



# SNS College of Technology

Coimbatore - 35



**19BAE711 – Working Capital Management**

**Unit V - Working Capital Financing**



**Presented by**

**Dr.V.Prabakaran**  
*Design Thinker*



# Guest the topic



# TRADE CREDIT

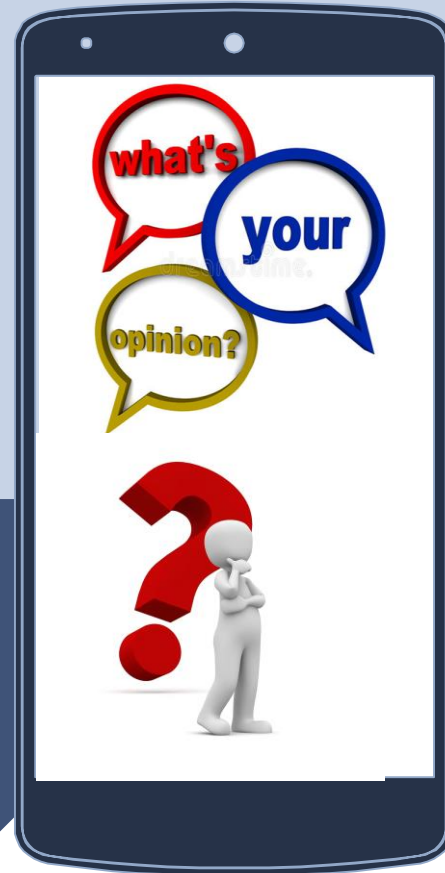




# Recall

- Forfeiting
- Characteristics
- Sources of Export Financing
- What Information Does a Forfeiter Need?
- Documents Required



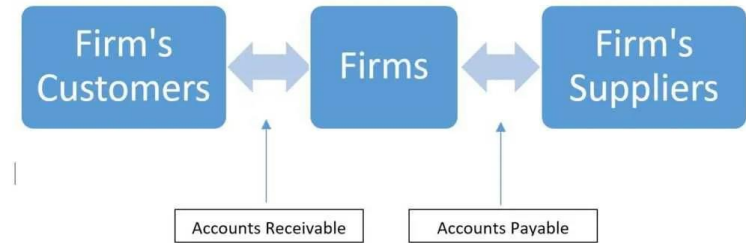


# What is Working Capital?



# Trade Credit

- A trade credit is an agreement or understanding between agents engaged in business with each other that allows the exchange of goods and services without any immediate exchange of money.
- When the seller of goods or services allows the buyer to pay for the goods or services at a later date, the seller is said to extend credit to the buyer.





# Benefits & Trade-Offs

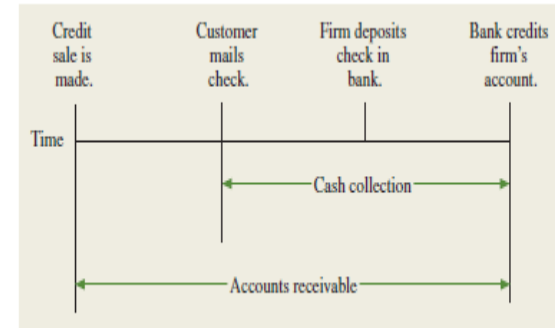
- From a borrower's perspective, using credit can enable expansion or development which may not be otherwise feasible if the company must pay for purchases immediately.
- A notable trade-off is that interest payments can accumulate and become overwhelming for borrowers (resulting in significant obligations which may compound).
- Providing credit allows convenience for the borrower (resulting in more transaction activity) and recurring interest income for the lender.
- Providing a borrower with credit has default risk associated with it, as a borrower may be unable to pay off the required debt obligations.



# Credit Period

Generally, a firm must consider three factors in setting a credit period:

- *The probability that the customer will not pay – A firm whose customers are in high-risk businesses may find itself offering restrictive credit terms.*
- *The size of the account – If the account is small, the credit period will be shorter. Small accounts are more costly to manage.*
- *The extent to which the goods are perishable – If the collateral values of the goods are low and cannot be sustained for long periods, less credit will be granted.*





# Credit Analysis

- Financial statements
- Credit reports on a customer's payment history with other firms
- Banks
- The customer's payment history with the firm
- The 5 C's of credit:
  - *Character – The customer's willingness to meet credit obligations*
  - *Capacity – The customer's ability to meet credit obligations out of operating cash flows*
  - *Capital – The customer's financial reserves*
  - *Collateral – A pledged asset in case of default*
  - *Conditions – General economic conditions*

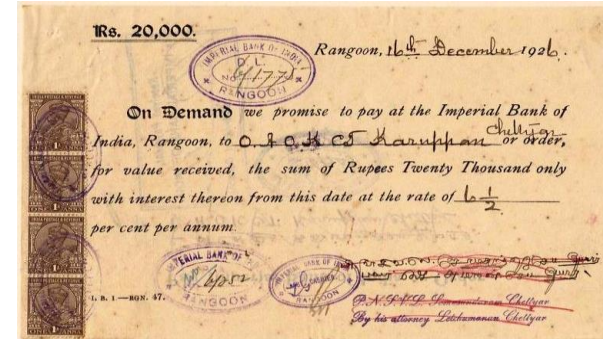






# Types Of Trade Credit

- Open Account
- Trade acceptance
- Promissory note



A Typical Trade Acceptance

TRADE ACCEPTANCE	Drawee	Payer
	Mytown, California	March 15 20 01
	To <u>Comfort Creations, Inc.</u>	
	On <u>June 15, 2001</u> PAY TO THE ORDER OF <u>Jackson River Fabrics</u>	
	<u>Fifty thousand and no/100</u> DOLLARS (\$ <u>50,000</u> )	
	The obligations of the acceptor hereof arise out of the purchase of goods from the drawer. The drawee may accept this bill payable at any bank or trust company in the United States which drawee may designate.	
	Accepted at <u>Blackacre, N.Y.</u> on <u>March 15</u> 20 <u>01</u>	
	Payable at <u>Bank of Blackacre</u> <u>Jackson River Fabrics</u>	
	<u>Blackacre, New York</u>	
	Buyer's Signature <u>Comfort Creations, Inc.</u> By <u>Joe Jones, Pres.</u>	
By Agent or Officer <u>Tom Smith, T.V. Pres.</u>		
Drawee-Acceptor	Drawer	

Chapter 19



# How to Calculate It?



- Early payment discount
- Late payment penalties



# Summary

- Trade Credit
- Benefits
- Credit Analysis
- Types of Trade Credit
- How to calculate?

SUMMARY





# Assessment

Character is one of the 5C's of Credit

**Ans: Yes**





# Reference

- <https://www.highradius.com/resources/Blog/what-is-trade-credit/>
- <https://cleartax.in/glossary/trade-credit/>
- <https://corporatefinanceinstitute.com/resources/accounting/what-is-trade-credit/>



# Reach Us



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*Thank  
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