Solution

His accountant and bank manager suggest:

factoring — the bank's factoring company will manage his debtors, lending him 80% of the £50,000 owing, thus releasing £40,000 which he can use in the business straightaway

commercial mortgage — the bank will lend him £40,000 for his new premises against a mortgage of the property; he will contribute the remaining £35,000

leasing — the bank's leasing company will buy the equipment he needs and lease it to him for a monthly rental

how much will it cost?

James will need to ensure that his business can afford these financial costs:

factoring

- an annual charge of 2% of the annual total of debts collected, here 2% x £350,000 = £7,000, plus
- interest on amounts borrowed, say an annual average of £40,000 at base rate (10%) + 4% = 14% = £5,600

commercial mortgage

- interest at Base Rate (10%) + 3% = 13%; the annual cost will be £40,000 x 13% = £5,200, plus any repayments
- arrangement fee 1.25% x £40,000 = £500
- security fee = £350

leasing

monthly rental payments to cover the financial cost of the lease, say twice the capital value of the assets (2 x £50,000) spread over 5 years (60 months):

$$\frac{£100,000}{60 \text{ months}} = £1,666 \text{ per month or } £20,000 \text{ per year}$$

other financial services

The bank manager also mentions a range of financial services which the bank can offer:

insurance — Will the premises, equipment and stock be adequately insured? Is James adequately insured – what protection exists if he dies or is disabled?

pensions — Does James have a suitable pension plan? As a self-employed man he is able to contribute to a plan and save tax.