TERM LOANS

Okay, here's a summary of the key topics from the PDF, with notes covering the details:

1. Term Loans

- Definition: Banks provide term loans for acquiring fixed assets (land, building, plant, machinery, infrastructure).
- Purpose: Unlike working capital loans (for current assets), term loans are for long-term assets.
- Working Capital Term Loan (WCTL): In some cases, banks provide term loans for current assets, known as WCTL, to address liquidity crunches.
- Repayment: Term loans are repaid according to a schedule, unlike working capital loans, which are payable on demand.
- Appraisal: Debt Service Coverage Ratio (DSCR) is important for term loans, while liquidity ratios are key for working capital loans.
- Repayment Schedule: Varies depending on the borrower's cash flow (e.g., EMI for salaried individuals, irregular for farmers, monthly/quarterly for industrial enterprises, or bullet repayment).

2. Deferred Payment Guarantees (DPG)

- Definition: A bank guarantee for a purchaser's payment to a supplier for fixed assets, paid over time.
- Nature: It's a non-fund-based method for financing fixed assets. If the purchaser defaults, it becomes a fund-based exposure for the bank.
- Risk and Appraisal: DPGs carry similar risks to term loans, so the appraisal process is the same.

3. Term Loan Appraisal vs. Project Appraisal

- Project Appraisal: Assesses all financial needs, including working capital.
- Term Loan Appraisal: For specific asset purchases, may involve a less detailed examination (e.g., focusing on DSCR for existing enterprises or individual loans).
- Basic Principles: The fundamental appraisal principles are the same for both.

4. Project Appraisal Steps

- Managerial Aspects: Assessing promoter credentials, financial stake, and organizational structure.

- Technical Appraisal: Evaluating location, production process, infrastructure, technology, construction details, waste disposal, raw materials, and marketing.
- Economic Appraisal: Analyzing return on investment (NPV, IRR, etc.), break-even point, and sensitivity to market changes.

5. Appraisal and Financing of Infrastructure Projects

- Definition of Infrastructure: As per the Ministry of Finance, including sectors like transport, energy, water & sanitation, communication, and social & commercial infrastructure.
- RBI Guidelines for Banks:
  - Types of Financing: Working capital finance, term loans, project loans, and investments in bonds/debentures/shares.
  - Take-out Financing: Arrangements with institutions like IDFC for transferring loan outstandings.
  - Inter-institutional Guarantees: Banks can issue guarantees if they have a funded share (at least 5%) and undertake due diligence.
  - Financing Promoter's Equity: Generally, banks shouldn't finance promoters' equity, but there are exceptions for infrastructure projects.
  - Appraisal: Due diligence on project viability, especially for government-owned entities, and assessment of individual financing components and returns.
  - Special Purpose Vehicles (SPVs): Infrastructure projects are often financed through SPVs, requiring specialized appraisal skills.
- Prudential Requirements:
  - Prudential Credit Exposure Limits: Higher limits for infrastructure projects.
  - Risk Weight for Capital Adequacy: Banks follow capital adequacy guidelines.
  - Asset-Liability Management: Banks must manage potential mismatches from long-term infrastructure financing.
  - Administrative Arrangements: Clear loan approval procedures and monitoring mechanisms are needed.
- Take-out Financing/Liquidity Support:

- Take-out Financing Arrangement: Mechanism to avoid asset-liability maturity mismatches.
- Liquidity Support from IDFC: IDFC commits to refinancing loans after a specific period.

- Partial Credit Enhancement (PCE) to Corporate Bonds:
  - Banks can provide PCE to enhance bond ratings for infrastructure projects.
  - PCE is currently offered as a non-funded irrevocable contingent line of credit.
- Financing of Cost Overruns:
  - International practice involves standby credit facilities for cost overruns.
  - Cost overruns are considered during the initial credit assessment.