

Chapter 17

Financing Current Assets

LEARNING OBJECTIVES

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After reading this chapter, students should be able to:

- Identify and distinguish among the three different current asset financing policies.
- Briefly explain the advantages and disadvantages of short-term financing.
- List the four major types of short-term funds.
- Distinguish between free and costly trade credit, calculate both the nominal and effective annual percentage costs of not taking discounts, given specific credit terms, and explain what stretching accounts payable is and how it reduces the cost of trade credit.
- Describe the importance of bank loans as a source of short-term financing and discuss some of the key features of bank loans.
- Calculate the effective interest rate for (1) simple interest, (2) discount interest, (3) add-on interest loans; and explain the effect of compensating balances on the effective cost of a loan.
- List some factors that should be considered when choosing a bank.
- Explain why large, financially strong corporations issue commercial paper, and why this source of short-term credit is typically less reliable than bank loans if the firm gets into financial difficulties.
- Define what a “secured” loan is and what type of collateral can be used to secure a loan.