III- Long Term Finance

Song term finance is defined as money rose for a period in excess of five years. The long term finance is mostly used by the business concerns for the purchase of fixed assets, modernization and expansion of business. The main sources of long term finance are as follows.

Sources of long term finance

(i) **Equity shares.** The issuing of equity shares (ordinary shares) is the most important source for raising the long term capital by a company. These shares are the best source because they are only paid back on the winding up of the company. Equity shareholders are the real owners of the company. Equity shareholders get dividend get dividend when the company is earning profit. The company tries to raise maximum amount of capital through the sale of equity shares. A company can now issue different classes and kinds of shares to raise its owned capital. The kind of shares will be issued according to the needs of the company and the preferences of the investors.

(ii) **Issue of right shares.** A public company may increase its subscribed capital by issue of right shares. Right shares are offered to the shareholders in proportion to their present holding often at a price which is less than the currently quoted price o the stock exchange.

(iii) **Debentures.** A company also raises long term finance through borrowing. These loans are raised by the issue of debentures. Of debentures. A debenture is an instrument issued by a company to acknowledge the loan taken by the company under its common seal, under certain terms and conditions which are endorsed on the back of the document. The term of conditions are the rate of interest, the mode of payment of principal sum and interest, the security if any offered etc. A debenture holder is the creditor of the company.

Under the Islamic modes of financing the debentures are replaced by a new corporate security called TFC (Term Finance Certificates). TFC entitles its holder to share in the profits loss of the company instead of a fixed interest security for the loan.

(iv) **Loans from industrial and financial institutions.** A Company also meets its long and medium term capital requirements from the industrial and financial institutions like IDBP, PICIC, BEL, and NIT etc. Such financial institutions help in promoting new companies, expanding and development of existing companies, providing underwriting facility, provision of local and foreign currency for the purchase of machinery etc.

(v) **Leasing,** Leasing is now a popular method of long term finance. It is gradually gaining ground in developing and developed countries of the world. It is a contract for the hire of a specific asset. A business may get plant, equipment, land, vehicle etc on a long term hire purchase. The business in this way has the use of assets which is does not own. It has however, to pay regular payments to the lesser under the agreement.

The advantage claimed for leasing are:

i) There is no pressure on existing resources of the business. Its assets are also not tied u as security for loan.

ii) The rent is paid from income generated by the use of the asset.

(vi) Ploughing back of profits. Ploughing back profit means the use of profits of the business for its development. Ploughing back of profits is a useful source of getting extra capital for building and expansion of business. In ploughing back of profit, there is no problem of taking loans and no burden of interest on the business.