Business Update - Interest-ing Times

Information correct as at 14:00pm on 19.06.2020

- The premium on fixed over variable interest rates is exceptionally low at 0.3% and a good opportunity to mitigate future risk
- Transferring expensive short-term debt to longer term borrowing with capital repayments could be an opportunity to reduce your liabilities
- Understanding third party lenders and what the risks are

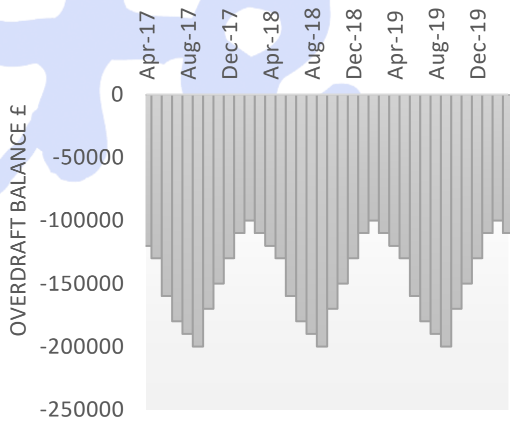
Interest Rates

As well as base rate being at an all-time low at 0.1%, the fixed interest rate premium is also exceptionally low at 0.3% where we would normally see it up between 1-1.5%. Recent indicative quotes for loans over 10 years have been 2.1-2.4% for variable rate interest and 2.4-2.7% for fixed rate interest.

This small differential makes fixed interest rates an attractive option to mitigate future risk exposure and guarantee low interest repayments, especially when considering the current base rate and the small extent to which variable rates could fall below the current level.

Reducing Overdrafts

With current interest rates being favourable and the availability of government lending schemes, businesses could consider transferring expensive short term borrowing such as overdrafts or short-term loans onto longer term loans with lower interest rates. The diagram shows the overdraft fluctuation of a farm that has £100,000 fully utilised on their overdraft, year after year. It is good practice for businesses to pay down their debt rather than leave it to sit as a liability on their balance sheet. The financial implications of this farm either leaving the £100,000 in the overdraft or transferring it to a 15-year loan and making capital repayments are detailed below:



Overdraft:		**Loan:**	
Recurring annual 1.5% Set up fee	£1,500	One-off setup fee of 1.5% is added to loan amount	£1,500
Base + 2.4% Interest	£2,500	15 years at 2.4% interest	£8,064
Total Annual Cost	£4,000 interest only*	**Total Annual Cost**	£8,064 interest and capital

*Assumes that interest rates stay at current levels for the entire 15-year period. If base rates increased to 3% the annual cost would be £5,400

The extra cost of putting this borrowing onto a loan is £4,064 per year or £339 per month. This capital repayment could be funded by a cost saving elsewhere in the business. For example, for 200 cows at 8500 litres a 0.24ppl cost saving would equate to £4,064 per year. If this farm were feeding 3 tonnes of concentrate per cow per year, this equates to £6.80 per tonne feed cost saving or a 0.014kg per litre feed rate reduction.

Transferring overdraft debt reduces a business' borrowings over time as well as stimulating operating cost savings or improved efficiencies elsewhere to support the capital repayments.

Third party lenders and Creditor Loans

Third party lenders offer schemes designed to structure repayments of large creditor debts onto short term loans. These can include cow loans or creditor loans where a business has a large bill for outstanding invoices. These agreements often have aggressive interest rates up to 10%, repayments structured over short time periods and heavy penalties can be incurred if businesses default on repayments.

We recommend any businesses considering taking out one of these loans should approach their high street lender first for any new loan arrangements and have a budget and business plan to ensure they can afford the repayments on any third party loan agreements.

For further discussion or to help with any questions that you may have, please contact Consultant Support on consultantsupport@kiteconsulting.com or 01902 851007 / 07542 403225