

A WORTHWHILE REVIEW

Albert Lo • E-mail: pkfchina@pkf-hk.com

Consulting on financing is the core strength of the Corporate Finance Department - the theme is to expand the financing frontier. It is quite common that we have noticed corporations do not always find the importance of reviewing banking facilities and year after year they are perfunctorily renewed that may not exactly answer the call of need. In this issue we will have a snapshot introduction of the general banking facilities in the market, an attempt to arouse interest to facility review.

Dissecting the activities of a corporation, we will have 3 areas where banks are servicing clients to grow: procurement; operations and expansion; and sales.

Procurement

a. Import L/C Issuing/Finance

Procurement of goods through letter of credit (LC) is a common form of trade finance and out of which trust receipt (TR) is to provide a finance term after the client has taken possession of the imported goods. The period of TR is mostly in line with the turnover time of the client from taking possession of raw materials, storage, to production, shipment and ultimately collection of money from buyer (with or without credit term).

b. Invoice Financing

There are situations whereby a client does not need to open LC as in the case of a local supplier. With the same turnover time, easing cash flow remains an issue to be addressed. Bank will give a period of finance to client matching with the same turnover time as if it were a LC case. The finance period starts from the date the bank pays the supplier after the credit term, if any, to the buyer.

This is an area some companies may have overlooked that can be added to their financing mix.

c. Packing Credit

By utilizing an export LC a client has received, bank will finance a loan to the client that is a certain percentage (for instance 80%) of the value of the LC for it to procure and pay for production inputs for the order received. This facility together with LC opening cum trust receipt, and invoice financing provides the major source of fund for procurement.

d. L/C Transfer

This is a common practice for a trader to transfer an export LC to its supplier where the goods in

description is or partially the same. The transfer LC will state smaller quantities (for there may be more than one supplier), selected items of goods from the LC received, and an earlier delivery date, etc. for the trader to meet the requirements of the master LC.

Operations/expansion

a. Equipment Financing

The common term is “leasing” or “finance lease”, a kind of financing in 2 forms – lease and hire purchase, differing under the treatments of accounting and taxation for acquisition of equipment.

Clients may also have come across operating lease that is pure rental with maintenance provided and the risks of ownership resting with the owner. This is off balance sheet arrangement, ideal for companies that have tight control on capital investment and a popular sales tool provided by computer/telecommunication equipment suppliers.

b. Mortgage Loan

This form of financing applies to acquisition of property that is pledged to the financier for procuring a loan.

c. Term Loan

As the name implies, it's a loan for a specified period. Instead of equal repayments we can put in step-up schedule, meaning that the amount of repayment increases in a progressive manner to lessen the burden in the early period of the contract or interest payment only without principal repayment for an early period to achieve the same purpose.

d. Syndication Loan

This is a more complicated form of financing. There is a leading bank forming a syndicate for a number of participating banks to share the loan commitment. In arranging so, the loan size is usually a big amount compared with a bilateral loan, interest at a lower level, with risks shared by a number of banks.

e. Project Finance

The loan is for a particular purpose, say a project at hand, and the fixed assets, intellectual properties, patents, licences of the project would form part of the collateral to the financier - a single bank or a syndicate.

f. Secured/Unsecured Overdraft

It's a standby facility for the operational needs of a company. Traditionally it's approved on

condition of collateral. In the last few years, some banks are more receptive in accepting unsecured overdraft that is good news to SMEs and companies that have little collateral to offer or had collateral already pledged.

Sales

a. Export DC Negotiation/Collection

This is post-shipment financing that the export LC is negotiated for payment prior to settlement by the issuing bank for smoothing the cash flow of the client. It's similar to factoring which will be explained below.

b. Factoring

For sales on credit terms, a company can elect to raise a loan from the accounts receivable, getting cash right after delivery to buyer. The loan carries interest in the credit term period and when the buyer pays to a designated account opened with the financing bank, the loan will get cleared up.

Traditionally companies do not like factoring because it involves in some cases disclosure of the financing arrangements to the buyers and of the lengthy process in setting up the facility. We've seen lately some forward-looking banks have improved a great deal in smoothing the process of application, setting up the facility in a much faster pace and allowing non-disclosure to buyers of the factoring arrangement.

The above is a brief coverage of the general banking facilities without going into how they operate or comparing among them. It's by no means exhaustive and banking products are all the time improved to meet the changing needs in the market. Each product deserves a dedicated coverage.

Regarding consulting on financing, Corporate Finance Department is specialized in advising on product bundling (the desirable financing mix), structure (the form of financing, terms and conditions) and interest cost after fact finding with clients. If you are not satisfied with the banking facilities you have or feel there is room for improvement or do not know exactly where the pain is, you are most welcome to talk to us. We will charge a very low fee for review or even free depending on the complexity of the work. **PKF**