Financial management of construction accounting

Questions:

You are advising a client who is highly respected in the industry as visionary and entrepreneurial. She is planning her next project, a mixed-use development (e. g. some residential units and two or three larger commercial buildings). This is to be just outside a large city near you, where infrastructure/transport links are established and ready for the growth.

She intends the commercial element to be attractive to large international businesses, perhaps as global or regional headquarters. The local authorities are supportive of the development on the basis that your client has agreed to work with them to also develop a new hospital as part of the project.

Write a letter of advice to the client outlining some options for funding the project, explaining why she should (or shouldn't) consider them as preferable. If appropriate, you may suggest a combination of approaches.

To:

Subject:

Project:

I appreciate the opportunity to advise you regarding the available option for funding your project. I look forward to assisting you with this project and achieving your project objectives.

I would like to draw your attention to the key financing options for the proposed project. It is important to remember that financing techniques/funding option constantly changed based on, for example, trends to equity participation by financiers as inflation of values occur, and also renewed interest in mortgages as property values fall. Therefore it is important to remember that a number of key decisions have to be made by those involved in arranging funding for this project.

The Interest rates are likely to be lower on corporate borrowing than on project-based funding, this is mainly due to the broader basis of the security available in this option. Borrowing can also be in the form of an overdraft, loan or mortgage on the other hand, or by the issue of securities, such as a debenture or loan stock. These stocks or bonds can be tradable on the stock market. They normally tend to have a fixed rate of interest and fixed term of maturity which can at times be beneficial if the rates are to rise in the future. Banks may offer funding that are fixed or floating rates of interest for a specified period of time.

The following facts are based on your written correspondence to me dated 12 th June 2016. It is worth considering the answers to the questions below.

1. What is to be the ratio of debt to equity in funding the project?
2. Is the finance to be project based or is it to be corporate finance?
3. What are the arrangements for refinancing the project?
4. Will the debt be funded by traded securities or will it be a loan?
5. What is the term of the loan or stock?
6. What will be the security for loan stock or loan?
7. Will a loan be fixed or floating rate?
8. What will be the term of the loan?

Other than that you have opportunity to deploy a consortium with a financial intuition. These are named asjoint venturesandsuch joint ventures arises when two or more parties act jointly to develop this mixed used development project. In these arrangements the participating institution will normally become the ultimate owner of the property. It is also worth noting here that joint ventures normally take the form of partnerships or joint venture (JV) companies.

Highlighted below are some of the advantages of such JV's;

- Secure adequate finance, particularly equity;
- Can be acquired expertise;
- Can be reduced risk of development;
- To enjoy off balance sheet financing, thereby reducing record debt;
- Meet the demands of foreign investors;

I hope my advice has been beneficial to you in making a decision for funding your next project. I look forward to working with you on this project. Please do not hesitate to contact me anytime if you have any questions or require further advice.

I look forward to hearing from you.

Kind Regards,

References

- Steven J. Peterson (2012). *Construction accounting and financial management* . 2nd ed. -: Pearson Education Inc.

- Danny Myers (2008). *Construction Economics a new approach* . 2nd ed. -: Taylor and Francis.