SHORT-TERM FINANCING

01.A manufacturing firm needs $85,000 to meet working capital requirement immediately for 3 months. It has the following alternatives:-

a. The company can use trade credit arrangement on terms of 3/15, net 45.
b. It can take a simple interest loan of $1,00,000 from Prime Bank @ 14% with 20% compensating balance requirement.
c. The company can also issue commercial paper with a face value of $ 1000 each sold at $950 having 1% flotation cost for 90 days.

You are required to calculate the cost of each specific source and then take a decision on which one will be preferred for the company.

02. Nita poultry firm needs TK. 80,000 to meet working capital requirements immediately. It has three alternative sources:-

a. The firm can buy Tk. 1,20,000 of materials on terms 3/30 net 90;
b. A bank will lend Tk. 1,00,000 at 13% interest with 20% compensating balance requirement.
c. A factor will buy firms accounts receivable of Tk. 1,00,000 per month and will advance at 12% per annum up to 80% of the face value. Average collection period is 30 days. The factor will charge 2% commission. It has been estimated that the factor service will save the firm's average administration cost Tk. 1,000 per month and 1% bad debt loss.

03. Megna Cement Ltd. needs to finance seasonal needs in inventory of a Tk. 10, 00,000. The funds are needed for six months and is consider the following alternatives:-

a. A terminal warehouse loan from a finance company of 15% annual rate of interest up to 80% face value of inventory. The ware house costs are Tk. 15,000 for six month period. The remaining funds requirements of Tk. 2, 00,000 will need to be finance forgoing some cash discount on accounts payable. The standard term purchase are 2/10 net 30. However company feels that it will pay on 40th day without any adverse effect.
b. A field warehouse loan from another finance company at 12% interest rate per annum. The advance up to 75% and field warehouse cost Tk. 25,000 for six months period. The remaining finance on cash discount basis as in alternative (a).
c. A flotation lien arrangement with another finance company with an effective interest rate 22.50%.

Which alternative method should be selected and why?

04. Apex footwear Ltd. wants to increase working capital by Tk. 1 crore. It has four alternatives sources:-

a. Credit purchase granted on terms of 3/20, net 60'
b. Borrowing from National Bank Limited at 15% interest per annum maintaining 12% compensating balance.
c. Issuing commercial paper at 12% p.a. flotation cost of 1%.
d. Issuing commercial paper of face value of Tk. 1, 08, 00,000 for 6 months. Cost of issue is Tk. 50,000 per issue.

Find out the effective interest rate of all the alternatives. Which alternative should be preferred by the company?

05. Que cement company limited has just expanded its activities for which it will soon need an additional working capital of Tk. 10,00,000. The company could identify three alternative sources:

a. The firm can buy Tk. 1,20,000 of materials on terms 3/25, net 75.
b. Bank loan could be taken Tk. 11,00,000 at 13% interest rate p.a., with 10% compensating balance requirement.
c. A factor will buy firms accounts receivable of Tk. 12,00,000 per month which average collection period is 30 days. The factor will advance up to 85% of the face value of the account receivables at 12% on an annual basis. The factor will charge 2% commission on account receivables purchased. It has been estimated that the factoring service will save tk. 25,000 per month consisting of the cost of credit administration and bad debt loss. Which method of financing should be selected?

06. Determine the effective annualized cost of financing for the following credit terms, assuming that discounts are not taken, accounts are paid at the end of the credit period and year has 365 days:-

Alternative	Credit terms
X	2/ 10, net 30
Y	10/ 30, net 60
Z	3/10, net 90

07.A company issues a 120 days commercial paper of face value of Tk. 1,000 at Tk. 975. The credit rating expenses are 0.5%of the size of issue, issuing and paying agent charges being 0.25% and stamp duty 0.5%. What is the cost of commercial paper?

08. A company needs Tk.8,00,000 to meet working capital requirement immediately. It has the following alternative sources:

i. The company can buy Tk.10,00,000 of raw-materials on terms of 3/30, net 90.
ii. A bank will lend Tk.10,00,000 at 13% interest with 20% compensating balance requirements are paid in advance.
iii. To issue commercial paper of Tk.10,00,000 of three month period and net sale value is 9,50,000.

09. Sameen and Saphin company ltd. wants Tk. 40,00,000 as working capital. Three following alternative modes of financing are available:

i. Forgo cash discount granted on a basis of 3/ 15, net 45 and pay on the final due date.
ii. Borrow Tk. 50,00,000 at 14% interest maintain 15% compensating balance, interest payment are made in advance.
iii. Issue Tk. 44,00,000 of six-month commercial paper to net 40,00,000.

Which alternative should the company select and why?

10. Beximco Ltd. has got Tk.60 lakh revolving credit agreement with IFIC bank at 10% interest rate per year and 1% commitment fee on the unused portion of the credit. The company utilized on an average 70% of the total commitment.

Required:

a) What is the expected annual cost of this credit arrangement?
b) What is the effective interest rate?
c) What will be the effective interest rate if the company utilized only 50% of the total commitment?

11. The credit terms for some alternatives are given below:

Alternative	**Credit terms**
X	**2/ 10, net 60**
Y	**3/ 15, net 80**

Z	**2/20, net 70**

Required:

a) Determine the cost of foregoing cash discount for each alternative.
b) The firm has another option to raise short term bank loan @ 13% interest. Should accept the firm the cash discount offer or not?
c) What would be the decision, if accounts payable are stretched by 30 days?

12. A company needs Tk.80,000 to meet working capital requirement immediately. It has the following alternative sources:

a) The company can buy Tk.1,00,000 of raw-materials on terms of 3/30, net 90.
b) A bank will lend Tk.1,00,000 at 13% interest with 20% compensating balance requirements.
c) A factor will buy company's account receivables (Tk.1,00,000 per month) and will advance at 12% p.a. up to 80% of the face value. Average collection period is 60 days. The factor will charge 2% commission. There has been estimate that the factor's service will save the company's A/R administration cost of Tk. 1000per month and bad debt loss of 1%.

Required: which alternative should the company choose?