

Renewal of CC Limit

Working capital cycle.

- * Cash→
- * Purchases →RM →
- * Processing→WIP→
- * Finished goods→
- * Sales→
- * Debtors→
- * Cash.

Factors determining the quantum of working capital.

- * Nature of business.
- * Size of business.
- * Production policy.
- * Length of production cycle.
- * Seasonal variations.
- * Stock turnover.
- * Credit policy.

Important Documents to be obtained.

- ❖ CC renewal application form.
- ❖ Previous year audited accounts, audit report, schedules etc.
- ❖ Note on financial performance of P.Y.
- ❖ Tax Audit report, Income computation &IT return copies of borrower, directors, partners, guarantors.
- ❖ Next year projected P&L, Balance Sheet, working notes/assumptions, expansion plans.
- ❖ Justification for enhanced limit.
- ❖ Company secretarial compliance certificate.
- ❖ Sales tax return copies for p.y.
- ❖ Copies of all relevant registration certificates, licenses etc.
- ❖ Statement of wealth of borrower & guarantors.
- ❖ Latest valuation report of property offered as collateral security.
- ❖ Proof of payment of all statutory dues.

Scrutiny of CC Renewal application

- ❖ Scrutinize the accounts of p.y. with special reference to growth in sales, profitability, break-even sales etc.
- ❖ Study the important ratios such as Current ratio, Acid test ratio, Debtors turnover ratio, stock turnover ratio etc.
- ❖ Work out Maximum permissible bank finance. (MPBF)
- ❖ Review Funds Flow statement for diversion of funds.
- ❖ Work out Drawing Power.
- ❖ Study stock statement submission behavior.
- ❖ Latest Insurance policy & adequacy of insurance cover.
- ❖ Inspection should be carried out.

- ❖ Note down queries / observations made by inspection team, Auditors etc.
- ❖ Credit summations in account, average utilization, Max. Utilization etc.
- ❖ Whether credit summations are commensurate with CC limit?
- ❖ Whether all statutory payments have been made?

Master Circular- Management of Advances.

- ❖ Important provisions contained in the Master circular issued by RBI to all UCBs pertaining to Working capital limits should also be referred.

MPBF

Tondon Committee 1st Method	Tondon Committee 2nd Method
❖ <u>Rs'000</u>	❖ <u>Rs'000</u>
❖ Current Assets 600	❖ Current Assets 600
❖ Less: Current Liabilities 200	❖ Less: Promoter's Con. @25 % 150
❖ -----	❖ -----
❖ Working capital gap 400	❖ Working capital gap 450
❖ Less: Promoter's Con. @25 % 100	❖ Less: Current Liabilities 200
❖ -----	❖ -----
❖ MPBF 300	❖ MPBF 250
❖ -----	❖ -----
	❖ Drawing Power 210

Drawing Power

<u>Rs.</u>	<u>Rs.</u>
♦ Stock 300000	♦ Debtors 200000
♦ Less: Creditors 30000	♦ Less: > 90 days 50000
♦ -----	♦ -----
♦ Paid Stock 270000	♦ Debtors < 90 days 150000
♦ Less: Margin @ 50 % 135000	♦ Less: Margin @ 50 % 75000
♦ -----	♦ -----
♦ Drawing power or Limit	♦ Drawing power or Limit
♦ Whichever is less 135000	♦ Whichever is less 75000
♦ -----	♦ -----

Management of receivables

Factors affecting the size of receivables:

- ❖ Type of Product.
- ❖ Type of Business.
- ❖ Terms of Trade.
- ❖ Working capital availability.
- ❖ Market segment.

Debtors Turnover Ratio

- ◆ Average debtors $\times 365$ divided by Sales = no. days credit period.
- ❖ It indicates average collection period.

Inventory Turnover Ratio

- ◆ Average inventory $\times 365$ divided by Material cost = average number of days for which stock is held.
- ❖ It indicates average holding period of stock.

Current Ratio

- ◆ Current assets divided by Current Liabilities
- ◆ Standard ratio= 2:1
- ❖ This ratio is concerned with the assessment of an organization's ability to meet its short-term obligations.

Acid Test Ratio

- ◆ Current Assets less Stock divided by Current Liabilities excluding Bank CC
- ◆ Norm: 1:1
- ❖ This ratio is also concerned with short-term liquidity.

Material Cost Ratio

- ◆ Material cost divided by Sales $\times 100$
- ❖ This ratio indicates Material cost visa-a-vis sales.

Debt Equity Ratio

- ◆ Total outside debt divided by Shareholder's funds.
- ❖ This ratio indicates relationship between external and internal long term financing.

Interest Coverage Ratio

- ◆ PBIT divided by Interest
- ◆ Norm: 2:1
- ❖ This ratio measures the safety available to Bank for recovery of interest.

Debt Service Coverage Ratio

- ◆ PAT + Interest + Depreciation divided by (Interest + Term loan installment)
- ◆ Norm: 2.5:1
- ❖ This ratio measures the safety available to Bank for recovery of interest & loan installment.

Documents to be obtained.

- ❖ Acknowledgement of debt.
- ❖ DP Note.
- ❖ Hypothecation bond.
- ❖ Guarantee bond.
- ❖ Letter of lien & set off.
- ❖ Letter of continuing security.
- ❖ Acceptance of terms & conditions of sanction.
- ❖ Board resolution in case of ltd. company.

If additional CC limit is sanctioned to the borrower.

- ❖ New documentation for additional cash credit limit & for existing cash credit limit, acknowledgement of debt & security bond should be taken. (In the said bond, dates & amount of all previous documents should be mentioned.)

Stamp duty on AODS

- ❖ Refer relevant circular.

Stamp duty on Hypothecation bond for TOD limit.

- ❖ The stamp duty to hypothecation bond for T.O.D. Sanctioned for the period of 90 days, is half of the stamp duty applicable. (Taking in to consideration all existing loans)

Stamp duty on Hypothecation bond

- ❖ 0.1% of Limit.
- ❖ Refer relevant circular for amendment if any.