equity Ratio, DSCR, Profitability Ratio, Collateral Security are rated high & offered lower rate of interest.

Role of CA's

- **Before Commencement of project.**
 - Assist in project identification.
 - Carrying out Technical, Commercial & Financial Feasibility Study.
 - Preparation of Detailed Project Report ("DPR")
 - Assisting in selecting optimal capital requirement / structure.
 - Arranging for finance & negotiations with the financiers.
 - Equity funding
 - Debt Funding
 - Negotiations with the vendors / contractors for the project.
- (Beneficiary: Borrower)

Role of CA's

- **Before Commencement of project.**
 - Independent appraisal of the project.
 - Vetting of DPR's
 - Carrying out TEV Studies of business ventures
 - Certification about net worth of the borrowers

(Beneficiary: Lender)

PART 2

DETAILS TO BE FURNISHED
WHILE SUBMITTING
APPLICATION FOR
FINANCIAL ASSISTANCE:

Along with the Project Report the following particulars to be submitted:

- Attested Photographs.
- Detailed Bio-data of Promoters / Directors.
- List of Associate companies.
- In case of existing company Audited Fin. Statements for last 3 years.
- Assets / Liabilities statements duly signed.
- If NRI, necessary permission from RBI.
- Copy of SSI Registration/
- Industrial License as applicable.
- Copy of various permissions, approvals & licenses from Govt., Local authorities as required.
- MPCB clearance for Red & Orange category industries.
- Copy of Sale Deed / Lease Deed.
- If unit is located at MIDC / SODCO or Govt. Ind. Estate, a copy of the allotment letter.
- Copy of the approved building plans.
- Copy of layout plans.
- Detailed estimates of the buildings to be constructed.
- Flowchart showing sequence for mfg. process.
- Quotations for the machinery proposed to be purchased.
- List of P & M.
- Raw material –Source, Tie up letters.

Checklist...

- Market survey reports.
- Market tie-up letters.
- Details of infrastructure availability. Viz.
 - Power
 - - Water
 - - Efficient Treatment
 - - Approach Roads.
 - - Labour Availability.
 - - Fuel Availability.
- Copies of I. Tax Returns & Personal Fin. Statements of Prop/ Partners / Directors for last 3 yrs.
- Arrangement made for W/c finance & its detail assessment.
- Detail of collateral security.
- Selling price evidence from customers.
- Copy of Collaboration / Tech. Know How/ Turnkey Agreement.

Checklist...

- If Partnership Firm:
- Copy of P/Deed.
- Reg. Certificate from Reg. of Firms.
- If Pvt. Ltd. Company:
- Memorandum of Association.
- Articles of Association.
- Company Incorporation Certificate from ROC
- Certificate of Commencement (in case of Public Co.) from ROC.
- If Co-op Society:
- Bye laws of the Society
- Associate Concern Details:
- Brief history / details of the concerns.
- Bankers name & address.
- Audited B/sheet & P& L A/c for last 3 years.
- Details of Fin. Assistance availed if any.

PART 3

PROJECT APPRAISAL

Project Appraisal

Project appraisal means the assessment of the viability of proposed long-term investments in terms of shareholder wealth & can be divided into 5 parts

1. Managerial Appraisal
2. Technical Appraisal
3. Market Feasibility
4. Economic Appraisal
5. Financial Viability

1. Managerial Appraisal

No Yardstick to Measure.

Some factors considered like:-

- i) Past track record.
- ii) Business experience (specially in the proposed activity)
- iii) Performance of the associate concern.
- iv) Bankers Report.
- v) Financial Resources.
- vi) Existing organizational setup & degree of professionalism.

2. Technical Appraisal

COVERS THE FOLLOWING ASPECTS

- i) Capacity
- ii) Product Mix
- iii) Manufacturing Process
- iv) Technical Know-how
- v) Raw Material
- vi) Requirement & Sources
- vii) Location & Site
- viii) Building
- ix) Plant & Machinery
- x) Manpower Requirement
- xi) Power Requirement
- xii) Other utilities
- xiii) Effluent disposal
Transport

3. Market Feasibility

- i) Products & its use
- ii) Demand projection & extent of competition
- iii) Adequacy of marketing infrastructure-
Distribution network
- iv) Demand-supply gap (specially in large projects)
- v) Whether ancillary unit or not
- vi) Industrial products or consumer products
- vii) Nature & status of the user industries

4. Economic Appraisal

-Specially for medium & large projects.

- i) Foreign exchange income & outgo
- ii) Employment of local people
- iii) Contribution to exchequer in terms of payment of duties & taxes
- iv) Exploitation of local resources
- v) Development of ancillary units
- vi) Impact on environment.

5. Financial Appraisal

- i) Determination of project cost.
- ii) Scheme of finance.
- iii) Appraisal of financial projections.

5 (i) Determination of project cost

-Investment in the following are considered in this head:

- i) Land & Site development
- ii) Building & Civil work
- iii) Plant & Machinery
- iv) Electric Installation
- v) Technical know-how fees
- vi) Other assets
- vii) Preliminary expenses
- viii) Preoperative expenses
- ix) Contingencies
- x) = **Capital cost (i to ix)**
- xi) Margin for working Capital
- xii) = **Total Cost (x+xi)**

5 (i) Determination of project cost

ESTIMATION OF TOTAL PROJECT COST IS VERY IMPORTANT AS THE SAME IS REQUIRED TO BE FUNDED **FROM LONG TERM SOURCES ONLY.**

5 (ii) Scheme of finance

- Various alternatives are available to the promoters to finance the project.
- According to the repayment capacity & projected profit generation by the unit, financial structuring is done.

Sources of finance

- i) Equity
- ii) Term loan
- iii) State incentives
- iv) Deferred payment scheme
- v) Unsecured loans & deposits
- vi) Internal accruals

Criteria applied to determine financial pattern

i) Debt Equity Norms

-Formula: Long term debt/Equity

-Normally accepted D/E ratio is between 2:1 to 1:1

-For mega project this ratio may be 3:1 to 4:1

ii) Margin concept- Margin on fixed assets

iii) Equity – Quasi Equity

iv) Promoters capacity to bring equity

Margin concepts

- In case of Bank Term Loans:
 - Land & Building: 30%
 - Plant & Machinery: 25%
 - 2nd Hand Machinery: 40%
 - Generally Banks there is apprehension about financing purchase cost of land.
 - Reimbursement of cost incurred, higher margins may be stipulated.
 - Generally cost incurred upto one year before are eligible for Bank finance

5 (iii) Appraisal of financial Projections

Net sales (Sales – Excise Duty / VAT)

(-) Cost of Production

= GROSS PROFIT (i-ii)

(-) Administrative Expenses , selling expenses

(-) Interest (on Term Loan, Working Capital / other loans)

= PROFIT BEFORE TAX (iii-(iv + v+ vi))

(-) Provision for income tax including MAT

= NET PROFIT AFTER TAX

Add Back:- Depreciation

= NET CASH ACCRUALS

(÷) Repayment of Term loans

= DSCR

RATIOS

- I) **PROFITABILITY RATIO**
 - i) Raw material to Sales – Imported : Indigenous
 - ii) Power to Sales
 - iii) Labour to Sales
 - iv) Gross profit to Sales
 - v) Net Profit to Sales
 - vi) Sensitivity Analysis (Very Important)

BREAK EVEN ANALYSIS

- $BEP = \text{Fixed Expenses} / (\text{Sales} - \text{Variable Exp})$
- Analyzing fixed & variable expenses is very important.
- Calculate at what capacity utilization, the unit achieve BEP.
- Whether unit can perform above BEP
- Higher the BEP as % of Capacity : Higher the risk
- Suggestion to convert fixed expenses in to variable expenses.

CASH FLOW ANALYSIS

Shows the movement of funds at different points of time indicating:

- i) Sources of funds (Long / Short Term)
- ii) Utilization of funds (Long / Short Term)
- iii) Net surplus (i-ii)

(+) Opening Balance

= Closing Balance

Ascertain whether long term sources are used for long term uses.

D.S.C.R

IV) Debt Service Coverage Ratio =

$$\frac{\text{PAT} + \text{DEP.} + \text{INT. ON TERM LOAN}}{\text{INT. ON TERM LOAN} + \text{INSTALLMENT OF T.L.}}$$

Normally Accepted - 2

Risky - < 1.5

More Comfortable - > 2

PAY BACK PERIOD

- **A statement to measure the time within which the initial investment in the project is recovered.**
- **Lower the payback period, higher the safety.**
- **It does not consider the time value of money at different period. This drawback can be met by discounting the future cash flow.**

NET PRESENT VALUE

NPV = Discounted Cash Inflows – Cash Outflows

- Consider the time value of money
- Useful for comparing the project giving different inflow at different times
- Future cash flow are discounted at the cost of capital (Opportunity Cost)

NPV ILLUSTRATION:-

	<u>Project X</u>		<u>Project Y</u>		<u>Project Z</u>	
<u>Investment Outlay</u>	1,00,000/-		1,00,000/-		1,00,000/-	
<u>Opportunity Cost</u>	10%		10%		10%	
<u>Cash Inflow</u>	<u>Gross</u>	<u>NPV</u>	<u>Gross</u>	<u>NPV</u>	<u>Gross</u>	<u>NPV</u>
Year 1	40000/-	36360/-	20000/-	18182/-	10000/-	9090/-
Year 2	40000/-	33040/-	30000/-	24780/-	20000/-	16520/-
Year 3	30000/-	22530/-	40000/-	30040/-	30000/-	22530/-
Year 4	<u>20000/-</u>	<u>13660/-</u>	<u>40000/-</u>	<u>27320/-</u>	<u>70000/-</u>	<u>47810/-</u>
<u>Total:</u>	<u>130000/-</u>	<u>105590/-</u>	<u>130000/-</u>	<u>100322/-</u>	<u>130000/-</u>	<u>95950/-</u>
NPV		+5590/-		+322/-		-4050/-

-Decision Rule: **Accept the project if NPV is positive.**

Internal rate of Return (IRR)

- IRR of a project is the discount rate which makes the NPV of inflow equal to NPV of outflow.
- It is useful for comparing the two alternative project.
- It pre-suppose the reinvestment of inflow at the IRR rate, which many times may not be easy.

CURRENT RATIO

- It is very useful for assessment of working capital loan
- Normally accepted ratio is 1.33
- It is calculated by dividing the current assets by current liabilities.
- Liability due within a period of one year is treated as current liability.

OBSERVATIONS :
MOVEMENT OF CURRENT
RATIO.

TABLE I

	PERIOD 1	PERIOD 2	PERIOD 3	PERIOD 4
Current Assets	1000	900	1200	1500
Current Liabilities	750	667	923	1095
Current Ratio	1.33	1.35	1.30	1.37

TABLE II

	PERIOD 1	PERIOD 2	PERIOD 3	PERIOD 4
Current Ratio	1.33	1.35 (Improves)	1.30 (Deteriorates)	1.37 (Improves)
NWC (CA – CL)	250	233 (Deteriorates)	277 (Improves)	405 (Improves)

TABLE III

	PERIOD 1	PERIOD 2	PERIOD 3	PERIOD 4
Bank Borrowings	500	500	575	725
Other C.L.	250	167	348	370
Total C.L.	750	667	923	1095
Total C.A.	1000	900	1200	1500
Bank Borrowing / TCA	50%	55.55%	47.92%	48.33%
Other C.L./ TCA	25%	18.55%	29%	24.67%
Current Ratio	1.33	1.35	1.30	1.37

TABLE IV

	PERIOD 1	PERIOD 2	PERIOD 3
Current Liab.	750	750	750
Current Assets			
Inventory	600	500	400
Receivables	250	400	550
Cash	150	100	50
Total Current Assets	1000	1000	1000
Current Ratio	1.33	1.33	1.33

TABLE V

	PERIOD 1	PERIOD 2	PERIOD 3
Break up Of Current Ratio			
Inventory / Current Liabilities	0.80	0.67	0.60
Receivables / Current Liabilities	0.33	0.46	0.60
Cash / Current Liabilities	0.20	0.20	0.13
Current Ratio (Total of Above)	1.33	1.33	1.33

Return on Investment (ROI)

ROI = Operating Profit/ Capital Employed.

- Operating Profit = Profit after Tax but before interest.
- Capital employed = Capital + Loan

ROI ratio is used to measure the firm's efficiency

Bank rate can be minimum expected ROI

PART 4

TERM LOANS

TERM LOAN STRUCTURE

- **YOURSELF**
- **THE PROJECT**
- **TYPE OF FUNDING**
- **SOURCES OF FUNDS**

TERM LOAN STRUCTURE

- **RESPONSIBILITY TO CLIENT**
- **RESPONSIBILITY TO BANKS**
- **RESPONSIBILITY TO PROFESSION**

TERM LOAN STRUCTURE - THE PROJECT

- **THE PROMOTERS AND THEIR EXPERIENCE**
- **PAST PERFORMANCE**
- **TECHNOLOGY & COST OF THE PROJECT**
- **MARKETABILITY**
- **HUMAN RESOURCE**
- **INFRASTRUCTURE, RAW MATERIALS, LOGISTICS**
- **EQUITY VS DEBT – OPTIONALLY CONVERTIBLE LOANS**
- **TAXATION BENEFITS – DEPRECIATION METHOD IN CASE OF MAT**
- **RISK AND MITIGATION**

TERM LOAN STRUCTURE - TYPE OF FUNDING

- **FOREIGN CURRENCY – FCNRB/ECB/ADR/GDR**
- **RUPEE FUNDS**
- **NON-FUND BASED – L/Cs/ BGs**

TERM LOAN STRUCTURE - SOURCES OF FUNDS

- **DEVELOPMENT BANKS & FINANCIAL INSTITUTIONS**
- **COMMERCIAL BANKS**
- **INTERNATIONAL AGENCIES**
- **INTERNATIONAL CAPITAL MARKET**
- **PARENT COMPANY EQUITY**
- **FOREIGN INSTITUTIONAL INVESTORS**
- **VENTURE CAPITAL FUNDING**
- **PRIVATE EQUITY**

TERM LOAN STRATEGIES

- **BEFORE AVAILMENT**
- **DURING AVAILMENT**
- **AFTER AVAILMENT**

TERM LOAN STRATEGIES- BEFORE AVAILMENT

- **EXHAUSTIVE DOCUMENTATION OF COST OF PROJECT**
- **TECHNO-ECONOMIC FEASIBILITY REPORT**
- **TAX BREAKS/SUBSIDIES/ SPECIAL RATES OF DEPRECIATION**
- **GET THE PROJECT APPRAISED**
- **APPLY TO 3-5 BANKS AT THE SAME TIME**
- **CONTINUOUS FOLLOW UP**
- **UNDERSTAND THE SANCTIONED TERMS WITH RESPECT TO:-**
 - **i. Rate of Interest**
 - **ii. Security & collateral**
 - **iii. Repayment schedule – ballooning**
 - **iv. Processing charges & Commitment charges**
 - **v. Prepayment charges**
 - **vi. Credit rating**
 - **vii. Special covenants**

TERM LOAN STRATEGIES- DURING AVAILMENT

- **COMPLETE SATISFACTION OF PRE-DISBURSEMENT CONDITIONS**
- **AVAILABILITY OF PROFORMA DOCUMENTATION**
- **STAMP DUTY/FRANKING VETTED BY BANKS ADVOCATE**
- **AVAILABILITY OF SIGNATORIES/GUARANTORS/COMMON SEAL**
- **AVAILABILITY OF KNOWLEDGEABLE PERSON IN BANK WHO IS CONVERSANT WITH BANK'S SOFTWARE**

TERM LOAN STRATEGIES- AFTER AVAILMENT

- **COMMENCEMENT OF REPAYMENT**
- **POSSIBILITY OF INCREASE IN FREQUENCY OF PAYMENTS**
- **PERIODIC RECONCILIATION**
- **INTEREST CHECKING**

Role of CA's

- During the implementation of the project
Periodic reports / certifications:
 - Work Progress.
 - Cost Incurred.
 - Sources of Finance used in the Project.
 - Act as Lender Independent Engineer.

(Beneficiaries: Borrowers / Lenders)

PART 5

WORKING CAPITAL **ASSESSMENT**

WORKING CAPITAL CYCLE

- Cash
- Raw Material
- Work in Progress
- Finished Goods
- Receivables

Bank Funding is available at every stage
(except of course cash)

ESTIMATES OF WORKING CAPITAL REQUIREMENT FOR SMALL UNITS

Sales for Month	50,000
Raw Material, power, wages, etc.	45,000
Surplus per month	5,000

Estimated Operating Cycle

Raw Material Holding	1 month
Semi Finished Goods	½ month
Finished Goods	½ month
Receivables	1 month
Total Working Capital Cycle	3 months

Working Capital Assessment

Borrowers having Turnover of < 5 crores.

- **Nayak Committee Norms**

- Working capital loan = Maximum 20% of the turnover
- Promoters contribution = Minimum 5% of the turnover.

Working Capital Assessment

Borrowers having Turnover of > 5 crores

Tandon Committee Norms

- **1st Method:**

- Calculate Working Capital Gap (Total CA – CL)

Finance available = Maximum 75% of the Working Capital Gap.

The balance to come out of long term funds.

- **2nd Method:**

- The borrower will provide for a minimum of 25% of total current assets out of long term funds. Credit for the current liabilities other than bank borrowings will be available & the balance will be financed.

ILLUSTRATION

Current Liabilities / Current Assets:

<u>Current Liabilities</u>		<u>Current Assets</u>	
Creditors for purchase	- 100	Raw materials	- 200
Other Current liabilities	- <u>50</u>	Stock in process	- 20
	150	Finished goods	- 90
Bank Borrowings	xxx	Receivables	- 50
		Other Current assets	- 10
	-----		-----
	150		370
	-----		-----

ILLUSTRATION

1st Method

Total C.A. - 370

Less:

C.L (other than Bank

Borrowings) - 150

W.C.G - 220

25% of W.C.G.

From L.T. Sources - 55

Maximum permissible

Bank Finance - 165

2nd Method

Total C.A. - 370

Less:

25% of above from

L.T.Sources - 92

Less: 278

C.L.(Other than Bank

Borrowings - 150

55

Maximum permissible

Bank Finance - 128

DRAWING POWER NOT ALLIGNED TO MPBF

Many times D/P is not aligned to MPBF due to various reasons:

- Margin Stipulations
- Amt of Current Assets other than Stock & Debtors.
- Sub Limits Stipulations
- No. of Days Stipulation.

- EXAMPLE:

- C.A. & C.L. Of the Company are :

- Creditors : 50 cr.

Current Assets:350 cr.

Stock : 140 cr.

Book Debts: 200 cr.

Other Current Assets: 10 cr.

- **Sanctioned Bank Limit : 210 cr.** (sub limits on Debtors Rs. 100 cr.)

- Margin Stipulation:

- Stock : 25 %

- Debtors : 35 % (upto 90 days)

DRAWING POWER NOT ALLIGNED TO MPBF

<u>MPBF</u>		<u>DRAWING POWER</u>	
Total C.A.	350.00	Stock (140-50)*75%	67.50
Less: C.L.	<u>50.00</u>	Debtors (200-20)*65%	100.00*
Net C.A.	300.00	<u>Total Drawing Power</u>	<u>167.50</u>
Less:		Since Sub limit on Debtors Rs 100 is less	
Margin on C.A.;	<u>87.50</u>	than available D/P Rs. 117.00	
<u>MPBF</u>	<u>212.50</u>		

*Present D/P Rs. 167.50 cr. Is much less than sanctioned limit 210.00 cr.

*The co. should approach the Bank to remove the stipulation of 90 days on Debtors & reduce margin on Debtors to 30%.

REWORKED DRAWING POWER

STOCK	67.50
DEBTORS	<u>140.00</u>
Total D/P	<u>207.50</u>

PART 6

ALTERNATE SOURCES OF WORKING CAPITAL FINANCE

ALTERNATE SOURCES OF FINANCE

- Factoring
- Forfaiting
- Securitization
- Bills Discounting
- Letter of Credit (LC)

FACTORING

Factoring is a financial transaction whereby a business sells its accounts receivable (i.e. invoices) to a third party (called a factor) at a discount in exchange for immediate money with which to finance continued business. Factoring differs from a bank loan in three main ways. First, the emphasis is on the value of the receivables (essentially a financial asset), [1][2] not the firm's credit worthiness. Secondly, factoring is not a loan – it is the purchase of a financial asset (the receivable). Finally, a bank loan involves two parties whereas factoring involves three

FORFAITING

In trade finance, forfaiting involves the purchasing of receivables from exporters. The forfaiter takes on all risks involved with the receivables. The forfaiting operation is a transaction-based operation (involving Exporters) involving the sale of one of the firm's transactions. Factoring is also a financial transaction involving the purchase of financial assets, but Factoring involves the sale any portion of a firm's Receivables.

SECURITIZATION

Securitization is the financial practice of pooling various types of contractual debt such as residential mortgages, commercial mortgages, auto loans or credit card debt obligations and selling said debt as bonds, pass-through securities, or Collateralized mortgage obligation (CMOs), to various investors. The principal and interest on the debt, underlying the security, is paid back to the various investors regularly. Securities backed by mortgage receivables are called mortgage-backed securities, while those backed by other types of receivables are asset-backed securities.

BILL DISCOUNTING

Under this particular type of lending, Bank takes the bill drawn by borrower on his (borrower's) customer and pay him or her immediately deducting some amount as discount/commission. The Bank then presents the Bill to the borrower's customer on the due date of the Bill and collect the total amount. If the bill is delayed, the borrower or his customer pay the Bank a pre-determined interest depending upon the terms of transaction.

LETTER OF CREDIT

A standard, commercial letter of credit (LC) is a document issued mostly by a financial institution, used primarily in trade finance, which usually provides an irrevocable payment undertaking. . Letters of credit are used primarily in international trade transactions of significant value, for deals between a supplier in one country and a customer in another. The parties to a letter of credit are usually a beneficiary who is to receive the money, the issuing bank of whom the applicant is a client, and the advising bank of whom the beneficiary is a client.

PART 7 - SWOT Analysis

- Strength
- Weakness
- Opportunity
- Threat

PART 8 - Other aspects

- Credit Rating by Institutions/Banks
- Impact of tax incentives declared by government.



THANK YOU

CA. JULFESH M SHAH

