Financial alternatives

Reputable organizations that operate parallel to the banking system are flourishing

• By JUAN DE LA ROCA

The banking system is the main supplier of finance in countries that have an organized financial system. But parallel to the banking system there are other institutions that cater to the financial needs of companies and individuals. Some of these are grey or even shady organizations that cater to the needs of those individuals and corporations that cannot receive credit from the banks.

But miles apart from loan sharks and other disreputable set-ups are corporate financial organizations that operate parallel to the banking system that are a respected and important element in the financial industry of any country. These are insurance companies, factoring companies and credit card companies.

In Israel, such institutions have been flourishing in the past two years, and with good reason.

The stringent regulations of the Bank of Israel which have been in force for more than a year do not allow clients to overdraw their current accounts beyond that which had been agreed beforehand. In the past the banks had very flexible rules, and corporate and private clients were allowed to overdraw their accounts.

This is no longer possible, thus many of those clients are meeting their financial needs through alternative finance companies. Insurance companies are an important source of finance primarily for the business sector. Insurance companies extend credit to the private sector but only in the form of mortgages.

Extra bank credit cards

Another source of alternative finance is credit card companies. Two years ago when the Bank of Israel decided to implement its current account policy, the three main credit card companies initiated what they called non-bank credit cards.

Hitherto credit cards had been issued only when guaranteed by the banks. The clients would request a credit card through the bank in which they conducted business. If the bank agreed, the credit card company issued the card and payment was guaranteed by the bank. This meant that the bank would include the credit card ceiling in the client's overall debit account.

MICHAEL AVNI
General Manager of Peninsula

The new system is completely different. Since the banks do not guarantee the credit card, it is not included in a client's overall commitments to the bank. This is an extra bank credit which supersedes the agreed credit arrangements with the bank. Clients can now avail themselves of extra credit arrangements. The three credit card groups – IsraCard, Visa and Leumi Card – introduced their new non-bank credit cards under different brand names. Leumi Card group called its new card Multi; IsraCard group called its card More; and the Visa group called it Cal.

The terms and conditions of the three companies are similar. Their interest rates differ for each client or group of clients, but they radiate around 10% per annum. The monthly repayment is about 5% of the outstanding credit but not less than NIS 200 to NIS 300.

The credit arrangements are at the discretion of the credit card companies but they are determined by the monthly income of the prospective client, as well as his/ her standing with the banks because one of the criteria is the authorized overdraft and the authorized credit ceiling of the bank credit card. And, of course, the credit history of the client.

Cal and More have a credit ceiling of NIS 45,000. The credit ceiling of the Multi is adapted to the client.

The credit arrangements of the Cal, More and Multi cards are oriented more toward the private user, although in some cases they are also used by small businesses. But the other alternative source of finance, the factoring companies, are oriented to the business sector.

Financing invoices

The factoring financial companies have existed for a long time, but it is only lately that they are really taking off. The reasons are similar to those of the extra banking credit cards. They constitute a ready source of credit for business organizations that may be temporarily strapped for cash because of the new overdraft regulations.

Michael Avni, the general manager of Peninsula, one of the four major factoring companies in Israel, says that in the past two years demand for their services has increased sharply. "In 2006 the overall turnover of the factoring companies amounted to some NIS 4 billion. This year we will probably have a turnover of more than NIS 5 billion."

A sharply growing industry indeed.

At present there are four large factoring companies in Israel: Clal Factoring; Peninsula Financial; Psagot Factoring; and Global.

The factoring financial institutions extend short-term credit because in essence they advance money on the strength of moneys they have to receive and are documented in invoices. If, say, a manufacturer of jeans delivers a consignment to a store worth NIS 50,000 for which he will receive payment in 180 days, the factoring company will advance the seller against the suitable documentation a sum of money that will amount to up to 60% of the value of the invoice. The borrower will then agree to instruct his client to make the payment directly to the factoring company. The factoring company will then reimburse them an amount equal to the amount of the invoice minus the loan, plus interest and fees.

Despite the fact that the cost of the credit from the factoring companies is more expensive than loans from the banking system, Avni explains that working through a factoring financial company has many advantages.

"We do not increase the client's liabilities to the banks and thereby allow the company full use of his credit facilities. We also take upon ourselves the risk element because if for any reason the buyer defaults, it would be the responsibility of the factoring company. The moment the factoring company agrees to accept payment for a certain invoice, which is also the collateral for the loan, then the responsibility for ensuring that the payment is made is transferred from the manufacturer to the financial company."

Another benefit is the level of finance against the invoices submitted. As experts in their field, factoring companies can analyze the credit value of invoices more efficiently than banks. Consequently, they are willing to extend larger credits for those same invoices than the banks.

Factoring companies can also finance expected payment from overseas customers, as well as advance payment to overseas suppliers. For example, a supplier in the UK may be in a tight money situation and is willing to give a 20% discount if the payment is made in cash. The factoring companies will also be willing to advance payment to the supplier provided the bill of lading for the goods is in their name because the equipment or goods will be sent to them and will serve as collateral for the loan.

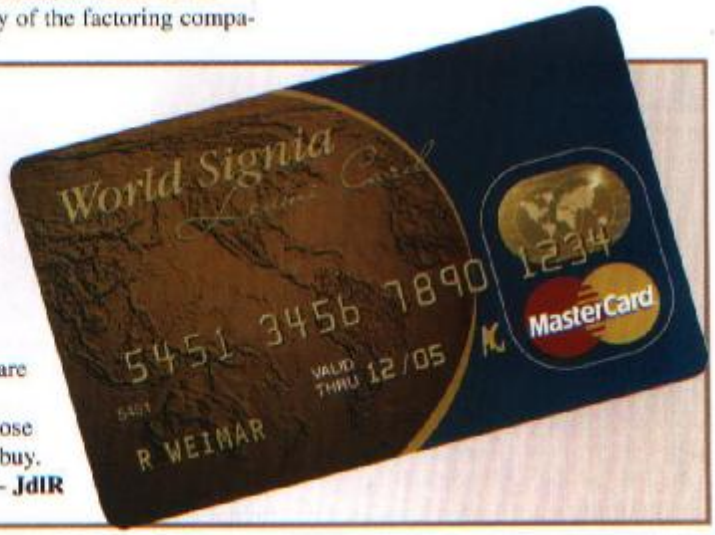
The factoring industry in Israel is expanding rapidly, but it still has a big way to go.

In the Western world, the turnover of factoring companies amounts to 2.5% of GDP. In Israel it is barely 0.20%. This means that in principle the industry can grow threefold. ■

Card-carrying convenience

An important status symbol among the affluent is the World Signia Credit Card. This cards allows the holder to make purchases of up to NIS 250,000 in Israel and $28,000 abroad.

Card holders enjoy a credit line of NIS 100,000. They can receive instant loans of up to NIS 50,000 bearing an interest rate of prime + 0.5. Card holders are automatically insured for the sum of $10 million.

They also receive additional services as befitting those who can afford the luxury and enjoy that money can buy.

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