RESOURCE MOBILISATION: A CASE STUDY IN MULTI-LATERAL FUNDING

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VARIOUS SOURCES OF FUNDS

- Grants
- Internally generated resources.
- Capital markets
- Debt – loan funds.

GRANTS

- Funding which does not look for direct financial returns – for economically viable projects.
- Usually spent on projects intended to improve quality of life.
- Sponsored mainly by government and non-profit making bodies.
- Limited availability

INTERNAL RESOURCES

- Surplus business income.
- Determining factors for employment of surplus :

  1. Cost of equity
  2. Cost of debt,
  3. Return on capital employed.
  4. Return to shareholders.

CAPITAL MARKETS

- Equity takes several forms.
- Private equity - capital contributed by one or several shareholders through a private agreement.
- Capital raised through a public offering of shares by a company
- Shares may be ordinary, preferential or debentures or in the form of loan capital.
- Borrowings through commercial paper like bonds

DEBT

- Debt comes in the form of loans repayable on certain specified conditions.
- These conditions vary widely .
- The basic conditions are rate of interest and repayment period.
- However there are a host of other conditions having a huge impact on the real financial value of the loan and which therefore affect the viability of the project.

COST OF CAPITAL

- Reserves and surpluses are a part of equity
- Equity is costlier than debt –opportunity cost & Risk .
- Normally debt is cheaper than equity due to less risk.
- A company with healthy profits may still like to resort to some debt – trading on equity.
- Decision depends on the Weighted Average Cost of Capital.

THE BEST OPTION

- Choice depends on the primary objectives.
- Non – financial goals ?
- Lack of financial muscle.
- Profit or efficient use of resources?
- Option depends on circumstances.

THE DEBT OPTION

- Cost of debt …..
- Risk perception of the financial institution – credit rating
- Internal Rate of Return
- Security
- Sectoral allocation.
- Default zone

LENDING INSTITUTIONS

- Commercial banks

  Custodian of individual & corporate deposits deployed as interest bearing loans. Spread in the source of profit.
- Financial institutions

  Obtain money from the public by issuing income earning bonds which are then used to finance debt requirements of various projects at profitable rate of interest for long term.

SOME FINANCIAL INSTITUTIONS

- IDBI-Industrial Development Bank of India
- IFCI- Industrial Finance Corporation of India .
- ICICI-Industrial Credit, Investment Corporation of India.
- IFC- International Finance Corporation
- ADB-Asian Development Bank
- IBRD-International Bank for Reconstruction and Development

MULTI –LATERAL INSTITUTIONS

- Financial institutions may be purely commercial or backed by governments (developmental).
- They may have the some sector focus: infrastructure or industry funding.
- Both raise money from the capital markets usually through bonds.
- The difference lies in the cost at which they raise funds - cheaper by developmental.
- Multi- lateral agencies like the World Bank are backed by member governments and carry very high credit rating –a virtual sovereign guarantee.
- They can command cheaper funds than private commercial bodies due to high credit rating..

ATTRACTIONS

- Institutions like ADB,IFC and IBRD have a low cost of borrowing hence can afford cheaper loans than purely commercial institutions.
- Since they are backed by governments committed to the stated mission focused on development of poorer countries they offer favourable terms and conditions for their loans.

CONSTRAINTS

- Currency risks are unpredictable over a long term period hence final liability hard to assess.
- Project implementation is subject to detailed periodic review not only in terms of performance but also in terms of the covenants and conditions of implementation.

CASE - STUDY

WAGONS PROCUREMENT

FOR

CONTAINER CORPORATION

OF INDIA

SCOPE OF THE PROJECT

- WB study revealed the lack of development in the transport sector for modern logistics requirements.
- Potential for growth enormous due to growth in international trade.
- CONCOR identified as nodal agency for developing containerization in India .
- The loan therefore was a transport sector infrastructure project for the WB.
- Holistic objective to not only fund the CONCOR asset acquisition , but also facilitate change in regulations and processes governing international trade.
- Initiate systematic cooperation between different organizations like railways, port authorities, Customs etc.

FEATURES

- Primary requirement was of a fleet of specialized wagons - flats.
- Second ,a hub container depot strategically located near Delhi.
- Detailed estimate of requirements and technical parameters spelt out.
- The loan of USD 94 million sanctioned for procurement of wagons and training and development of manpower in modern container logistics planning and management as well as technical assistance in planning the mega ICD and drawing up a long term strategic business plan.

STRUCTURE OF LOAN

- $ 94 million.
- Twenty year repayment period with moratorium of 5 years on repayment of principal.
- Project life 5 years.
- Interest – cost of borrowing +0.5 %(variable)
- Commitment charges – 0.75 % on unutilized amount.
- Biannual payment of interest and principal.

COVENANTS

- Procurement of wagons would be on International Bidding Terms prescribed by the World Bank.
- Adherence to pre –determined performance parameters both physical and financial included in the loan agreement.
- Submission of quarterly progress reports on prescribed proforma.
- Submission to biannual review mission by the World Bank for the duration of project implementation.
- Divestment of equity 5% to public as precursor to privatizing – can be problem for few Govts..

OTHER FEATURES

- Bilateral loan between World Bank and Container Corporation of India instead of through the Government of India.
- Direct interaction of the company with WB for negotiating and finalizing terms and conditions, as well as review of implementation.
- However because of a sovereign guarantee the company bound to pay an annual guarantee fee of 2.5%on the outstanding loan amount to GOI.

OUTCOME

- Plus points
- Compulsory performance review induced good discipline and accountability.
- Importance of monitoring the right performance parameters was established.
- Training and development covered the entire organization and provided invaluable exposure.

ADVANTAGEOUS TERMS

- Interest rate much lower than domestic market rates.
- Moratorium on principal payments for 5 years.
- Long term amortization.
- Reasonable pre-payment terms.

FRINGE BENEFITS

- Establishment of efficient monitoring mechanism :

  Wagon utilization,

  Equipment availability.

  Financial ratios
- Technical assistance from M/s Haskoning

WB BIDDING TERMS

- Global bids.
- Two packet system.
- Technical short list.

  Exhaustive process with transparent discussions with suppliers.
- Financial bids,detailed ,rigorous, no scope for ambiguity.No scope for negotiation.

SOME FINANCIAL ISSUES

- Financial bids- firm prices as on delivery to be quoted , with break-up of all charges ,transportation, insurance and all duties and levies .
- Option to quote in foreign currency for imported items with exchange rate applicable as on date of import.
- No clarification having financial implication permitted.

CONSEQUENCES

- Foreign bidders out priced.
- Lowest bidder did not enumerate excise duty, nor commit firm price,hence disqualified.
- Successful bidder did not take advantage of quoting in foreign currency for imports, and suffered great financial loss with subsequent hardship to the company.

CURRENCY IMPLICATIONS

- Common pool currency /single currency
- Basket of currencies

  33%–USD

  33%–Japanese Yen

  22%-European currencies

  10%-other currencies.
- Choice of allocation left to borrower mainly in consultation with WB
- Advantage was that Foreign Exchange risk was distributed.
- Interest was variable .

CURRENCY IMPLICATIONS contd.

- The WB offered a switch to single currency loan in 98-99.
- Interest rate linked to LIBOR-1-2%
- Lower interest rate to be evaluated against the valuation of the principal outstanding.
- In Concor’s case this was reducing in rupee terms.

CURRENT STATUS

- 1999-2000 onwards CONCOR started prepaying, first the Common Pool Loan, then the Single Currency Loan since USD was rapidly appreciating.
- The project was extended to FY2000 and then terminated.
- Delay in wagon deliveries led to the extension.
- But now CONCOR in a cash rich situation meant that it could self- finance its assets.
- Final draw down was only $53 million out of $94 m. rest was cancelled

CONCOR SELF SUFFICIENT

- FY 2004-05

  Revenues : Rs.2044 cr.

  Net profit : Rs. 440 cr.

- Net worth from Rs 98 cr.in ’93 to Rs.1800cr.approx.
- Estimated cash balance Rs.500cr.
- Now Zero- debt company.

THANK YOU